

NO. 44591-3-II

COURT OF APPEALS
OF THE STATE OF WASHINGTON
DIVISION II

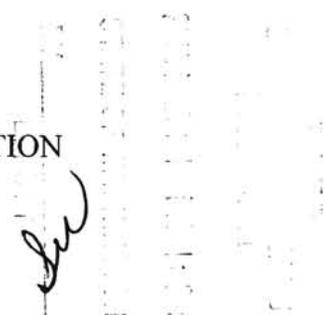
PACIFICORP d/b/a PACIFIC POWER & LIGHT COMPANY,

Appellant,

vs.

WASHINGTON UTILITIES AND TRANSPORTATION
COMMISSION, a Washington state agency,

Respondent.



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I. INTRODUCTION

The fundamental issue before the Court is whether the Washington Utilities and Transportation Commission (“Commission”) violated the prohibition on retroactive ratemaking and the filed rate doctrine in Orders 10 and 11, issued in Phase II of the general rate case that PacifiCorp d/b/a Pacific Power & Light Company (“PacifiCorp”) filed in May 2010 (Docket UE-100749).

This issue is a question of law. The prohibition on retroactive ratemaking and the filed rate doctrine are *statutory limitations* on the Commission’s authority.¹ As the dissent in Order 11 correctly recognized,² the majority acted illegally by reaching back into closed rate periods and ordering PacifiCorp to credit revenues from those past periods to future customers. In its response brief, the Commission attempts to justify its illegal actions by abandoning the majority’s rationale in Orders 10 and 11 and offering new rationalizations. But contrary to these new arguments, this case is not about the Commission’s discretion in setting utility rates or the various “tools” in the regulatory “tool bag.”³ No regulatory tool allows the Commission to ignore the statutory limitations on its authority.

¹ RCW 80.28.080 (prohibiting “greater or less or different” rates than filed rates); RCW 80.28.020 (the Commission may change rates prospectively by determining rates “to be thereafter observed and in force”); RCW 80.04.130(2)(d)(ii) (“The Commission may prescribe a different rate to be effective on the prospective date stated in its final order...if it concluded...that the originally filed and effective rate is unjust, unfair, or unreasonable.”); *see also* Clerks’ Papers (“CP”) 475-76, *In re Application of Puget Sound Energy for Authorization Regarding Deferral of Net Impact*, Docket No. UE-010410, Order at ¶ 7, WL 34797555 (Nov. 9, 2010) (“retroactive rate making...is illegal under the statutes of Washington State” (internal citation and quotation marks omitted)).

² Appendix (“App.”) 59 (Administrative Record (“AR”) 1793), Order 11 at ¶ 43.

³ Commission Br. at 21.

Order 06, issued in Phase I of PacifiCorp's 2010 general rate case, is an example of the proper exercise of ratemaking authority to establish new rates prospectively. Those new rates included an estimate of PacifiCorp's future annual revenues from the sale of renewable energy credits ("RECs").⁴ That estimate was based on PacifiCorp's actual REC revenues in the 2009 historical test year used in the rate case.⁵ Order 06 demonstrates the correct use of historical data to set prospective rates, and PacifiCorp did not appeal this order. The Commission's actions in Orders 10 and 11, however, demonstrate the opposite.

Orders 10 and 11 were issued in an unusual second phase of PacifiCorp's 2010 general rate case. The Commission initiated Phase II to consider a single element of PacifiCorp's rates—REC revenues.⁶ Instead of determining the appropriate rate treatment for REC revenues on a prospective basis only, the Commission went beyond its statutory authority and re-examined PacifiCorp's historical REC revenues over PacifiCorp's objection that revisiting these revenues violated multiple aspects of Washington law.⁷

In Orders 10 and 11, a majority of the Commission did exactly what the prohibition on retroactive ratemaking and the filed rate doctrine forbid—it plucked past revenues from closed rate periods and ordered

⁴ App. 18-19 (AR 845-46), Order 06 at ¶¶ 204-06.

⁵ App. 15 (AR 842), Order 06 at ¶¶ 195-96; *see also* App. 11-12 (AR 784-85), Order 06 at ¶¶ 13-16.

⁶ App. 20-22 (AR 1566-68), Order 10 at ¶¶ 1-7.

⁷ App. 20-42 (AR 1566-88), Order 10; App. 43-59 (AR 1777-93), Order 11.

PacifiCorp to credit these historical revenues to future customers, despite the fact that estimates of these revenues had already been credited to customers in previous final, binding rate orders.⁸ Orders 10 and 11 are unlawful and destabilize ratemaking in Washington to the detriment of utilities and their customers. Orders 10 and 11 must be set aside.⁹

II. ARGUMENT

A. The Prohibition on Retroactive Ratemaking and the Filed Rate Doctrine Bar the Commission's Actions in Orders 10 and 11

Orders 10 and 11 violate Washington law preserving the finality of filed rates by requiring PacifiCorp to pay approximately \$17 million in future rate credits based on past REC revenues. Despite the efforts by the Commission and intervenors to confuse and complicate this case, the law is clear, and its application here is unambiguous.

Recognizing the legislative nature of ratemaking, the filed rate doctrine provides that the “only legal rate is the filed rate”¹⁰ and “neither the courts nor the regulatory agency has the power to retroactively alter a properly filed rate.”¹¹ Instead, “once a rate is in place with ostensibly full legal effect and is not made provisional, it can then be changed only

⁸ App. 29 (AR 1575), Order 10 at ¶ 26; App. 45-56 (AR 1779-90) Order 11 at ¶¶ 5-34.

⁹ RCW 34.05.570(3) (this Court grants relief from agency orders if agency acted contrary to its statutory authority, contrary to law, or inconsistently with its rules).

¹⁰ Scott Hempling, *Regulating Public Utility Performance* at 304, 312 (ABA Section of Environment, Energy and Resources, 2013); see also *Puget Sound Navigation Co. v. Dep't of Pub. Works*, 157 Wash. 557, 561, 289 P. 1006 (1930), 160 Wash. 703, 295 P. 949 (1931) (en banc) (“[W]hen a rate is filed, published and permitted to become effective...it is...the only lawful rate[.]”).

¹¹ *Hardy v. Claircom Commc'n Group*, 86 Wn. App. 488, 493, 937 P.2d 1128 (1997).

prospectively.”¹² Whether the Commission specifically approved the filed rate in whole or in part is irrelevant: ““It is the filing of the tariffs, and not any affirmative approval or scrutiny by the agency that triggers the filed rate doctrine.””¹³

One of the purposes of the filed rate doctrine is “to ensure that a commission acts consistently with its own prior decisions.”¹⁴ In Orders 10 and 11, the Commission admitted that it issued an order in 2009 that approved rates with a specific estimate for REC revenues.¹⁵ The Commission also issued an order in 2008 that approved rates reflecting a settlement “of all contested issues in [the] proceeding.”¹⁶ It is undisputed that the underlying tariffs filed in that case reflected a revenue requirement including an estimate of REC revenues.¹⁷ Despite the binding, final 2008 and 2009 rate orders, the Commission in Orders 10 and 11 required PacifiCorp to credit additional REC revenues from the same periods covered by those orders. Orders 10 and 11 violate the filed rate doctrine.

¹² App. 26-27 (AR 1572-73), Order 10 at ¶ 20 n.17 (quoting *Columbia Gas Transmission Corp. v. Fed. Energy Reg. Comm’n*, 895 F.2d 791, 797 (D.C. Cir. 1990)).

