Service Date August 31, 1984

DEPARTMENT OF PUBLIC SERVICE REGULATION
BEFORE THE PUBLIC SERVICE COMMISSION
OF THE STATE OF MONTANA
* * * * * * *

IN THE MATTER of the Application of PACIFIC POWER & LIGHT COMPANY for Authority to Adopt New Rates and Charges for Electric Service Furnished in the State of Montana - COLSTRIP UNIT NO. 3 AND RELATED FACILITIES.	) UTILITY DIVISION)) DOCKET NO. 83.10.71)) ORDER NO. 5028c))

APPEARANCES

FOR PACIFIC POWER AND LIGHT COMPANY:

George M. Galloway, Attorney at Law; Stoel, Rives, Boley, Fraser & Wyse, 1730 M Street, NW, Suite 900, Washington, D.C. 20036

I. James Heckathorn, Attorney at Law; Murphy, Robinson, Heckathorn & Phillips, P. O. Box 759, Kalispell, Montana 59901

FOR THE MONTANA CONSUMER COUNSEL

James Paine, Consumer Counsel, 34 West Sixth Avenue, Helena, Montana 59620

FOR THE COMMISSION

Opal Winebrenner, Staff Attorney, 2701 Prospect Avenue, Helena, Montana 59620

BEFORE:

HOWARD L. ELLIS, Commissioner, Presiding
CLYDE JARVIS, Commissioner
JOHN B. DRISCOLL, Commissioner

FINDINGS OF FACT
PART A
GENERAL

1. On October 21, 1983, PP&L filed with the Commission an application for authority to increase rates and charges for electric service. PP&L requested an annual revenue increase of $467,000 or 1.9 percent to recover the Company's increased purchased power costs due to the Bonneville Power

Administration's (BPA) wholesale rate increase. PP&L also requested a $776,000 or 3.1 percent rate increase to cover the inclusion of PP&L's portion of the Colstrip Unit 3 plant. The rate increase was decreased to $766,000 at the public hearing, as explained in Finding of Fact No. 61.

2. On October 21, 1983, PP&L filed an application for an interim rate increase of $1,243,000 based on the increased BPA rates which were effective November 1, and the Colstrip Unit 3 production and transmission plant addition scheduled to be placed in service in December, 1983.

3. On October 31, 1983, the Commission issued Interim Order No. 5028 which granted PP&L approximately $322,000 in interim relief to reflect the BPA increase. The $322,000 does not reflect that portion of the request associated with BPA's transmission charges.

4. On February 6, 1984, the Commission issued Supplemental Interim Order No . 5028a, which granted PP&L approximately $145,000 in interim relief, to reflect the increase associated with the BPA transmission rates disallowed by the Commission in Interim Order No. 5028. The Federal Energy Regulatory Commission (FERC) had approved the BPA transmission rate increase effective February 1, 1984.

5. On February 6, 1984, the Commission issued a Notice of Application and Proposed Procedural Order. The Procedural Order was finalized on February 17, 1984.

6. On March 1, 1984, the Commission issued a Notice of Commission Action informing parties to the Docket that PP&L's proposed power sales agreement with the Black Hills Power and Light Company would be considered in this Docket.

7. On January 16, 1984, PP&L requested authorization from the Commission to either allow deferred billing of Colstrip Unit No. 3 costs with a surcharge for 12 months, or to allow the continued accrual of AFUDC (Allowance for Funds Used During

Construction) on the Colstrip Project.
On May 1, 1984, the Commission issued Accounting Order No. 5028b which authorized PP&L to accrue AFUDC on Colstrip Unit No. 3 and related facilities, pending the Commission's final decision in this Docket. AFUDC would be calculated upon the exact number of days between January 10, 1984, the commercial operation date for Unit No. 3, and the date of issuance of the Commission's final order, using 10.75 percent, PP&L's cost of capital from Docket No. 83.5.36, as the rate of interest.

8. The Montana Consumer Counsel (MCC) intervened and participated in this Docket, on behalf of electric utility customers throughout these proceedings.

9. On June 12 and 13, 1984, pursuant to public notice, the Commission held the hearing on this Docket at the Outlaw Inn, Kalispell, Montana. Evening public hearings were held June 12 in Kalispeil, and June 13 in Libby, Montana.

PART B
MOTION TO STRIKE
Background

10. On April 9, 1984, PP&L filed a Motion to Strike and Supporting Memorandum that requested the Commission to strike pages 6-17 and 19-22 of witness Basil L. Copeland's prefiled Direct Testimony presented on behalf of the Montana Consumer Counsel. Those portions of Copeland's testimony set forth his contention that PP&L's investment in Colstrip Unit 3 and its related facilities represent "excess capacity. " PP&L contends that the Montana Board of Natural Resources and Conservation's (BNR) 1976 decision that there is a need for Colstrip Unit 3 precludes the Commission from reinvestigating whether Colstrip Unit 3 is "used and useful."

11. On April 30, 1984, the Commission deferred acting upon the Motion to Strike until after the completion of the Docket's public hearing, and following receipt of briefs on

the Motion from PP&L and MCC. At the hearing, PP&L made a continuing objection to the presentation of testimony on the excess capacity question.

12. On July 20, 1984, the PSC voted to deny the Motion to Strike and proceeded to determine the merits of the case.

13. PP&L's Motion to Strike contains essentially the same arguments as were included in the Montana Power Company's (MPC) Motion to Strike and Memorandum filed in Docket No. 83.9.67, MPC's Colstrip Unit 3 rate application.

