

**REPORT ON THE PROPOSED
WASHINGTON COUNTY PEOPLES' UTILITY DISTRICT
BY THE
OREGON DEPARTMENT OF ENERGY
JULY 8, 2004**

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Introduction

This is the Oregon Department of Energy's report on the proposed Washington County People's Utility District (PUD). Under ORS 261.151, the Department of Energy must hold a hearing and issue a report not less than 30 days and not more than 60 days after receipt of a petition to form a PUD.

The statute provides that the report should be concise and should address the availability and cost of power or water resources, potential tax consequences and any other information relevant to the proposed formation of the PUD. In preparing the report, the Department of Energy is to obtain the advice and the assistance of the Public Utility Commission. A copy of the report is to be provided to the county governing body.

This report is not intended to take the place of a detailed feasibility or engineering study. The time provided by law for the Department to conduct a hearing and to issue a report limits the scope of this report and precludes a more in-depth analysis which an engineering study or a detailed feasibility study could provide. Upon completion of this report the Department has no further role in this process.

The Department consulted with the Public Utility Commission in the preparation of this report as required by law. The contents and conclusion of the report, however, are solely those of the Department. The Public Utility Commission did provide a letter through its Assistant Attorney General at a previous hearing on formation of a proposed PUD in another county. The letter discusses the role of the Commission to protect regulated ratepayers in the event of an attempted condemnation by a publicly-owned utility of utility property owned by an investor-owned utility. A copy of that letter is included as an attachment to this report.

Background

A petition to form the Washington County PUD was filed with Washington County, certified by the county and received by the Department on May 12, 2004.

The proposed area of the PUD would include all of Washington County except the City of Forest Grove and other territory served by the municipal electric utility of the City of Forest Grove. Currently, the electricity provider in the area of Washington County covered by the proposed PUD is Portland General Electric (PGE).

Pursuant to ORS 261.113, the PUD chief petitioners also propose the question of whether the proposed PUD would be authorized to impose a one-time special levy of 3 mills per one thousand dollars of assessed valuation (equal to \$3 per million dollars of assessed valuation) to finance an engineer's report and the election under ORS 261.355(1)

Summary of the Hearing

A hearing was held on June 30, 2004 at the City of Tigard Town Hall Meeting Room. Approximately forty people attended the hearing. Twenty-four people spoke at the hearing. A list of those who testified is attached.

In addition, written comment was accepted through Friday July 2, 2004. Nearly forty written comments were received.

Supporters of the proposed PUD explained the purpose of forming a PUD and their reasons for supporting it. These reasons included among others the following:

PUD supporters believe that there are many advantages which would result from local control over electricity service which a PUD would provide. These include potential advantages in the price of electricity through access to BPA power, reduced operating costs by a PUD being a non-profit governmental entity; and tax savings to the customers of a PUD from the absence of corporate income taxes which a PUD would not have to pay. In addition, the PUD supporters believe that the PUD could acquire through condemnation any generating and distribution assets it needed to serve its load. They also believe that the absence of privately-held stock would assure that decisions made by a PUD on electricity service are made only with the interests of consumers in mind.

The PUD supporters also believe that the PUD would have financial advantages over an investor-owned utility by being able to issue tax-exempt bonds and to acquire resources through condemnation at "book value". In addition, they believe that removing PGE ratepayers from the Enron corporate entity is in the interests of electric ratepayers and consumers. PUD proponents believe that a bankruptcy court could order sale of PGE assets to pay off Enron creditors and that the interest of ratepayers would not be considered in such a sale. They also believe that questions of funds withheld for income taxes but not paid by Enron provide additional reasons to form a PUD. They also believe that the pending sale of PGE to the Texas Pacific Group would be no better than ownership by Enron.

PUD supporters also believe that the experience of other PUDs formed in Oregon and Washington show that it is possible and practical to create and operate a PUD economically and efficiently. They also believe that the experience of these other PUDs indicates that it is not technically difficult to create a PUD or to address technical issues of interconnection, separation of a new PUD from PGE's system, reliability and other operational questions.

Opponents of the proposed PUD also provided a number of reasons for their opposition. These reasons included, among others the following:

PUD opponents expressed concern about the impact of forming a PUD on PGE customers who are not in Washington County; and the impact on the local economy of replacing a private business with a governmental entity including loss of tax base, elimination of private sector jobs, loss of charitable contributions, loss of public purpose funding and other adverse impacts. They believe that there would be a loss of volunteer community efforts currently provided by PGE employees if a PUD took over PGE's operations.