¹³ Hempling, *Regulating Public Utility Performance* at 304 (quoting *Town of Norwood v. Fed. Energy Reg. Comm’n*, 202 F.3d 48, 419 (1st Cir. 2000)); see also, e.g., RCW 80.28.060; *Wash. Indep. Tel. Ass’n v. Wash. Utils. & Transp. Comm’n*, 148 Wn.2d 887, 893, 64 P.3d 606 (2003) (if Commission does not act on filed tariff, tariff becomes effective “and has the force and effect of state law”).

¹⁴ Hempling, *Regulating Public Utility Performance* at 322.

¹⁵ App. 29 (AR 1575), Order 10 at ¶ 26; App. 54 (AR 1788), at ¶ 27.

¹⁶ CP 86, 2008 GRC Stipulation at ¶ 28; CP 96-109, Order 05, Docket UE-080220.

¹⁷ AR 1639-42, Ex. RBD-4 at 3.5.1, Docket UE-080220; AR 1643-46, Ex. RBD-3 at 3.7, Docket UE-09025.

Orders 10 and 11 also violate the prohibition on retroactive ratemaking, which is “an outgrowth of the filed rate doctrine” that precludes a commission “from adjusting current rates to make up for over- or under-collections of costs in prior periods.”¹⁸ Thus, even though PacifiCorp’s actual REC revenues diverged from the estimates in rates, the Commission had no authority in Orders 10 and 11 “to adjust current rates to make up for past errors in projections” because such adjustments are illegal retroactive ratemaking.¹⁹

The gravity of the Commission’s legal error in Orders 10 and 11 is evident in the constitutional underpinnings of the prohibition on retroactive ratemaking:

The rule against retroactivity prevents ratemaking-by-ambush. Rates, like statutes, are prospective legislative acts. Prohibiting retroactivity aligns rates with legitimate expectations, thus satisfying the Constitution and making policies predictable. Look-backs are permissible, however, if preceded by notice.²⁰

¹⁸ Hempling, *Regulating Public Utility Performance* at 313 (internal quotation marks and citation omitted); see also, e.g., *Wash. Utils. & Transp. Comm’n v. Puget Sound Power & Light Co.*, Docket U-81-41, 6th Supp. Order, 99 P.U.R.4th 305, 315-16 (Dec. 19, 1988) (“retroactive ratemaking [is] surcharges or ordered refunds applied to rates which had previously been paid”); *Utility Reform Project v. Pub. Util. Comm’n of Or.*, __ Or. App. __, __ P.3d __, 2014 WL 767951 (Feb. 26, 2014) (“the rule against retroactive ratemaking...prohibits applying past profits or losses in determining future rates unless the legislature authorizes otherwise”).

¹⁹ CP 475, *In re Application of Puget Sound Energy for Authorization Regarding Deferral of the Net Impact*, Docket UE-010410, Order at ¶ 7, WL 34797555 (Nov. 9, 2010) (quoting *Town of Norwood, Mass. v. Fed. Energy Reg. Comm’n*, 53 F.3d 377, 381 (D.C. Cir. 1995)).

²⁰ Hempling, *Regulatory Public Utility Performance* at 337.

Washington courts have consistently adhered to these ratemaking laws and uniformly applied them, signaling an understanding that their equity “lies in [their] steady application regardless of what party is seeking to reexamine the past.”²¹ Similarly, the Commission has previously interpreted RCW 80.28.020 (prospective rates only) and 80.14.130 (the filed rate doctrine) to apply in all cases, instructing that retroactive ratemaking is “illegal under the statutes of Washington State[.]”²² In failing to adhere to these ratemaking laws in Orders 10 and 11, the Commission erred as a matter of law.

B. None of the Commission’s or Intervenors’ Arguments Overcomes the Illegality of Orders 10 and 11

In their response briefs, the Commission and intervenors offer different rationales to justify Orders 10 and 11, but none overcomes the illegality of reaching back into closed rate periods and ordering PacifiCorp to pay a rate credit for past revenues to future customers. Despite the Commission’s protests that Orders 10 and 11 are ordinary and proper rate orders, Orders 10 and 11 are unlike any past Commission orders because the majority disregards the filed rate doctrine and the prohibition against retroactive ratemaking. Under Washington law governing ordinary and proper ratemaking, Orders 10 and 11 must be set aside.

²¹ Hempling, *Regulatory Public Utility Performance* at 327 (quoting *Pub. Utils. Comm’n of Cal. v. Fed. Energy Reg. Comm’n*, 894 F.2d 1382, 1384 (D.C. Cir. 1990); see also, e.g., *Gen. Tel Co. v. Bothell*, 105 Wn.2d 579, 585, 716 P.2d 879 (1986) (“Once a utility’s tariff is filed and approved, it has the force and effect of law.”).

²² *Wash. Utils. & Transp. Comm’n v. Puget Sound Power & Light Co.*, Docket U-81-41, 6th Supp. Order, 99 P.U.R.4th 305, 315-16 (Dec. 19, 1988).

1. The Commission Cannot Salvage Orders 10 and 11 with New Arguments on Appeal

On appeal, the Commission's brief urges that Orders 10 and 11 are entitled to deference, claiming that the rate credit for PacifiCorp's historical REC revenues was consistent with "common ratemaking techniques."²³ In Orders 10 and 11, however, the majority took the position that PacifiCorp's historical REC revenues were "not part of the ratemaking process" even though estimates of those revenues were included in setting PacifiCorp's past filed rates.²⁴ Relying on that position, the majority claimed that the prohibition on retroactive ratemaking and the filed rate doctrine were "inapplicable" and "irrelevant" to the rate credit for PacifiCorp's historical REC revenues.²⁵

It is a "fundamental rule of administrative law" that "a reviewing court...must judge the propriety of [agency] action solely by the grounds invoked by the agency" in its order.²⁶ Because courts do not accept "*post hoc* rationalizations for agency action," the Commission cannot salvage Orders 10 and 11 with new arguments on appeal.²⁷ This is particularly true because the Commission's *post hoc* rationale directly conflicts with its

²³ Commission Br. at 17.

²⁴ App. 35 (AR 1581), Order 10 at ¶ 47.

²⁵ App. 29 (AR 1575), Order 10 at ¶ 26; App. 55 (AR 1789), Order 11 at ¶ 29.

²⁶ *Sec. & Exch. Comm'n v. Chenery Corp.*, 332 U.S. 194, 196 (1947); *see also Nw. Envtl. Def. Ctr. v. Bonneville Power Admin.*, 477 F.3d 668, 688 (9th Cir. 2007) ("we must look to [the agency's] reasoning in making its decision...and not to other reasons for its decision that [it] might marshal before us.").

²⁷ *Burlington Truck Lines, Inc. v. United States*, 371 U.S. 156, 168-169 (1962) ("The courts may not accept appellate counsel's *post hoc* rationalizations for agency action...an agency's discretionary order [must] be upheld, if at all, on the same basis articulated in the order by the agency itself.").

original rationale—the Commission’s actions cannot be an exercise of its normal ratemaking authority (as it now contends) if REC revenues are not part of normal ratemaking (which was the rationale in Orders 10 and 11).²⁸ The Commission’s new rationale—just like the majority’s original rationale—also fails as a matter of law.

2. Orders 10 and 11 Are Not a Lawful Exercise of Ratemaking Authority

In defending Orders 10 and 11, the Commission asserts that “[t]his 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.” In fact, as discussed above, this Court has long recognized that the Commission’s ratemaking authority is limited to setting rates only prospectively.²⁹ Orders 10 and 11 are not a lawful exercise of ratemaking authority. Just as this Court “does not defer to the Commission the power to determine the scope of its own authority,”³⁰ it does not defer to the Commission when it exercises its authority in an illegal manner.