14. On July 3, 1984, MPC filed with the Montana Supreme Court, a Petition requesting that the Court assume original jurisdiction, and decide the issues raised in the Motion to Strike. The Petition is now pending.

Major Facility Siting Act

15. PP&L's Motion to Strike requires the PSC to interpret 69-3-109, MCA, commonly known as the "used and useful" statute, which states:

The Commission may, in its discretion, investigate and ascertain the value of the property of every public utility actually used and useful for the convenience of the public. The Commission is not bound to accept or use any particular value in determining rates; provided, that if any value is used, such value may not exceed the original cost of the property. In making such investigation the Commission may avail itself of all information contained in the assessment rolls of various counties, the public records of the various branches of state government, or any other information obtainable, and the Commission may at any time of its own initiative make a revaluation of such property. (emphasis added)

16. PP&L contends that this statute must be interpreted, in

this case, in concert with the provisions of the Montana Major Facility Siting Act (MFSA, or Siting Act), Title 75, Chapter 20, MCA.

17. The used and useful statute is today, and has been since adopted by the Montana Legislature, a cornerstone of public utility regulation. The rates consumers pay for utility service are substantially determined by what investments are considered actually used and useful for the convenience of the public. Thus, PP&L's claim is a very serious one, since it would guarantee full ratemaking treatment for any facility subject to the Major Facility Siting Act.

18. The PSC, in recent years, has had occasion to interpret the used and useful statute as it applies to new plants. In Docket No. 81.1.2, Order No. 4799b, the PSC concluded that part of the Montana-Dakota Utilities Company's Coyote Plant was excess, and made a rate base adjustment to account for that fact. More recently, in Docket No. 82.7.53, Order No. 4975, the PSC concluded that the used and useful statute precluded rate making for abandoned nuclear plants in which PP&L had an interest.

19. PP&L contends that the BNR's 1976 decision to grant a certificate of environmental compatibility and public need for Colstrip Unit 3 was conclusive. In PP&L's view then, the PSC " . . . has no jurisdiction to reinvestigate whether Colstrp Unit 3 is 'used and useful' . " (Memorandum, p . 4) In making its contention, PP&L cites the supremacy language from 75-20-103, MCA, and 75-20-401, MCA, from the Siting Act as " . . . reflecting clear legislative intent to have the BNR's findings conclusive and final - an intent contrary to the notion that the need for Colstrip Unit 3 can be relitigated in yet another Montana Administrative forum. " (Memorandum, p. 5).

20. As stated by MCC, PP&L "simply assumes that (1) these statutes override any powers of the PSC, namely the power to

evaluate 'used and useful' utility property, and (2) there exists a conflict between the Major Facility Siting Act provisions and 69-3-109, MCA. " (MCC Response, p. 2).

21. In essence, PP&L is arguing that the Siting Act's statutory terms of "need" and "public convenience and necessity" are equivalent to the PSC's statutory phrase "actually used and useful. " Further since the PSC, as a statutorily created body, has only the powers conferred upon it by the legislature, PP&L contends that the legislature has not conferred upon the PSC " . . . the jurisdiction to determine whether major facilities constructed in Montana are needed." (Memorandum, p. 4).

22. To accept PP&L's interpretation of statutory terms would utterly ignore the timing differences inherent in the BNR preconstruction process to determine "need" and "public convenience and necessity," and the PSC post construction process to determine whether a utility's investment is "actually used and useful" for today's ratepayers.

23. The terms "need" and "public convenience and necessity" are not exclusive to the Siting Act, but are technical terms that must be interpreted in a number of contexts by different agencies. For example, the PSC is charged with reviewing applications from motor carriers. Only upon a finding that the public convenience and necessity would be served, can the PSC allow a proposed new motor carrier service. 69-12-323, MCA. Similarly, new health care facilities cannot begin operation until the Board of Health finds a "need" for the proposed service. 50-5-301 et seq, MCA. Neither of these statutes, either implicitly or explicitly, guarantees any future economic benefits. This is true even when the PSC exercises ratemaking jurisdiction, as it does for certain classes of motor carriers. Both, like the MFSA, go to the issue of whether there should be a new service or a new facility. PP&L's argument incorrectly seems to assume that these terms have no accepted or technical meaning and that their meaning must be construed for the first time here and

only in the context of the Siting Act.

24. Based on its experience with public convenience and necessity determinations under the Motor Carrier Act, as well as its involvement in the Siting Act, both in the legislative and administrative arenas, the PSC finds PP&L's interpretation of the phrase "public convenience and necessity" illogical. It is the PSC's interpretation of that phrase and the statutory intent underlying it, that such a barrier is intended to reduce costs by eliminating duplicative services and facilities. The same seems to be true of the Board of Health's role in making need determinations for health care facilities. Contrary to that interpretation, PP&L would convert what are obviously consumer protection statutes and, in the case of the Siting Act environmental protection statutes, into revenue guarantee statutes for the regulated industries. Thus, such statutes would insure higher costs, whether or not reality matched the predictions that must be made in such preconstruction, pre-initiation of service determinations.

25. Like the terms used in the MFSA, the phrase "actually used and useful" in public utility law goes back to the very root of public utility regulation. Its meaning has been interpreted repeatedly by this Commission and virtually every Commission in the country.