PUD opponents also believe that forming a PUD sends an anti-business message by replacing a private business with a governmental entity; and the PUD would lack independent regulatory oversight which the Oregon Public Utility Commission currently provides over investor-owned utilities. They believe that PGE has a good record of customer service and performance and a strong record of economic development activities which benefit the entire region.

Those opposing formation of the PUD also stated that they believed it was unlikely that a new PUD would have access to BPA power; that the PUD would need to incur a large amount of indebtedness to acquire utility assets from PGE; and that the ability of the State of Oregon to continue to use tax-exempt financing for housing, economic development and other purposes would be adversely affected if a new PUD issues tax-exempt bonds. They also expressed concern about the loss of many skilled and dedicated workers, and the likelihood that a new PUD would have to acquire resources on the volatile open market, which could result in higher rates. They also believe that a PUD does not have condemnation authority over generating power facilities. In addition, they believe that separating the transmission and distribution system of Washington County from the rest of PGE would be very complicated and expensive, costing \$15-20 million.

Discussion of Major Issues

Access to BPA Power

Consumer-owned utilities in the Northwest, including PUDs, have traditionally had access to wholesale power from the Bonneville Power Administration (BPA). In the past, such utilities have usually had the option to contract with BPA for as much power

as they have needed. However, it is likely that BPA will have difficulty in acquiring additional low-cost resources to serve a new large load formed by a new PUD.

Moreover, BPA's wholesale rates have increased substantially in the last few years as a result of supply and price problems in the wholesale market. These factors make it difficult to determine whether any substantial rate benefit would occur if a new PUD had access to BPA power for a substantial part of its load.

Access to BPA power at BPA's lowest cost-based rate is also uncertain even under the status quo. Currently until October 1, 2006, any new publicly-owned utility would have access to BPA power at prices above BPA's lowest cost-based rate. The higher rate charged by BPA is intended to reflect the additional costs of serving new utility customers. BPA is also considering alternative pricing policies that could affect the price at which a new PUD could buy power from BPA.

Acquisition of Other Resources

ORS 261.305 provides that people's utility districts have the power "...to acquire, develop, and otherwise provide for a supply of water for domestic and municipal purposes, waterpower, and electric energy, or electric energy generated from any utility, and to distribute, sell, or otherwise dispose of water, water power, and electric energy within or without the territory of such districts."

While a PUD can provide either water or electricity service, the PUD proponents indicated that their intent at this time is to provide electric service. The information provided by people who spoke at the hearing both in favor and against formation of a new PUD dealt only with issues regarding electric service.

PGE opposes the formation of a PUD in its service area. PGE officials indicated that they would not willingly sell or transfer their facilities, including generating resources and distribution assets, to a new PUD. The PUD would likely be required to acquire assets from PGE through condemnation. In the absence of agreement between the new PUD and PGE a court would need to determine the value of any property acquired by the new PUD through condemnation.

Valuation of such assets would require a detailed engineering and appraisal study. In addition, while the PUD proponents believe that a PUD would have authority to acquire power generating resources through condemnation, PGE disputes that the PUD would have such authority. Resolution of the limits of PUD condemnation authority would likely also require a determination by a court.

If the new PUD did not try to acquire PGE's generating assets it could purchase power on the open market or finance new generating facilities. The open market is very volatile and the price of power, especially for long-term contracts, is uncertain. The costs of financing new generating resources directly by a PUD are also uncertain. Issuance of bonds by a PUD poses a number of questions requiring further study.

These include whether bonds would be tax-exempt or taxable, at what cost such bonds could be issued, the impact on other public debt issued by state and local governments in Oregon and other issues.

The PUD supporters offered a preliminary feasibility study prepared by D. Hittle and Associates for the recently proposed Clackamas PUD as evidence that a new PUD would be able to become operational, acquire energy resources and could operate at lower rates than PGE. PGE in response offered a study by Sam Van Vactor of Economic Insight, Inc., indicating that a new PUD would likely be unable to acquire power without paying substantially more than PGE now pays to provide service to its existing customers.

To assure that energy conservation and renewable resources play a key part of resource acquisition, Oregon's restructuring law provides that PGE customers pay a 3% public purpose charge to fund energy conservation, renewable resources and other public purposes. A new PUD would not be obligated to pay this 3% public purpose charge. However, the PUD may choose to fund through its rates an equivalent amount of energy conservation and renewable resources, although it would not be required by law to do so.