In Order 06, the Commission used actual results from the historical 12-month test year (calendar year 2009), modified for known and measurable future changes, to set rates for the rate period beginning April

²⁸ See, e.g., *Assoc. Gas Distribs. v. Fed. Energy Reg. Comm’n*, 893 F.2d 349, 361 (D.C. Cir. 1989) (no deference is owed to commission when its findings and rationales are unclear, contradictory, or unsupported).

²⁹ *Hardy*, 86 Wn. App. at 493; see also, e.g., *Wishkah Boom Co. v. Greenwood Timber Co.*, 88 Wash. 568, 572-73, 153 P. 367 (1915) (“the establishment of a rate is the making of a rule for the future”).

³⁰ *U.S. West Commc’n, Inc. v. Wash. Utils. & Transp. Comm’n*, 134 Wn.2d 74, 86, 949 P.2d 1337 (1997).

2011.³¹ To determine the amount of REC revenues in rates, the Commission used actual revenues from the test year, adjusted for projected increased sales in the rate year, to set a REC revenue credit of \$4.8 million annually. This is how ratemaking is supposed to work, and the Company did not seek review of Order 06.

This appeal concerns what the Commission did next. After correctly using 2009 test-year data to set prospective rates in Order 06, the Commission returned to the 2009 rate year and illegally reopened it to take PacifiCorp's actual REC revenues from 2009 through early 2011 and fund a rate credit to future customers. Orders 10 and 11 demonstrate retroactive ratemaking at its most egregious: a rate credit or charge designed to recoup gains or losses from fully settled and closed rate periods. Because the Commission exercised its ratemaking authority in an illegal manner in Orders 10 and 11, Orders 10 and 11 must be set aside.

Citing cases from other jurisdictions, the Commission claims that the application of the prohibition on retroactive ratemaking is flexible and within the Commission's discretion.³² But the prohibition on retroactive ratemaking is not discretionary, and the cases cited by the Commission do not hold to the contrary. The decision in *Turpen v. Okla. Corp. Comm'n*³³ concerned a FCC-ordered reimbursement to ratepayers. The state commission determined that the prohibition on retroactive ratemaking did

³¹ App. 18 (AR 845), Order 06 at ¶ 204.

³² Commission Br. at 25-30.

³³ 769 P.2d 1309 (Okla. 1988).

not preclude the commission from ordering the utility to give the reimbursements to ratepayers because reimbursements had “nothing to do with mistakes in past ratemaking” but were an unexpected, one-time revenue item that was intended to go to ratepayers.³⁴ Similarly, the decision in *Narragansett Elec. Co. v. Burke*³⁵ involved the recovery of unexpected and exceptional storm damage costs. Unlike Orders 10 and 11, neither case involved adjustments to make up for imprecise cost or revenue estimates in past rates.³⁶

The other extra-jurisdictional cases that the Commission cites also do not support its position. The decision in *Wash. Gas Light Co. v. Pub. Serv. Comm'n*³⁷ involved an order *prospectively* changing an accounting treatment for gains on reacquisition of long-term debt. The commission expressly took care “not to indulge in retroactive ratemaking” and matched only unamortized gain in the test year to offset corresponding test-year debt costs.³⁸ In determining the order did not involve retroactive

³⁴ *Id.* at 1332-33.

³⁵ 415 A.2d 177 (R.I. 1980).

³⁶ In its response brief (at 28), the Commission also tries to distinguish the decision in *Citizens Utils. Co. v. Ill. Commerce Comm'n*, 124 Ill.2d 195, 529 N.E.2d 510 (Ill. 1988), that PacifiCorp cited in its opening brief (at 30). But the Commission does not dispute that the decision illustrates that a commission violates the prohibition on retroactive ratemaking by applying a new accounting treatment retroactively. *See Citizens Utils. Co.*, 124 Ill.2d at 211 (concluding same). Although the Commission argues that the decision involved only pre-test year expenses, the state commission in *Citizens Utils. Co.* properly matched test year expenses and revenues in setting the utility’s rates, and there was no retroactive ratemaking issue on those expenses. *See id.* at 215-16. In contrast, the Commission here reached back and ordered a rate credit for historical REC revenues incurred over 27 months from January 1, 2009 forward, after it had already used the 2009 test-year revenues as the basis for setting prospective rates.

³⁷ 450 A.2d 1187 (D.C. Cir. 1982).

³⁸ *Id.* at 1217-18.

ratemaking, the court explained that, irrespective of the accounting practice used, past repurchases of debt resulted in *present* gains that should be used to offset *present* debt costs, agreeing with the comparison that the order was no different than “charg[ing] present ratepayers for the current cost of debt securities issued in years past.”³⁹ The decision in *S. Union Gas Co. v. Texas R.R. Comm’n*⁴⁰ similarly does not help the Commission. That case involved an order determining the value of a tax credit in the test year to offset the cost of the property that produced it. The utility challenged the order as retroactive ratemaking because the tax credit was received in a prior year.⁴¹ The court disagreed because a statute specifically required sharing of utility tax credits with customers, and the commission incorporated only the prorated test-year amount.⁴² Neither the Commission nor intervenors identify any case in which a court approved reaching back into closed rate periods and applying a new accounting treatment to capture actual past revenues reflected in prior rates.

3. The Commission and Intervenors Cannot Circumvent the Prohibition on Retroactive Ratemaking and the Filed Rate Doctrine By Misstating PacifiCorp’s Brief and Distorting Historical Test-Year Conventions

The Commission’s brief claims that “PacifiCorp’s basic theory in this case is that in setting utility rates, it is illegal for the Commission to

³⁹ *Id.* at 1217-18.

⁴⁰ 701 S.W.2d 277 (Tex. Ct. App. 1985), *overruled on other grounds by Pub. Util. Comm’n v. GTE-Southwest*, 901 S.W.2d 401 (Tex. 1995).

⁴¹ *Id.*

⁴² *Id.*

use anything other than estimates of future costs.”⁴³ PacifiCorp has never taken that position. Instead, PacifiCorp argues that the Commission lacks authority to order a rate credit for REC revenues from past rate periods without proper notice, especially when estimates of REC revenues were included in PacifiCorp’s filed rates.⁴⁴ Rather than respond to these arguments, the Commission’s brief deflects them by misstating PacifiCorp’s position, making what is straightforward seem complex.

Under “long-established principles of utility ratemaking and historic Commission practices,” the Commission sets rates by determining “what levels of prudently incurred expenses the Company will experience *prospectively*.”⁴⁵ The Commission generally uses an historical test year as a starting point to determine future costs and revenues because a utility’s “cost, revenue...and other pertinent information are known and measurable” in that historical period.⁴⁶ In unusual cases, when there is a recoverable but non-recurring cost or revenue item in the test year, the Commission may allow recovery of that non-recurring item on a one-time basis, either all at once or spread out over several years.⁴⁷ Under either

⁴³ Commission Br. at 17.

⁴⁴ Opening Br. at 27-45.

⁴⁵ *Wash. Utils. & Transp. Comm’n v. Puget Sound Energy*, Docket Nos. UE-090704, UG-090705, Order 11 at ¶ 19, 281 P.U.R.4th 329 (April 2, 2010) (emphasis added); *see also* App. 10 (AR 783), Order 06 at ¶ 12 (“We must determine... the Company’s prudently-incurred expenses and allow recovery of those expenses prospectively in rates.”).

⁴⁶ App. 11 (AR 784), Order 06 at ¶ 13; *see* Commission Br. at 18 (acknowledging same).