The Montana statute gives the PSC the power to value investment that is "actually used and useful for the convenience of the public." "Actual" is defined as "existing in act; real; in opposition to speculative, or existing in theory only." (Webster's New Twentieth Century Dictionary).

26. Ignoring over 65 years of regulatory experience, PP&L now asks the Commission to adopt the position that these terms - "need," "public convenience and necessity," "actually used and useful" - are precisely synonymous. No legal support is offered for this position.

27. Unlike the Montana Power Company, PP&L's Motion to Strike and Memorandum in Support did not address the legislative history the Montana Power Company contends so clearly prevents the PSC from making its 69-3-109, MCA "used and useful" determination.

28. MCC's Response Brief included an attachment of the arguments it made. in the MPC Colstrip case concerning MPC's assumptions in discussing the Siting Act, and 69-3-109, MCA, the PSC's "used and useful" statute. MPC's assumptions are that "the legislature has transferred some power from the PSC to the BNR" (cite omitted), and that "certain provisions of the Major Facility Siting Act are in conflict with Title 69, MCA provisions" (cite omitted). (MCC Response, Attachment A).

29. PP&L has made the same assumptions as MPC, that somehow the PSC's used and useful statute was changed or impliedly amended by the Legislature's adoption of the Siting Act. Such an interpretation by PP&L ignores elemental rules of statutory construction.

30. Under well-settled legal principles, it has been deemed that a general repealing clause cannot be considered an express repeal, since it fails to identify or designate any statute to be repealed. 1A Southerland Statutory Construction '23.08 (1973). Further such general repealing clauses are legally considered a nullity. Id. See also State ex ref. Charlotte v. District Court, 107 Mont. 489, 494, 86 P.2d 750 (1938) which stated, "Courts in general, in speaking of these repealing clauses, have held that they add nothing to the repealing effect of the Act of which they are a part. . . ".

31. Neither can the Siting Act be considered an implied repeal. Repeals by implication are not favored. Dolan v. School District No. 10, 195 Mont. 340, 636 P.2d 825 (1981) and State v. Gafford, 172 Mont. 350, 563 P.2d 1129 (1977).

In keeping with that principle, every effort is made to reconcile statutes and render provisions of each effective. State ex ref. Nagle v. The Leader Co., 97 Mont. 586, 37 P.2d 561 (1934), and State ex ref. Nonmile v. Cooney, 100 Mont. 391, 47 P.2d 637 (1935) . Repeals by implication of the specific provisions of an earlier statute will not be made unless the intent to repeal is clearly manifested or unavoidably implied by irreconcilable provisions. Kuchan v. Harvey, 179 Mont. 7, 585 P.2d 1298 (1978).

As noted by the MCC, the Siting Act "nowhere purports to repeal or amend any of the provisions of Title 69, MCA. " (MCC Response, Attachment A)

32. The PSC believes that the provisions of the Siting Act can be easily and logically harmonized with the "actually used and useful" provisions of 69-3-109, MCA. -

Within the limits of proceedings that must necessarily rely on estimates of future energy needs and intelligent speculation based on forecasts, the Siting Act intends to screen out undesirable and clearly unneeded facilities. The Act is administered by a Board whose expertise is in the area of natural resources.

The PSC's considerations, under Title 69, Chapter 3, MCA, look at very different issues and involve an entirely different set of factual determinations. The issues involve whether, at the time the utility plant goes into service, current ratepayers require it for their energy needs. An ancillary determination must be made as to what monetary value should be assigned to these plants.

33. If the legislature indeed intended to repeal the "actually used and useful" statute, it seems curious that when it amended 69-3-109, MCA, in 1975, no reference was made to its repeal under the Siting Act's repealing provisions.

(Sec. 1, Chi. 28, L. 1975) This lapse by the legislature seems especially peculiar in light of the Siting Act's passage in 1973, and the very visable controversy that surrounded the proposed construction of Colstrip Units. 3 and 4 from 1973, when PP&L, MPC and the other utilities filed with the Department of Natural Resources and Conservation an application for a certificate of environmental compatibility and public need for the units, until 1979, when the Supreme Court upheld the BNRC decision.

34. The implied repeal theory suffers from other infirmities: It has been called the golden rule of statutory interpretation that reasonableness of the result produced by one among alternative possible interpretations of a statute is reason for rejecting that interpretation in favor of another which would produce a reasonable result. It is said to be a well established principle of statutory interpretation that the law favors rational and sensible construction. Yunker v. Murray, 170 Mont. 427, 434, 524 P.2d 285 (1976), quoting 2A Sutherland, Statutory Construction '45.12.

35. Statutory construction should not lead to absurd results if a reasonable construction will avoid it. State ex ref. Ronish v. School District No. 1, 136 Mont. 453, 348 P.2d 797 (1960); Montana Power Co. v. Cremer, 18Z Mont. 277, 596 P.2d 493 (197g).