These uncertainties and questions cannot be easily answered without a detailed financial analysis of different scenarios, and an analysis of which scenarios are most likely to bound the range of uncertainty. The analysis required to answer these questions is beyond the scope of this report.

Tax Consequences

Under Oregon law, a PUD has the power to issue revenue bonds (ORS 261.355) and general obligation bonds (ORS 261.360) upon receiving voter approval. Revenues from the bonds may be used for any purpose authorized by law. General obligation bonds must not exceed two and one-half percent (.025) of the real market value of all taxable property within the district.

ORS 261.385 provides that a PUD may also levy and collect property taxes prior to receipt of operating revenues. In any one year, the tax cannot exceed one-twentieth of one percent of the true cash value of all taxable property within the PUD. Over 10 years, the tax cannot exceed in the aggregate one-fourth of one percent of the true cash value of property within the PUD.

A PUD may have access to tax-exempt bond financing for capital acquisition and possibly for some operating costs. Current federal limits on state and local tax-exempt financing make it difficult to determine to what extent a new PUD could use tax-exempt bonds for its financing. Moreover, the U.S. Treasury continues to seek further restrictions from Congress on the use of tax-exempt bonds by state and local governments, making the future access to this form of financing uncertain.

Taxable bonds, which incur higher interest charges than tax-exempt bonds, could also be issued by a new PUD, but whether they would be less expensive than the current costs of capital of PGE is uncertain, given PGE's long history of access to the capital markets with a variety of financial instruments.

A PUD pays no state or federal income taxes, but a PUD is subject to property tax assessment under ORS 261.050 to the same extent as property of an investor-owned utility is taxed.

Conclusion

In order to fully analyze the economic advantages and disadvantages of forming a new PUD, many questions must be analyzed thoroughly. There are also factors which could vary greatly and have significant impact on whether a PUD would have access to a supply of power at reasonable rates. For example, whether a new PUD would have access to significant amounts of BPA power, how much BPA rates will increase, whether a PUD could condemn PGE's generating resources and if so, at what price, what the cost of financing capital for a new PUD would be and to what extent tax-exempt bonds could be used are all factors which could impact the cost of electric service by a new PUD compared to the cost of service currently provided by PGE.

In addition, non-economic questions, such as the value of local control, the benefits of private enterprise, the role of government and other issues involving value judgements as well as economic considerations must be examined. Many of these issues were raised and discussed at the hearing and in the written comments filed in this record.

The resolution of the questions raised and the differing perspectives and opinions expressed cannot be readily resolved, without more extended study and analysis of these issues. Questions such as the valuation of utility property, what utility property is subject to condemnation, access to BPA power, and the availability or lack of tax-exempt financing are all complex issues requiring extended review and analysis.

Because these issues require extensive investigation and analysis to resolve, the limited scope of this report precludes making a definitive conclusion as to the impact on rates caused by forming a new PUD. In addition, other questions such as the role of private businesses compared to a publicly-owned utility system present value judgements for the voters.

This report makes no recommendations as to whether the proposed Washington County PUD should or should not be formed. That is a decision for the voters to make, after evaluating many issues including the issues raised in this report.



DEPARTMENT OF JUSTICE
GENERAL COUNSEL DIVISION

April 11, 2003

Michael Grainey, Director
Office of Energy
625 Marion Street NE, Suite 1
Salem, Oregon 97301-3742

Re: Oregon Office of Energy Report on PUD Formation in Multnomah County

Dear Mr. Grainey;

The Public Utility Commission of Oregon has asked me, as its chief counsel, to submit comments in the Oregon Office of Energy's report regarding PUD formation in Multnomah County. The Commission made its request to me because members of the Oregon Legislative Assembly asked the agency for comments.

The Commission does not have a position regarding the formation of a PUD in Multnomah County, but it has asked me to discuss PUC statutes that may come into play and positions the Commission has taken in the past regarding condemnations by consumer-owned utilities of property owned by investor-owned utilities. The condemnations have involved distribution and generation assets. I will discuss each separately.

Distribution Assets

A Multnomah County PUD would need to acquire the distribution assets that Portland General Electric Company and Pacificorp now use to serve their customers within the county. In cases in which a consumer-owned utility is condemning distribution assets of a utility regulated by the PUC, and thereby is also taking responsibility to serve some customers, the Commission's duty is to protect remaining customers of the regulated utility.