⁴⁷ *See, e.g., Wash. Utils. & Transp. Comm’n v. Puget Sound Energy*, Docket U-85-53, 2d Supp. Order, 74 P.U.R.4th 536 (May 16, 1986) (allowing cost recovery over a five-year amortization period for non-recurring seismic study costs accrued in test period under FERC accounting rules; also allowing consideration of one-time gains on property sales that occurred during test period; rejecting “challenge that the rate-making, which is

approach, the Commission follows the “matching principle,” which requires costs and revenues to be matched from the same time period.⁴⁸

The Commission argues that PacifiCorp’s 2009 REC revenues were “at issue” as test-year revenues in this rate case.⁴⁹ But this argument supports only Order 06, not Orders 10 and 11. PacifiCorp’s 2009 test-year costs and revenues were “at issue” for estimating REC revenues for the future rate period, not for adjusting 2009 rates. And PacifiCorp’s 2010 REC revenues were not “at issue” at all because these revenues were outside the historical test year. The Commission’s brief also points to the treatment of non-recurring rate items in the historical test year as support for Orders 10 and 11.⁵⁰ Notably, the Commission’s Staff and Public Counsel made this same argument before the Commission in this case, and the majority declined to adopt it in Orders 10 and 11.⁵¹ Most basically, this rationale fails because—unlike the cost items that the Commission cites—REC revenues are a *recurring* revenue item.

In claiming that PacifiCorp’s historical REC revenues were subject to recovery as test-year revenues, the Commission relies on the *POWER*

prospective in nature, is retroactive”); *Wash. Utils. & Transp. Comm’n v. Avista Corp.*, Docket Nos. UE-991606, UG-991607, 3rd Supp. Order, 204 P.U.R.4th 1, 26-27 (Sept. 29, 2000) (disallowing storm expenses incurred before test period as an out-of-period, non-recurring cost, agreeing with Public Counsel’s, ICNU’s, and staff arguments that utility was required to file deferring accounting to recover storm costs).

⁴⁸ See App. 11-12 (AR 784-85), Order 06 at ¶¶ 13-16 (discussing same).

⁴⁹ Commission Br. at 24 (stating notice requirements satisfied because “all parties were on notice that REC revenues were at issue in this case”).

⁵⁰ Commission Br. at 35-36.

⁵¹ App. 35 (AR 1581), Order 10 at ¶ 47 (stating “no test period restriction” applied because “RECs are not part of ratemaking”).

case involving abandoned nuclear plant costs.⁵² The Commission asserts that the *POWER* case demonstrates that Washington has allowed recovery of actual, historical expenses in rates, even though such expenses do not represent “an estimate of the future level of such expenses.”⁵³ But, as noted above, PacifiCorp has never disputed the Commission’s authority to account for non-recurring items from test years in setting future rates. The key issue in *POWER*—whether and how to allow a large, one-time expense from the historical test year into rates—did not implicate the filed rate doctrine or prohibition on retroactive ratemaking.⁵⁴ In fact, because *POWER* did not involve reopening and restating past rate periods, there is no discussion of retroactive ratemaking or the filed rate doctrine in the majority’s opinion or the dissent.

The Commission’s brief also relies on a case in which another utility sought recovery of Y2K computer costs incurred the test year.⁵⁵ The Commission allowed recovery of these costs given their non-recurring nature and spread recovery over five years. Like *POWER*, this case is

⁵² *People’s Org. for Wash. Energy Res. v. Wash. Transp. Comm’n*, 104 Wn.2d 798, 711 P.2d 319 (1985) (“*POWER*”).

⁵³ Commission Br. at 19. In *POWER*, the utility realized the loss on the nuclear plant as a one-time expense item in the historical test year, so the entire amount of the loss was properly before the Commission. 104 Wn.2d at 802.

⁵⁴ *POWER*, 104 Wn.2d at 802-803.

⁵⁵ *Wash. Utils. & Transp. Comm’n v. Avista*, Dockets UE 991606, UG-991607, 3rd Supp. Order at ¶ 234, 204 P.U.R.4th 1 (Sept. 29, 2000) (allowing amortization of Y2K technology costs incurred in test period over a five-year period). At page 16 of its brief, Public Counsel (but not the Commission) points to a different part of the Avista case, where the Commission required Avista to reflect lump-sum revenues received from the buy-out of a contract in the test year. See *Avista*, 3rd Supp. Order at ¶¶ 19-28. Like the cases cited in the Commission’s brief, this case involved the proper rate treatment of a large, non-recurring item in the test year, not a true-up of past rates for actual results.

irrelevant to the prohibition on retroactive ratemaking because it does not involve reopening past rate periods to capture actual results.⁵⁶

Public Counsel also tries to defend Orders 10 and 11 by pointing to orders that are similarly off point. Public Counsel first cites an order permitting recovery of a utility's litigation settlement costs incurred in the test year.⁵⁷ In explaining why recovery of the settlement costs was lawful, the Commission explained “[r]etroactive ratemaking involves the *current* collection, through rates, of *past* obligations...[u]ntil [the utility] reached a settlement earlier this year, it had no obligation[.]”⁵⁸ Thus, like the orders discussed above, this order did not implicate the prohibition on retroactive ratemaking or the filed rate doctrine because the settlement costs accrued in the test period and were reflected in rates on a one-time basis.

Public Counsel also claims that “the Commission allowed PacifiCorp to recover \$2.9 million in past period pension gains” in PacifiCorp's 2009 general rate case stipulation.⁵⁹ Because PacifiCorp provided notice by seeking deferred accounting for those gains, that case does not support Orders 10 and 11.⁶⁰ Public Counsel also has the facts backwards: the stipulation gave customers the benefit of \$2.9 million in

⁵⁶ Additionally, because the utility sought and received costs for the non-recurring item in the 12-month test year only, this case highlights the unprecedented nature of the 27-month historical recovery period in Orders 10 and 11.

⁵⁷ *Wash. Utils. & Transp. Comm'n v. Avista*, Dockets UE-080416, UG-080417, Order 08, ¶ 78, 2008 WL 5432187 (Dec. 29, 2008); *see also* Public Counsel Br. at 27-28 (citing same).

⁵⁸ *Wash. Utils. & Transp. Comm'n v. Avista*, Dockets UE-080416, UG-080417, Order 08, ¶ 78, 2008 WL 5432187 (Dec. 29, 2008) (emphasis in original).

⁵⁹ Public Counsel Br. at 16.

⁶⁰ *Petition for Regulatory Accounting Order*, Docket UE-081997 (Nov. 4, 2008).

pension-related deferred income and precluded PacifiCorp from recovering its deferred costs.⁶¹

Finally, Public Counsel claims that “the REC sales proceeds in dispute are contemporaneous with other costs and revenues used to set PacifiCorp’s 2010 rates in this case.”⁶² This claim is false. PacifiCorp’s costs and revenues from the 2009 test year were properly matched in Order 06 for forecasting future costs and revenues in the rate period beginning in April 2011.⁶³ But Orders 10 and 11 reach back and capture more than two additional years of actual REC revenues without any offsetting costs. In fact, Orders 10 and 11 do not even address the fact that PacifiCorp’s actual net power costs for 2009 and 2010—the costs for the generating facilities that produced the RECs at issue—exceeded the net power costs in PacifiCorp’s rates by \$10.3 million.⁶⁴

4. No Ratemaking “Tool” Allows Violation of the Prohibition on Retroactive Ratemaking or the Filed Rate Doctrine

The two other ratemaking “tools” cited in the Commission’s brief—power cost adjustment tariffs and deferred accounting—also do not support Orders 10 and 11. The Commission implements power cost adjustment tariffs prospectively with advance notice to all parties.⁶⁵ These

⁶¹ *Wash. Utils. & Transp. Comm’n v. PacifiCorp*, Docket UE-090205, Order 09 at Attachment 1, ¶ 18, 2009 WL 4898823 (Dec. 16, 2009).