Such a result would flow from an acceptance of PP&L's theory. The BNR made its determination of need for Colstrip 3 and 4 on July 22, 1976. Colstrip 3 went into commercial operation on January 10, 1984. By PP&L's interpretation, the State of Montana has decided that ratepayers must, by law, pay for a plant, based on an eight year old estimate of future energy requirements, no matter what facts supercede that determination. Although PP&L itself regularly updates information it uses to plan future resources, its legal

theory requires the PSC to conclude that, by law, the State of Montana wishes to ignore completely new factual data in its imposition of new resource costs on PP&L's ratepayers. That is, indeed, an absurd result. It is especially absurd if one accepts the view that the Siting Act was designed, at least in part, to help assure better resource and environmental planning. Under PP&L's theory, once a certificate was issued by BNR, all planning could be abandoned by the utility for the certificate facility because the utility would then be guaranteed a return on investment, whether or not intervening conditions changed the estimates that were presented to BNR during Siting Act proceedings. Thus, PP&L's theory would transform a law designed to encourage intelligent planning, into one that absolves corporations of any planning responsibility for a proposed facility. The absurdity of this kind of approach is exemplified by decisions that allow rate base treatment for abandoned plants, plants that are never expected to produce one kilowatt of power. See Rochester Gas and Electric Corp ., 41 P.U.R. 4th 438.

36. If PP&L's position were accepted, neither the BNR nor the PSC could judge, based on known facts, whether a plant was "actually used and useful" at the time it went into commercial operation, since the determination was made in 1976 before anyone knew the actual cost of the project. A statutory scheme designed to encourage intelligent planning has, under PP&L's theory, become a carte blanche for a utility's investment decisions, including the construction of huge generation plants. This the PSC cannot accept.

Promissory Estoppel

37. PP&L has argued that the PSC cannot make an "actually used and useful" determination for Colstrip Unit 3 due to the doctrine of promissory estoppel. Without the ability to make a "used and useful" determination, PP&L contends the PSC is precluded from making any excess capacity determination regarding Colstrip Unit 3.

38. Under PP&L's contention, the State of Montana, acting as the Board of Natural Resources and Conservation, made a "promise" to all the utilities involved in the Colstrip Project. As PP&L states in its Memorandum, "By issuing the certificate of environmental compatibility and public need, the State of Montana is making an implicit, but unambiguous, promise -- that it would not once again raise the issue of the need for Colstrip Unit 3. " (Memorandum, p. 6).

39. The MCC argued in its Response that PP&L has failed to show any evidence that the BNR had any power, authority or capacity "to promise that Colstrip Unit No. 3 would be granted a return through inclusion in rate base. " (p. 12)

40. The PSC cannot accept PP&L's analysis. PP&L mischaracterizes a regulatory relationship as a contractual one. Certainly, a state can enter into contracts in its proprietary capacity. The relationship between a state and-public utility, however, is regulatory -- not contractual. The state acts in its sovereign, not in its proprietary function. In regulating a public utility, the state exercises its police power in the public interest. The state need not and does not promise or give up anything in order to regulate. The limits on the exercise of the police power lie in the Constitution, not in any private agreement between the state and the regulated entity. Public utilities derive their powers from legislative enactment, not from private bargaining.

41. Terms of the Siting Act itself contradict PP&L's claim of promissory estoppel. For example, 75-20^403, MCA, allows the BNR to unilaterally revoke the certificate. Such a power is not consonant with the characterization of the certificate as a contractual promise. Further, 75-20-408, MCA, provides for civil penalties for violations. Penalties are a regulatory tool. They are forbidden as remedies for violation of contracts. The remedies available by law for breach of a contract are limited to damages, restitution and specific

performance. Restatement (Second), Contracts, ' 1 (1981).

42. Even if the certificate granted by BNR could be characterized as a promise, it is not sufficiently specific to allow application of the doctrine of promissory estoppel. Nowhere does the certificate even allude to future rate base treatment. "The first element [of promissory estoppel] that must be established to prove a contract by the doctrine of promissory estoppel is the. . . clear and unambiguous promise. The terms of the promise must be certain, as there can be no promissory estoppel without a real promise. " v. Glacier Park, Inc., Mont. , 614 P.2d 502, 506, 37 St. Rep. 1151 (1980). PP&L claims that, the "promise" is "implicit, but unambiguous." The BNR's so-called promise to include Colstrip 3 within PP&L's rate base does not even rise to the level of ambiguity because it was never articulated in the first place. Its terms are unknown -- how much of the plant's costs may be included in rate base? Does PP&L have a carte blanche to pass off all expenses to the consumer, including ones that are found unreasonable? Does PP&L have the sole authority to determine when rate base treatment will be granted? A court cannot enforce a promise that is indeterminate. If PP&L wants to characterize the certificate as a contractual promise, it should have at least bargained for clear terms.

43. The Montana Supreme Court has consistently disfavored estoppel as a general rule. Tribble v. Reely, 171 Mont. 201, 557 P.2d 813 (1976); Boise Cascade Corp . v. First Security Bank, 183 Mont. 378, 600 P .2d 173 (1979) . This is particularly true when estoppel is urged against the government:

As a result of these policy considerations, we have stated in previous cases that the application of the doctrine of equitable estoppel to government entities will be looked upon with disfavor. The doctrine will be applied only in exceptional circumstances or where there

is manifest injustice. (Citations omitted). Chennault v. Sager _Mont. _, 610 P.2d 173, 37 St. Rep. 857

44. Estoppel has no applicability to a change of position with respect to a matter of law. Colwell _ City of Great Falls, 117 Mont. 126, 157 P. 2d_
1013 (1945). This means, of course, that even if the estoppel theory were otherwise applicable, it would fail, since the State's alleged change of position with respect to the effect of the certificate on rate base treatment is based on legal theories.