Under ORS 757.480, a public utility, such as PGE or Pacificorp, may not dispose of property with a value in excess of \$100,000 unless it has the consent of the Commission. If a Multnomah County PUD condemns assets of an investor-owned utility, then the statute may not apply, as the court's award may supercede the Commission's authority. On the other hand, if there is a settlement, then it would be up to the Commission to approve the price.

There have been two recent court cases involving condemnation by consumer-owned utilities of distribution assets of PacifiCorp, one case in the Halsey area and the other in Hermiston. The Commission was involved in both cases, taking the position that fair market

value, not book value, is the appropriate standard for courts to apply in such cases. In both cases, the market value of the distribution assets was in fact well above book value. When the utility receives more than book value, the Commission's policy is to award the vast majority of the excess (i.e. the capital gain) to the remaining customers. That is precisely what the Commission did after PacifiCorp received settlements well in excess of book value for the Halsey and Hermiston assets.

The Commission gives the vast majority of the capital gain on sales of distribution assets to customers because they pay rates based on the utility's book value. If market value is below book value, customers "lose" because they return the higher book value to the utility, as well as a return on the higher book value. Conversely, when a utility sells an asset that has a market value that is above book value, customers "win" by having the Commission use the capital gain to reduce rates.

Generation Assets

The PUC was also an intervenor in a case in which Emerald People's Utility District attempted to condemn four PacifiCorp hydro-electric facilities on the North Umpqua. The Commission intervened in that case, and along with PacifiCorp, successfully prevented the condemnation. *Emerald People's Utility Dist. v. PacifiCorp*, 100 Or App 79, on reconsideration, 101 Or App 48, review denied 310 Or 121 (1990). The Commission opposed the condemnation because PacifiCorp would have had to replace low-cost hydro-electric resources with more expensive resources, thereby raising the company's rates. The Court prohibited the condemnation, finding that it was not in the public interest, as it would have lowered Emerald's already low rates and would have increased Pacificorp's comparatively high rates.

If a Multnomah County PUD is formed, and it wishes to condemn generation assets that either PGE or PacifiCorp uses to serve its customers, and if the utilities have to replace those resources with more expensive ones, then the Commission will likely oppose such a condemnation because it would not be in the interest of customers whom the Commission must protect.

Please do not hesitate to contact me if you have any questions.

Sincerely,

Paul A. Graham
Attorney-in-Charge
Regulated Utility & Business Section

cc: Lee Beyer, Commission
Roy Hemmingway, Commission
Joan Smith, Commission
John Savage, Utility Director – PUC
Lee Sparling, Utility – PUC
Marc Hellman, ERFA – PUC

List of Those Who Made Statements at the Hearing

Proposed Washington County Peoples' Utility District

Jim McNaughton
Dan Meek
Tom Civiletti
Lloyd Marbet
Peggy Fowler
Steve Hawke
Joe McArthur
Rob Drake, Mayor of City of Beaverton
Donna Schmidt
Henry Germond
Ken Griffin
Liz Trojan
Wayne Lei
Nancy Newell
Christine Dunn
Grant Kirby
Mike Caruso
Jonathan Schlueter
Tom Fishback
Steve Geiger
Renee Cannon
Jim Hirte
Colm Brennan
Eulia Mishima

List of Those Who Provided Written Statements

Proposed Washington County Peoples' Utility District

Barbara Block, Tektronix
Douglas J. Schaffer
Randall Edwards, Oregon State Treasurer
Valerie Bass
Tualatin Chamber of Commerce
Gregory R. Mowe
Jim Piro, PGE
Shantu Shah
Bill Miller, IBEW Local 125
Howard South
Tigard City Council
Kristine Fagler
Dan Meek
Tom Civiletti, D. Hittle Study for Clackamas County
Lloyd Marbet
Peggy Fowler
Steve Hawke
Joe McArthur
Rob Drake, Mayor of City of Beaverton
Donna Schmidt
Henry Germond
Ken Griffin
Liz Trojan
Wayne Lei
Christine Dunn
Grant Kirby
Mike Caruso
Jonathan Schlueter, Westside Economic Alliance
Tom Fishback
Steve Geiger
Jim Hirte
Lisa Melyan
Chris Dieterle
Joan Horton
Jay Formick, Oregon Heat
Sam Van Vactor and Fred Pickel
Pamela Lesh
Hillsboro Chamber of Commerce
Curt Sommer
Gary Duel