⁶² Public Counsel Br. at 17.

⁶³ See App. 11-12 (AR 784-85), Order 06 at ¶ 14-15 (discussing matching principle).

⁶⁴ AR 5203-04, Ex. ALK-2CT at 5-6.

⁶⁵ *Wash. Utils. & Transp. Comm’n v. Puget Sound Power and Light Co.*, Docket U-81-41, 6th Supp. Order, 99 P.U.R.4th 305, 316 (Dec. 19, 1988) (adjustment clauses are not retroactive ratemaking because such clauses involved a rate “to be applied only prospectively and only after hearing”); see also, e.g., *Town of Norwood*, 53 F.3d at 383

tariffs operate like the annual “true-up” adjustment for future REC revenues included in Order 06, which PacifiCorp has not challenged.⁶⁶ Similarly, an accounting deferral applies only prospectively from the petition date. For this reason, an accounting deferral “is not considered a violation of the prohibition on retroactive ratemaking, but instead is recognized as a shift in the timing of the collection of the expense.”⁶⁷

The Commission harmonizes adjustment tariffs and deferred accounting with its mandate under RCW 80.28.020 to set rates prospectively by strictly applying notice requirements and applying changes only prospectively from the date of notice.⁶⁸ There is no merit to the Commission’s claim that PacifiCorp’s position would impair the

(“Thus, it is permissible for a company to *defer* collection of certain charges until the point at which they become ascertainable, so long as the ratepayers have notice that the charges will be collected in the future. It is not, however, permissible for a company to devise a formula intended to *estimate* actual charges—to serve as a proxy for actual charges—and then go back and collect any shortfall caused by imperfections in that proxy.” (emphasis in original)).

⁶⁶ Public Counsel also points to cost-adjustment tariffs as a supposed example of the Commission taking a “flexible approach” to the prohibition on retroactive ratemaking. See Public Counsel Br. at 27. But, in the very order that Public Counsel cites, the Commission expressly rejected the notion that cost-adjustment tariffs implicated retroactive ratemaking, stating “the ‘true-up’ involves a rate which is to be applied only prospectively and not retroactive.” *Wash. Utils. & Transp. Comm’n v. Puget Sound Power and Light Co.*, Docket U-81-41, 6th Supp. Order, 99 P.U.R.4th 305, 316 (Dec. 19, 1988). Public Counsel identifies no order showing that the Commission has applied the prohibition on retroactive ratemaking with a “flexible approach” in past proceedings.

⁶⁷ *In re Petition of PacifiCorp for an Accounting Order*, Docket UE-020714, 3rd Supp. Order, ¶ 24, 2002 Wash. UTC LEXIS 364 (Sept. 27, 2002).

⁶⁸ See *In re Petition of PacifiCorp for an Accounting Order*, Docket UE-020417, 6th Supp. Order at ¶ 36, 226 P.U.R.4th 150, 157 (July 15, 2003) (allowing recovery of past costs incurred before filing of deferred accounting would “undeniably...violate the general prohibition against retroactive ratemaking and is thus not a legally sustainable result.”); see also Hempling, *Regulating Public Utility Performance* at 330-31 (discussing these exceptions and their operation).

Commission’s “tool bag” for regulating in the public interest.⁶⁹ The Commission is free to use various mechanisms in setting rates prospectively, as demonstrated by Order 06. But the Commission may not reach back and adjust costs or revenues from past closed rate periods without notice.

5. The Filed Rate Doctrine Protects Final Rates from Retroactive Adjustment, Even if Those Rates Were Adopted Through a Rate Settlement

To avoid the prohibition on retroactive ratemaking and the filed rate doctrine, the response briefs also claim that Orders 10 and 11 merely establish a prospective rate credit for PacifiCorp to return actual historical REC revenues that were not included in past closed rates.⁷⁰ To support that argument, the Commission’s brief claims that Orders 10 and 11 made a “finding” that PacifiCorp’s historical REC revenues were not included in its past rates, except for the amount explicitly identified in the 2009 rate case settlement.⁷¹ But the import of PacifiCorp’s filed tariffs in the 2008 and 2009 general rate cases and the Commission’s approval of all-issue settlements in those cases is a legal—not factual—question.

As noted above, the law is clear that “[i]t is the filing of the tariffs, and not any affirmative approval or scrutiny by the agency, that triggers

⁶⁹ See Commission Br. at 45 (arguing same).

⁷⁰ Commission Br. at 24 (asserting that 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 also ICNU Br. at 21 (making similar argument).

⁷¹ Commission Br. at 31.

the filed rate doctrine[.]”⁷² There is no dispute that PacifiCorp’s tariffs in its 2008 and 2009 general rate cases included its estimated REC revenues for the time period covered by Orders 10 and 11. Thus, because all components of filed tariffs become part of a utility’s rates unless changed by the Commission, PacifiCorp’s REC revenues were included in rates as a matter of law.⁷³

According to the response briefs, the Commission could determine that the “black box” settlements in the rate cases did not include REC revenues.⁷⁴ But rates set by the Commission’s approval of a rate settlement are subject to the filed rate doctrine, just like rates set by operation of law or by order after contested case proceedings.⁷⁵ The approved settlements for the rate cases specifically resolved all issues in the cases, which included REC revenues.⁷⁶ The Commission’s Staff, Public Counsel and ICNU also were all parties to the rate settlements.

⁷² Hempling, *Regulating Public Utility Performance* at 304.

⁷³ *Gen. Tel. Co.*, 105 Wn. 2d at 585 (“Once a utility’s tariff is filed and approved, it has the force and effect of law.”); see also *In re Application of PacifiCorp for an Accounting Order Regarding Excess Net Power Costs*, OPUC Docket UM 995 *et al.*, Order No. 02-469 at 7, 218 P.U.R.4th 465 (July 18, 2002) (“If a party does not propose a change in a particular item [in proposed rates], or if the Commission does not raise the issue, the item is adopted when the Commission issues its final order.” (internal quotation marks and citation omitted)).

⁷⁴ See, e.g., ICNU Br. at 25; Commission Br. at 31-32.

⁷⁵ See *Pub. Counsel v. Utils. & Transp. Comm’n*, 128 Wn. App. 81, 832, 116 P.3d 1064 (2005) (settlement “became the Commission’s order when the Commission approved it and issued its Rate Plan Order”).

⁷⁶ CP 86, 2008 GRC Stipulation at ¶ 28 (providing settlement resolved “all contested issues in [the] proceeding”); CP 96-109, Order 05, Docket UE-080220; CP 180-210, Order 09, Docket UE-090205; CP 123, 2009 GRC Stipulation at ¶ 22 (addressing RECs).

The Commission and ICNU additionally argue that the Commission's ability to regulate in the public interest would be impaired if the Commission lacked authority to revisit the rate treatment resolved through settlements.⁷⁷ But upholding the finality of rate settlements is not contrary to Washington public policy. Washington "law favors settlements, and consequently it must also favor their finality."⁷⁸ Respondents' arguments also misrepresent the nature of rate settlements. The Commission must determine the lawfulness of a proposed rate settlement before approving it, and the Commission may adopt rate settlements with or without conditions.⁷⁹ Under the Commission's rules, rate settlements are not precedential in future rate cases, but the filed rate doctrine still applies, and the Commission may adopt different ratemaking treatment prospectively only.⁸⁰

While ICNU and Public Counsel contest the preclusive effect of the rate settlements in this appeal, they clearly recognized that a rate settlement barred their ability to recover additional REC revenues when they filed a complaint to set aside the 2009 general rate case settlement in

⁷⁷ See ICNU Br. at 1 (arguing that requiring Commission to honor rate settlements "turns the regulatory compact on its head by subjecting the regulator to the decisions of the regulated" and "would bind the Commission to PacifiCorp's own ratemaking decisions"); Commission Br. at 45 ("it would prejudice the Commission's ability to address issues when they are actually presented for a Commission decision on the merits").