45. In addition to legal barriers that prevent acceptance of PP&L's argument, the factual record in this case does not support PP&L's claim that, in constructing Colstrip 3, it reasonably relied on the "promise" that rate base treatment would be afforded on demand. In fact, the record strongly suggests just the opposite.

46. The Commission has traditionally disallowed rate base treatment for investment in plant that was not yet completed. Such investments are labeled "construction work in progress" or "CWIP. " PP&L has not challenged the Commission's exclusion of these investments in PP&L's prior rate applications.

47. Additionally, during the 1981 Montana Legislative Session, PP&L, along with the Montana Power Company, supported House Bill 395. HB 395, if passed, would have explicitly required the Commission to provide regulated utilities with rate base treatment for CWIP.

48. This brief history of PP&L's action indicates that it has not relied upon BNR's issued certificate throughout the construction period for Colstrip Unit 3. Had PP&L actually consistently so relied, it would have challenged the Commission's exclusion of CWIP, and HB 395 would not have been necessary. Since PP&L's Motion to Strike theory requires

rate base treatment for every dollar of investment after issuance of the BNR Certificate, whether the plant facility is completed or not, PP&L's actions have been inconsistent with its theory.

Collateral Estoppel

49; PP&L contends, as did MPC in its Docket No. 83.9.67 Motion to Strike, that "the doctrine of collateral estoppel precludes the Commission from inquiring into the need for Colstrip Unit 3. " (Memorandum, p. 5). PP&L argues that collateral estoppel prevents the Commission from making any determination involving the PSC's "used and useful" statute. 69-3-109, MCA.

50. To make its collateral estoppel argument, PP&L contends that the "need" question that BNR is statutorily required to determine prior to plant construction, is identical to the "actually used and useful" determination made by the PSC after a plant is constructed. The Commission does not find such contention persuasive.

51. Both PP&L and MCC agree that the four-part collateral estoppel test contained in Stapleton v. First Security Bank, _Mont , 635 P.2d 83, 38 St. Rep. 2015 (1983), applies here:

1) The issue must be the same and must relate to the same subject matter;
2) The subject matter of the action must be the same;

3) The parties or their privies must be the same;

4) The capacities of the person must be the same in reference to the subject matter and to the issues between them.

52. PP&L contends that the first and second criteria are met in this Docket, i. e. the issue is the same and must relate

to the same subject matter, because the issue and subject matter is "whether there is a need for the power generated by Colstrip Unit 3." (Memorandum, p. 6).
MCC, on the other hand, argues that "[t]he issues before BNR and the PSC have been rendered separate and distinct by the changed factual situation," and that Copeland's "testimony relates to the traditional how and when considerations concerning rate base which are solely within the province of the PSC and have not been considered appropriate to the function of the Board. " (MCC Response, pp. 10-11).

53. As to the first and second criteria, the Montana Supreme Court has stated that the "precise question" must have been litigated in the prior action before the doctrine of collateral estoppel will be applied. Stapleton v. First Security Bank, Mont , 675 P. 2d 83, 40 St. Rep. 2015 (1983), quoting Gessel v. Jones, 149 Mont. 418, 427 P.2d 295 (1967) . No detailed analysis is needed to conclude that the issue presented to BNR and the Montana Supreme Court in BNRC v. Northern Plains Resource Council, 83 Mont. 540, 601 P.2d 27 (1979), is very different than that presented to the PSC in this case. Contrary to PP&L's assertion, the ultimate issue and purpose of the inquiry of the BNR is very different than the PSC's. BNR is charged with the duty of reviewing energy forecasts to determine if there is the need for a plant such that whatever environmental impacts are caused by it are justified. The nature of the determination is to allow or disallow construction of any energy facility. By contrast, the issue and purpose of the PSC's inquiry is to determine whether a particular utility investment will actually serve and actually benefit ratepayers to require the investment be allowed into the utility's rate base. BNR makes a build/no build decision; the PSC makes a pay/no pay decision. The question of whether or not Colstrip 3 is presently surplus, is actually used and useful could not have been raised in BNR v. NPRC, supra, since Colstrip 3 construction had not even begun. The issues involved in the two determinations are not precisely the same; they are not even similar.

54. As MCC's Response acknowledges, the doctrine of collateral estoppel is related to the doctrine of res judicata, although more limited in scope. As MCC explained, in quoting from Professor Kenneth C . Davis' article, "Res Judicata in Administrative Law, " 25 Texas Law Review 199:

Courts normally apply laws to past facts which remain static - where res judicata operates at its best - but agencies often work with fluid facts and shifting policies. (Response, p . 5)

The PSC agrees with MCC that the regulatory process cannot be frozen in time. One of the primary reasons for having administrative agencies regulate public utilities is to enable the state to respond to changing circumstances. The business world for both regulated and unregulated enterprise is dynamic. From the view of sound public policy, freezing one part of the process makes no sense, and the PSC does not believe such a result is required by Montana law. Indeed such a result is not allowed.

55. As to the third and fourth criteria, PP&L alleges that "the Commission is in privity with the BNR, because the BNR was acting as the representative of the State of Montana. " (Memorandum, p. 6) Concerning the status of MCC, PP&L also contends that "although certain parties to this proceeding were not parties in the certification proceeding and its appeal, they are also bound by the prior proceedings because they are citizens or residents of Montana and the State represented them in the litigated resolution of an essentially public question -- the need for Colstrip Unit 3. " (Id., p. 6). PP&L is essentially contending that every interest and every person in the State of Montana was represented during the BNR hearings and in subsequent judicial proceedings. This contention is made even though MCC did not participate in either the hearings or the proceedings, and though the PSC did not participate in the

judicial proceedings.

56. The Commission finds PP&L's allegation supports, rather than opposes, the conclusion that the doctrine of collateral estoppel does not
apply in this instance.

57. The Montana Consumer Counsel, a constitutionally created entity, has "the duty of representing consumers interests in hearings before the Public Service Commission. . . " Montana Constitution Art. XIII, '2. The Consumer Counsel is not included under the Siting Act provisions as one of the state agencies to be copied with a certificate application, nor is it required to report to the Department of Natural Resources and Conservation concerning how the proposed plant site affects MCC's area of expertise. 75-20-211, MCA and 75-20-216(5), MCA.

58. The Commission cannot accept PP&L's allegation that the concerns of the consuming public MCC is required to represent were addressed, let alone represented, by any party at the BNR hearings, or during the judicial determination concerning the BNR decision.

By definition the Consumer Counsel is only to represent the consuming public in matters that come before the PSC, not the BNR. Obviously, the MCC would not have been involved in the BNR deliberations because the BNR was not considering the issues that are involved in the usual PSC proceeding, i. e. the consideration of a utility's application to raise rates. Appropriately, the MCC has participated and represented the consuming public's interest in this Docket - PP&L's request to raise rates.

59. The Commission, a statutorily created agency, has the duty to decide whether a utility's investments should be included in the rate base upon which the rates charged to consumers are determined. Such issues are not included in the

areas that the BNR is required to consider under the

60. The Commission does not find that the Commission is collaterally estopped from making an "actually used and useful" determination, nor that the MCC is collaterally estopped from addressing such issue in presentation of its evidence in a rate hearing.

PART C

EXCESS CAPACITY

Background

61. With this application, PP&L has asked the Commission to allow it to add its full investment in Colstrip Unit No. 3 to its rate base. PP&L is a partner in the Colstrip Project and owns a 10 percent share of Colstrip Unit 3, or approximately 70 megawatts of capacity. If PP&L's request were to be granted, Montana's allocated share of the associated rate increase would be approximately $766,000.

During the hearing in this Docket, PP&L witness Stephen Pearson explained that Montana's allocated share had decreased from the $776,000 rate increase request contained in PP&L's original application to $766,000. The decrease was the result of PP&L's update of the Colstrip revenue request to the actual January closing figures, and the use of applicable costs from PP&L's 1982 general rate case. (Tr. p. 14).

62. The Commission, in assuring that rates are just and reasonable, must carefully and independently scrutinize major additions to a utility's rate base. Under Section 69-3-109, MCA, the Commission, in order to establish reasonable rates, must determine the value of PP&L's investment in the Colstrip Unit No. 3 plant that is "actually used and useful for the convenience of the public.

Prudence

63. In this Docket, PP&L has contended that it is entitled to recover from Montana ratepayers its investment in Colstrip Unit No. 3 and related facilities, because PP&L's decision to invest in the plant was prudent. The Commission finds that it is not necessary to make any determination regarding the prudency of PP&L's participation in the Colstrip No. 3 project.

64. As the Commission explained in Order No. 4975, Docket No. 82.7.53, PP&L's Abandoned Nuclear Projects case:

. . .the standard set forth by the legislature and applied by the Commission is whether the projects are used and useful and not whether PP&L was prudent in participating in them. Had the legislature intended to allow utilities to recover from ratepayers all of their "prudent" investments rather than only those investments that are "actually used and useful" it could easily have substituted "prudency" language for the "used and useful" language in 69-3-109, MCA. (Docket No. 82.7.53, Order No. 4975, Finding of Fact No. 21)

65. In this Docket, unlike Docket No. 82.7.53, the utility plant in question, Colstrip Unit 3, is in commercial operation . The Commission, however, must apply the same "used and useful" standard contained in 69-3-109, MCA, to determine whether PP&L is entitled to include its Unit 3 investment in rate base.

66. A utility's rate base consists of discreet investments that a utility has made to serve its customers. In determining whether a particular investment should be included in a utility's rate base, the Commission must examine whether that investment provides service that benefits the utility's current ratepayers .

Firm Sales Normalization Adjustment

67. This Commission has continually been concerned with the

amount of excess or surplus generating capacity that is present within PP&L's electric system. In the January, 1983 Order No. 4928a, for Docket No. 82.4.28, PP&L's Electric Rate Increase Application, the Commission put PP&L on notice that the PSC in the future would "consider disallowing excess generating capability in the rate base, thus allowing the stockholders of PP&L to experience the cost of subsidizing off-system sales losses. Another possible approach would be to allow the excess in the rate base and impute revenues to off-system sales equal to PP&L's Long-Run Incremental Cost or the full revenue requirement of existing thermal facilities. " (Order No. 4928a, Finding of Fact No. 52.)

68. In the last two PP&L Dockets, the Commission has ordered PP&L to make a firm sales normalization adjustment that assumes that any firm surplus can be sold by PP&L at 36.44 mills.

In its reply brief, PP&L contended that the MCC had not distinguished this Docket from prior PP&L dockets, therefore, the Commission is again compelled to address PP&L's excess capacity through the use of a firm sales normalization adjustment.