⁷⁸ *Haller v. Wallis*, 89 Wn.2d 539, 544, 573 P.2d 1302 (1978).

⁷⁹ WAC 480-07-740 (procedure for Commission's consideration and acceptance of proposed rate settlements); WAC 480-07-750 (Commission's authority to approve or reject proposed rate settlements).

⁸⁰ WAC 480-07-510(e)(i) ("Commission approval of a settlement does not constitute commission acceptance of any underlying methodology unless so specified in the order approving the settlement").

an attempt to capture 2010 actual REC revenues in rates.⁸¹ As a matter of law, the Commission ALJ dismissed ICNU and Public Counsel’s complaint on multiple grounds, including the fact that the “Commission cannot legally establish retroactive rates.”⁸² The ALJ explained that “the Commission cannot hold the Company to the bargain it made with all the parties in Docket UE-090205, reopen the matter to litigation and reduce the agreed revenue requirement, and enforce an order producing such a result.”⁸³ Orders 10 and 11 must be set aside because the Commission reopened the 2008 and 2009 settlements in the manner described as “legally unsustainable” by the ALJ.⁸⁴

C. No Exception to the Prohibition on Retroactive Ratemaking or Filed Rate Doctrine Applies in this Case.

Orders 10 and 11 also cannot be upheld based on any exception to the prohibition on retroactive ratemaking or the filed rate doctrine. PacifiCorp had no notice before Order 06 that the Commission would reopen PacifiCorp’s approved final rates and reconsider the ratemaking treatment of its historical REC revenues. In addition, although Public Counsel (but not the Commission or ICNU) urges this Court to uphold

⁸¹ App. 63-88, *Wash. State Atty. Gen. Office et al. v. PacifiCorp*, Docket UE-110070, ALJ Order 01, Initial Order Dismissing Complaint (April 27, 2011) (“ALJ Order”). The Notice of Finality issued under RCW 80.01.060(3) stated that the Commission does not endorse the reasoning and conclusions in allowing the ALJ Order to become final. *See* App. 88, Docket UE-110070, Notice of Finality (May 26, 2011).

⁸² App. 77, ALJ Order at ¶ 35.

⁸³ App. 82, ALJ Order at ¶ 46.

⁸⁴ App. 80, ALJ Order at ¶ 41 (stating that “ICNU and Public Counsel, in retrospect, apparently regret their decision to settle the REC issue on the terms to which they agreed” but no “legally sustainable” grounds existed for amending the settlement).

Orders 10 and 11 based on its rehashed misconduct allegations, the Commission in Orders 10 and 11 expressly declined to find that PacifiCorp engaged in any intentional misconduct. PacifiCorp also did not receive a “windfall” in its prior rate cases, and no “windfall” exception exists to the prohibition on retroactive ratemaking or the filed rate doctrine. Orders 10 and 11 are unlawful and must be set aside.

1. PacifiCorp Did Not Have Notice that the Commission Would Reopen Its Past Rates and Retroactively Treat REC Revenues as “Comparable” to Utility Property

The Commission and intervenors wrongly contend that PacifiCorp had sufficient notice before Order 06 that the Commission would reopen its approved final rates and retroactively change the ratemaking treatment of its historical REC revenues.⁸⁵ Courts—and the Commission itself in prior orders—have long recognized that, “when determining whether a [commission] order violates either the filed rate doctrine or the rule against retroactive ratemaking,” the critical inquiry is whether the party at issue “had sufficient notice that the approved rate was subject to change.”⁸⁶ As one court explained, “[i]t is not that notice relieves [a commission] of the bar on retroactive ratemaking, but that it changes what would be purely retroactive ratemaking into a functionally prospective

⁸⁵ Commission Br. at 43-49; ICNU Br. at 24-28; Public Counsel Br. at 41-46.

⁸⁶ *Pub. Utils. Comm’n of Cal. v. Fed. Energy Reg. Comm’n*, 988 F.2d 154, 164 (D.C. Cir. 1993); see also, e.g., *In re Petition of PacifiCorp for an Accounting Order*, Docket UE-020417, 6th Supp. Order at ¶ 36, 226 P.U.R.4th 150, 157 (July 15, 2003) (allowing recovery of past costs incurred before filing of deferred accounting petition “undeniably would violate the general prohibition against retroactive ratemaking and thus is not a legally sustainable result”).

process by placing the relevant audience on notice at the outset” that the rates may be subject to later revision.⁸⁷

For Orders 10 and 11 to be lawful, notice needed to be given to PacifiCorp as of January 1, 2009 (that is, the starting date of the recovery of historical REC revenues in Orders 10 and 11) that the amount of REC revenues reflected in its rates were provisional and subject to future adjustment. But the Commission and intervenors do not dispute that the Order 06—issued over two years later on March 25, 2011—was the first time that the Commission issued an order notifying PacifiCorp that it would revisit historical REC revenues. The Commission and intervenors also do not dispute that no party ever petitioned for deferred accounting of those revenues. Instead, the Commission and intervenors argue that it was “not reasonable” for PacifiCorp to rely on the inclusion of its historical REC revenues in its prior rates,⁸⁸ but they cite no authority supporting the view that the Commission may avoid its notice obligations to PacifiCorp. And no such authority exists.⁸⁹

⁸⁷ *Pub. Utils. Comm'n of Cal.*, 988 F.2d at 164 (internal quotation marks and citation omitted); see also Hempling, *Regulating Public Utility Performance* at 330-31 (quoting same and discussing notice).

⁸⁸ Commission Br. at 45; ICNU Br. at 25-28; Public Counsel Br. at 41-46.

⁸⁹ In addressing notice, the Commission again mischaracterizes PacifiCorp’s position, arguing that the Commission satisfied procedural due process requirements by providing a full hearing in Phase II. See Commission Br. 43-44. But PacifiCorp never argued that Phase II was procedurally inadequate. PacifiCorp argued—as the dissenting Commissioner in Order 11 recognized—that notice was required before the Commission applied a new accounting treatment and adjusted its past rates to recover its historical REC revenues. See App. 59 (AR 1793), Order 11 at ¶ 44.

In their response briefs, the Commission and intervenors insist that PacifiCorp should have anticipated that the Commission would determine to treat RECs as “comparable” to utility property.⁹⁰ But, as the Commission in Order 10 expressly observed, *all* parties were operating from the premise that “REC sale proceeds are...‘revenues’ to be factored into the ratemaking process” before Order 10.⁹¹ The Commission itself now argues on appeal that Orders 10 and 11 are ratemaking orders. And, although the response briefs try to make much of Oregon’s treatment of RECs as property,⁹² Oregon adopted this approach prospectively (like Order 06), not retroactively (like Orders 10 and 11).⁹³

Public Counsel and ICNU also imply that other utilities sought express regulatory approval for treatment of REC revenues, suggesting that PacifiCorp acted in bad faith for not doing so.⁹⁴ But intervenors’ attempt to impute bad faith to PacifiCorp is disingenuous. Contrary to ICNU’s representation,⁹⁵ Puget Sound Energy, Inc. (“PSE”) filed a deferred accounting petition because PSE sought keep a portion of its REC revenues instead of crediting them to customers.⁹⁶ In objecting to

⁹⁰ Commission Br. at 45; ICNU Br. at 27-28; Public Counsel Br. at 46-47.