69. Any addition of new plant capacity requires careful scrutiny by the Commission. In this Docket, the Commission finds that Colstrip Unit 3's 70 megawatts are a significant addition of new plant capacity to a system which already has substantial excess, and constitute a discreet plant investment.

70. The fact that the Commission has allowed PP&L to use a firm sales normalization adjustment for its excess capacity in prior dockets does not preclude the use of a different ratemaking treatment now or in the future. To accept PP&L's contention would mean that once the Commission decides to use a particular ratemaking method for a particular area in one docket, the Commission must continue using that method in

subsequent dockets. Such an argument flies in the face of administrative law. An administrative agency, by its design, is created to enable government to be responsive to changing facts and circumstances.

71. As discussed below, the Commission finds that the Colstrip Unit 3 plant addition, does require a different ratemaking treatment to reflect a fair sharing of costs and risks between stockholders and ratepayers; the Commission finds that the 70 megawatts of Colstrip Unit 3 capacity is excess and should be disallowed in rate base. The Commission has clearly given PP&L notice that its system excess would continue to be reviewed, and that various ratemaking treatments could be used to address the situation.

72. MCC witness Copeland indicated that the entire output of PP&L's Colstrip 3 share (70 MW) is excess capacity. In his testimony (Exh. A, pp. 9 & 10) he explains why the plant is excess:

Colstrip No. 3 will add 70 MW to PP&L's inventory of power resources. Colstrip No. 3 is not required now or in the near future to meet PP&L's peak load requirements or maintain necessary reserves. PP&L' already has substantial excess capacity, Colstrip No. 3 will merely add to this excess. Since it is not needed to meet PP&L's peak load requirements or to maintain necessary reserves, it is not used and useful.

Q. On what do you base this conclusion?

A. I base this conclusion on two basic sources of information. The first is PP&L's Power Resources Department's own current forecast of loads and resources. Exhibit (BLC-1) summarizes the pertinent data from this forecast for the operating years 1983-1990. Over this seven-year period, PP&L projects an average of 369.1 MW of capacity above load and required reserves.

It is apparent that neither Colstrip No. 3, nor No. 4, will be required to meet projected load or required reserves. The Colstrip units thus represent excess capacity relative to projected load and reserve requirements.

The second source of information leading me to conclude that Colstrip is excess capacity is the Company's aggressive efforts to sell its interest in the plant, as discussed in the testimony of Mr. Watson supplied in response to Staff's request for testimony which supports the need for the power generated by Colstrip No. 3. The Commission, in evaluating the issue of excess capacity, is concerned with the balance of loads and resources in the test year. The Commission questioned Mr. Steinberg on this point:

Q. Mr. Steinberg, can you tell me what the surplus of energy system wide is for the test year that's being used in this docket?

A. Under the firm power sales normalization procedure that was adopted by this Commission for rate-making purposes, that firm sales normalization adjustment, if you will, enables us or forces us or requires us to dispose of approximately a 109 average megawatts of energy during the test period assuming Colstrip. Forty-two hour megawatts of that is of Colstrip. The remainder has to do with changes in system loads and changes to our firm resources during the test period. (Tr. p. 159)

Based upon this answer by Mr. Steinberg, it is clear that there is excess capacity on an energy basis in the test year. The Commission takes note of the fact that 42 MW of the excess come from Colstrip 3 at a 60 percent capacity factor. Use of a higher plant capacity factor would produce an even greater level of excess capacity on the PP&L system.

73. Looking beyond the current test year, Company witness Watson provided testimony which supported the contention of Copeland regarding the continuation of a system surplus:

Q. In discussing your activities that the Company is undertaking to try to bring loads and resources into closer balance, do you have any projection of when you're going to get those loads and resources into a fairly close balance?

A. I have a lot of projections. I think our latest load forecast, which didn't take into account a lot of things that we've been doing here lately, said that loads and resources would come into balance in the early 90's. (Tr. p . 332)

74. After a careful review of the record, the Commission finds no evidence to support the idea that PP&L is not in a condition of excess capacity. Not only is there an excess of energy in the test year, the loads and resources of the Company will not be in balance for the rest of this decade based upon current estimates. Having found that the Company has excess capacity, the Commission examined the alternatives presented by the Company and MCC.

75. PP&L in its filing assumed that the excess power from Colstrip 3 was sold off-system at the rate of 36.44 mills, and those revenues were then used to reduce the rate increase caused by adding the plant to the rate base. This treatment is consistent with the method of treating surplus power in Docket No. 83.5.36, Order No. 5009a.

76. Copeland, in his testimony, proposed four options that the Commission could use to treat PP&L's excess capacity:

1. Exclude the capacity from rate base and dismiss the application.

2. Exclude the capacity from rate base but allow the Company to continue to capitalize its cost of capital on the excluded investment until such time as that investment is needed
to serve jurisdictional load.

3. Exclude the capacity from rate base but allow a partial capitalization-of capital costs, with a disallowance of the equity component of the Company's capital costs.

4. Allow the capacity in rate base but allow only partial capital cost recovery in current rates, but disallowing the equity component cost of capital. (Exh. A, pp. 14 and 15)

77. Copeland testified that he preferred the Commission adopt Option 1, or in the alternative, Option 3.

78. Watson, in his rebuttal testimony, expressed concern with adoption of any of the alternatives proposed by Copeland. Option one should be rejected according to PP&L because the possibility of disposing of all output through off-system sales opportunities is small and fixed costs would have been higher if the plant was placed in service at a later date. In Watson's opinion, options two and three represent a one-sided taking of benefits without compensation and should not be seriously considered. Option four ignores the real costs of money and should not be adopted.