⁹¹ App. 28 (AR 1574), Order 10 at ¶ 25.

⁹² ICNU Br. at 27; Commission Br. at 40-41.

⁹³ *In re PacifiCorp Application Requesting Approval of Sale of Renewable Energy Credits*, OPUC Docket UP 260, Order No. 10-210, 2010 WL 2406405 (June 9, 2010).

⁹⁴ ICNU Br. at 25-27; Public Counsel Br. at 7-8.

⁹⁵ See ICNU Br. at 26 (stating PSE filed deferred accounting so “the *actual* revenue it received from REC sales would be used to benefit its customers” (emphasis in original)).

⁹⁶ See CP 374-76, *In re Amended Petition of Puget Sound Energy, Inc. for an Order Authorizing the Use of Proceeds*, Docket UE-070725, Order 03 at ¶¶ 6-12, 282 P.U.R.4th 303 (May 20, 2010) (discussing same).

PSE's proposal, Public Counsel pointed to the treatment of PacifiCorp's RECs as operating revenues as the correct ratemaking approach.⁹⁷ PacifiCorp also had no notice that its ratemaking treatment was improper from the PSE case, which made no determination that RECs were properly treated as utility property. In fact, Order 06 expressly stated that the Commission had not yet determined "the precise rate treatment" to be given to REC revenues.⁹⁸ The PSE order also was not final until October 2010, and it described the factual circumstances in the case as "unique and non-recurring."⁹⁹

For the first time, Public Counsel and ICNU additionally argue that "[t]he 2009 Settlement Order effectively put PacifiCorp on notice and opened the door, by design, to potential recovery in a later case of PacifiCorp REC proceeds that might come to light under the agreed reporting provisions."¹⁰⁰ But the terms of the 2009 rate settlement expressly "opened the door" only for parties to request the Commission to authorize deferred accounting or some similar action, stating only

⁹⁷ AR 5644, *In re Amended Petition of Puget Sound Energy, Inc. for an Order Authorizing the Use of Proceeds*, Docket UE-070725, Public Counsel Br. (Redacted Version) at ¶ 19 (March 17, 2010) ("In the latest PacifiCorp general rate case, this Commission approved an all-party settlement that recognized an offset to PacifiCorp's revenue requirement representing Washington-allocated REC sales proceeds.").

⁹⁸ App. 17 (AR 844), Order 6 at ¶ 201; App. 24 (AR 1570), Order 10 at ¶ 14 ("we address the nature and distribution of PacifiCorp's REC sale proceeds for the first time in this proceeding").

⁹⁹ CP 390, *In re Amended Petition of Puget Sound Energy, Inc. for an Order Authorizing the Use of Proceeds*, Docket UE-070725, Order 03 at n.56, 282 P.U.R.4th 303 (May 20, 2010).

¹⁰⁰ Public Counsel Br. at 42; *see also* ICNU Br. at 25 (arguing "2009 settlement put all parties on notice, including PacifiCorp, that the Commission could reexamine the Company's REC revenues at a later date").

“[n]othing 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.”¹⁰¹ To argue now that the settlement made such a filing unnecessary turns the language of the settlement on its head. The 2009 rate settlement preserved the parties’ existing rights related to REC revenues, but explicitly did not “expand” those rights beyond normal ratemaking laws and principles.

Finally, PacifiCorp had no notice that the Commission would retroactively reclassify its historical REC revenues based on the Energy Independence Act (“EIA”) or its related regulations. As discussed in the opening brief, PacifiCorp’s historical REC revenues were not “useful” under the EIA, and thus did not fit the definition of utility property under Washington law.¹⁰² The Commission and intervenors argue vigorously that the majority nevertheless had discretion to decide to treat REC revenues as “comparable” to utility property.¹⁰³ PacifiCorp agrees that the Commission had authority to do so, *but only prospectively*. As the dissent in Order 11 recognized, PacifiCorp had no notice that the Commission would reopen past rate periods and order a new treatment for its historical REC revenues.¹⁰⁴ Without such notice, the rate credit violates the prohibition on retroactive ratemaking and the filed rate doctrine.

¹⁰¹ CP 123, 2009 GRC Stipulation at ¶ 22.

¹⁰² See Opening Br. at 31-33.

¹⁰³ Commission Br. at 38-42; Public Counsel Br. at 21-25; ICNU Br. at 38-45.

¹⁰⁴ App. 59 (AR 1793), Order 11 at ¶ 44. As noted in PacifiCorp’s Opening Brief (at 42), the dissent in Order 11 would have found that PacifiCorp had notice from the time of the initial testimony of Commission Staff in this rate case. But the Commission never

2. **PacifiCorp Did Not Engage in Misconduct, and the Commission Did Not Find Otherwise**

In Orders 10 and 11, the majority refused to adopt Public Counsel’s and ICNU’s arguments that PacifiCorp engaged in misconduct warranting an exception to the prohibition on retroactive ratemaking.¹⁰⁵ In its response brief, Public Counsel nevertheless again resurrects its misconduct allegations and urges this Court to uphold the illegal rate credit on the basis of such an exception.¹⁰⁶ But courts normally will not uphold agency action on grounds not expressed in the agency’s final order because “[t]o do so would propel the court into the domain which Congress has set aside exclusively for the administrative agency.”¹⁰⁷ As the Commission did in Orders 10 and 11 did, this Court should reject Public Counsel’s arguments.

In ordering the rate credit in Orders 10 and 11, the majority refused to rely on Public Counsel’s and ICNU’s misconduct allegations, stating specifically in Order 10 that “we emphasize that we make no finding that PacifiCorp engaged in such intentional manipulation.”¹⁰⁸ On appeal, the Commission likewise refuses to join Public Counsel’s position and expressly acknowledges that it “made no finding of intentional misconduct

previously has recognized anything less than a deferred accounting petition as adequate notice, which is consistent with generally accepted view. *See Hempling, Regulating Public Utility Performance*, at 330-31 (discussing notice and deferred accounting).

¹⁰⁵ App. 29-32 (AR 1575-78), Order 10 at ¶¶ 26-35; App. 45-55 (AR 1779-89), Order 11 at ¶¶ 5-29.

¹⁰⁶ Public Counsel Br. at 26-41.

¹⁰⁷ *Chenery Corp.*, 332 U.S. at 196.

¹⁰⁸ App. 31 (AR 1577), Order 10 at ¶ 32.

by PacifiCorp” in Orders 10 and 11.¹⁰⁹ Although Public Counsel and ICNU try to discount the Commission ALJ’s order, the ALJ rejected the same accusations of misconduct against PacifiCorp after reviewing the record, and Public Counsel and ICNU did not seek review of the ALJ’s order. Contrary to Public Counsel’s arguments, the Commission has made no finding that PacifiCorp engaged in intentional misconduct warranting an exception to the prohibition on retroactive ratemaking.

The relevant case law also does not support Public Counsel’s position. Courts uniformly have applied misconduct exceptions only in cases in which a utility engaged in “egregious” acts, usually resulting in substantial utility over-earning.¹¹⁰ In the Utah case that Public Counsel cites in its response brief, for example, the utility intentionally charged charitable contributions to ratepayers despite an order clearly ruling that such charges were unlawful and despite an express inquiry into the practice.¹¹¹ In sharp contrast, PacifiCorp has not violated any orders, and it reasonably accounted for its historical REC revenues as operating revenues. The Commission ALJ also determined that PacifiCorp fully complied with all disclosure requirements.¹¹² Public Counsel’s misconduct

¹⁰⁹ Commission Br. at 49.

¹¹⁰ See, e.g., *Cal. ex rel. Lockyer v. Fed. Energy Reg. Comm’n*, 383 F.3d 1006, 1015-16 (9th Cir. 2004) (FERC had authority to order retroactive refunds “when a company’s non-compliance has been so egregious that it eviscerates the tariff”); *MCI Telecomm. Corp. v. Pub. Serv. Comm’n of Utah*, 840 P.2d 765, 774-75 (Utah 1992) (remanding for factual hearing on utility in light of “extraordinary” overearnings and failure to respond to interrogatories about earnings).

¹¹¹ *Salt Lake Citizens v. Mountain States Tel.*, 846 P.2d 1245, 1248 (Utah 1992).

¹¹² App. 83, ALJ Order at ¶¶ 50-55.

allegations do not support any exception to the prohibition on retroactive ratemaking.

There also is no merit to Public Counsel's and ICNU's arguments that other parties lacked sufficient information to request deferred accounting of PacifiCorp's historical REC revenues. The 2009 rate settlement permitted Public Counsel and ICNU to seek information about PacifiCorp's REC revenues, but they never did so. The record evidence showed that the other parties knew about PacifiCorp's California REC contracts no later than January 2010, shortly after the contracts became fully effective.¹¹³ The Commission ALJ determined that Public Counsel and ICNU "knew beyond peradventure" of PacifiCorp's actual REC revenues by the May 2010 filing date of PacifiCorp's 2010 rate case.¹¹⁴ Although ICNU tries to deflect that evidence by claiming that it is "disturbing" that PacifiCorp relies on other sources of reporting about its REC contracts,¹¹⁵ that evidence shows that PacifiCorp's contracts were far from secret and parties had more than sufficient knowledge to file deferred accounting petitions. In fact, ICNU filed such a request for deferred accounting in Oregon in late 2009.¹¹⁶ As the dissent in Order 11 correctly

¹¹³ See AR 1539 (citing testimony in January 2010 in PSE REC Case).

¹¹⁴ App. 76, ALJ Order at ¶ 33.

¹¹⁵ ICNU Br. at 31.

¹¹⁶ CP 123, 2009 GRC Stipulation at ¶ 22 from Docket UE-090205; see also AR 5825, Motion to Dismiss in Docket UE-110070 (citing testimony of ICNU witness referencing to PacifiCorp's California contracts in support of ICNU's request for deferring accounting arising from REC-related contract (*In re Application of ICNU for Deferred Accounting Order Regarding Certain Costs and Revenues*, OPUC Docket UM 1465, ICNU/100, Falkenberg/3:3-11)).

recognized,¹¹⁷ the Commission had no authority to make adjustments to those revenues without a deferred accounting or similar advance notice of possible future ratemaking.

3. There is No “Windfall” Exception to the Prohibition on Retroactive Ratemaking and the Filed Rate Doctrine, and PacifiCorp Did Not Receive Any Windfall

Finally, in attempting to justify the rate credit in Orders 10 and 11, the response briefs mischaracterize the record surrounding PacifiCorp’s historical REC revenues and wrongly claim that PacifiCorp seeks to retain a “windfall” that belongs to its customers. But PacifiCorp did not receive any windfall, and there is no “windfall” exception to the prohibition on retroactive ratemaking and the filed rate doctrine.

Contrary to the Commission’s and intervenors’ arguments, imprecision in cost and revenue estimates in rates is not unusual. Because the Commission sets rates on a prospective basis, estimates used in ratemaking necessarily will vary from a utility’s actual costs and revenues during the rate period because it is impossible to predict actual future costs and revenues exactly.¹¹⁸ Rather than adjust for imprecise estimates, the ratemaking theory is that imprecise revenue and cost estimates ultimately

¹¹⁷ App. 59 (AR 1793), Order 11 at ¶ 43.

¹¹⁸ See, e.g., *Utility Reform Project*, 2014 WL 767951 (Feb. 26, 2014) (“Necessarily, future rates must be based on the utility’s best estimates of its future expenses and revenues, and the utility must operate with rates in effect until future rates are approved in the next rate case. Because of the rule against retroactive ratemaking, as a general matter, adjustments to rates can compensate the utility on a going-forward basis only. The general rate case does not provide a utility with an opportunity to recoup expenses beyond those forecast in prior rates; nor is the utility expected to remit revenues higher than those previously forecast.”).

balance out over time.¹¹⁹ As the Commission itself has explained, “[o]nce set, levels of expenses vary, and are expected to vary, from those established.”¹²⁰

In this case, although the response briefs repeatedly stress that PacifiCorp underestimated its historical REC revenues,¹²¹ the briefs ignore PacifiCorp’s significant overestimation of REC revenues in past projections. For example, in the nine months between April 2011 and December 2012, it is undisputed that PacifiCorp *over-credited* \$3.6 million in REC revenues to customers.¹²² The response briefs also disregard PacifiCorp’s significant underestimation of its net power costs in 2009 and 2010. For example, for just hydro-related net power costs, PacifiCorp’s actual costs exceeded rate estimates by \$7.9 million in 2009.¹²³ This is comparable to the average annual under-estimation of REC revenues for the 27-month period from January 2009 to April 2011, which was approximately \$7.5 million.

It is undisputed that PacifiCorp’s rates of return in 2009 and 2010 were far below the authorized rates, even factoring in PacifiCorp’s actual historical REC revenues.¹²⁴ This fact is irreconcilable with respondents’

¹¹⁹ See, e.g., *Indus. Customers of Nw. Utils. v. Or. Pub. Utils. Comm’n*, 196 Or. App. 46, 49, 100 P.3d 1072 (2004) (“[U]tilities bear the risk of unforeseen costs but also receive the benefit when revenues are higher than predicted.”).

¹²⁰ See, e.g., *Wash. Utils. & Transp. Comm’n v. Avista Corp.*, Docket Nos. UE-991606, UG-991607, 3rd Supp. Order at ¶ 205, 204 P.U.R.4th 1 (Sept. 29, 2000).

¹²¹ See, e.g., WUTC Br. at 9-10.

¹²² AR 1872, PacifiCorp’s Letter in Compliance with Order 12.

¹²³ AR 5203, Ex. ALK-2CT.

¹²⁴ AR 5194-95, Ex. ALK-1T; AR 5204, Ex. ALK-2CT.

claims of a “windfall.” The REC revenues at issue in this case did not provide a windfall to PacifiCorp, and this false assertion provides no basis to jettison a fundamental tenet of Washington ratemaking.

III. CONCLUSION

In Orders 10 and 11, a majority of the Commission exceeded its statutory authority and acted contrary to law by ordering a rate credit to recover PacifiCorp’s historical REC revenues from past closed rate periods. Orders 10 and 11 constitute a major departure from court and commission precedents. If adopted, customers and utilities will be free to seek to reopen closed rate periods on a single-issue basis whenever costs or revenues in rates deviate from actual amounts. This will destabilize ratemaking in Washington to the detriment of all. Orders 10 and 11 pose a real and significant threat to the integrity of ratemaking in Washington. Orders 10 and 11 are unlawful and must be set aside.

Respectfully submitted this 21st day of March, 2014.

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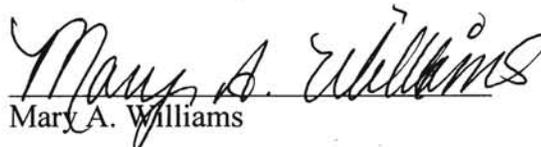
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CERTIFICATE OF SERVICE

I hereby certify that on the 21st day of March, 2014, I caused to be served the foregoing REPLY BRIEF OF APPELLANT on the following parties at the following addresses:

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by delivering to them a true and correct copy thereof, certified by me as such, by way of E-mail and U.S. Postal Service-ordinary first class mail.


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