79. In its opening brief, PP&L argues that Copeland in defining excess capacity failed to distinguish between regulated and nonregulated enterprises. PP&L, in its argument on this point, has lost sight of the purpose of regulation. In exchange for the right to provide a monopoly service, the utility is subject to regulatory control. The purpose of regulation is to replicate, as closely as possible, the

competitive market. To argue, as PP&L does, that a utility in a surplus condition should be allowed to add still more generation to rate base, is exactly opposite of a competitive market.

80. The Commission finds that the past practice of inputting off-system sales to dispose of surplus is not appropriate in this case. The levelized cost of Colstrip 3 is 65 mills compared to the sales price of 36.44 mills . While the Commission agrees with PP&L that this method represents a sharing of costs, it increases rates to add power which is not needed to serve jurisdictional customers. The Commission cross-examined Watson on the spread between the Black Hills Power and Light Company contract (see Finding of Fact No. 116 et seq.) and the cost of energy from Colstrip 3:

Would it be safe to say that one of the things that is at issue here is the difference between the 37 mills that you've indicated for Black Hills Power and Light contract and the 65 mills that you've indicated for the Colstrip 3, cost of energy, who's paying that? (Tr. p. 105)

81. Based on both PP&L's and MCC's testimony, as presented in this Docket, the Commission finds that PP&L's 70 MW portion of Colstrip Unit 3 constitutes excess capacity, is not "used and useful," and therefore, PP&L's investment in the Unit should be excluded from PP&L's electric utility rate base .

Marketing Efforts

82. The Commission's conclusion that PP&L has substantial excess capacity on its system is further supported by PP&L's marketing efforts to eliminate various amounts of capacity.

83. Beginning in early 1983, PP&L attempted to eliminate its 10 percent share or 70 MW of Colstrip Unit 3 through an asset sale of its share. The Colstrip Project ownership agreement

required PP&L to give the other Colstrip owners the opportunity of first refusal on the proposed asset sale. Of the owners, only Puget Sound Power and Light Company was interested, but Puget was unable to purchase the asset due to its own financial difficulties .

84. PP&L then offered its 10 percent share to Black Hills Power and Light Company, as a proposed asset sale, but Black Hills was also unable to purchase the share due to financial problems and operating reasons.

85. PP&L next attempted to negotiate a long-term power sale, and successfully completed such a sale agreement for 75 MW with Black Hills effective January, 1984. (The Black Hills Agreement is discussed in detail in Finding of Fact No. 116 et seq.)

As additional support for his excess capacity finding, Copeland cited the Black Hills Agreement as further evidence "that capacity from Colstrip is excess with respect to PP&L's system load and resource obligations." (Exh. A, p. 10).

86. During cross-examination, PP&L witness James Watson was asked whether PP&L would still have considered a long-term system sales to Black Hills Power and Light Company if PP&L had either made an asset sale of Colstrip Unit No. 3 or if Unit No. 3 had, for whatever reason, not come on line. Watson replied:

In the position we were at that time when the deal (Black Hills Agreement) was negotiated, I think we would have still been looking at firming something up for a period of time. I'm not really sure if we would have put the deal together for 40 years if we had other options. (Tr. p. 333)

* * * *

standing at the point in time that the negotiators were asked, I think that we would have still been looking at 75 megawatts or maybe even a little bit more. Now, the more that we would have been able to sell or willing to sell, I think we would have started looking at shortening up the term. (Tr. p. 334).

87. In February, 1984, PP&L and other Northwest Region electric utilities received solicitation letters from the Bonneville Power Administration wherein BPA asked the utilities if they were interested in having BPA act as an agent for them in trying to market surplus power outside the region.

88. PP&L responded in March, 1984 to the BPA letter providing four acceptable power sale options that BPA could offer to power purchasers outside the region.

The options were discussed during Consumer Counsel Paine's cross-examination of PP&L witness Steinberg: ;

Q. Looking at alternative number 1, Pacific would offer up to 150 megawatts for a period between 10 and 15 years of firm power if BPA combined with that, over the same period of time, 100 megawatts; is that correct?
A. That's one of the options. That's alternative number 1. " (Tr. p. 41)

Q. Fine. Alternative number 2 under that scenario, Pacific would be willing to offer 400 average megawatts for a period of 5 years if it were combined with 400 megawatts of either peak or energy from BPA for an additional period of 10 years to complete what's called a 15-year package; is that correct?

A. That's correct. That's what's stated.

Q. Alternative number 3 assumes that Pacific would be

willing to offer up to 140 megawatts of unit power of Colstrip Unit numbers 3 and 4; that power will be combined with an amount of either BPA or British Columbia power or a combination of the two and sold for a period of up to 15 years; is that correct?

A. That's a direct quote.

Q. Alternative number 4 under that scenario, Pacific would offer any of the alternatives that I've discussed, 1 through 3, combined with an exchange provision providing for coverage in the event of adverse water conditions; is that correct?

A. Yes. (Tr. p. 43)

Later, during the hearing Watson indicated that certain conditions are attached to PP&L marketing surplus power through BPA:

A. Before we go through each alternative, I think it's very important to set the stage as to what Bonneville would have to do for Pacific; and that's shown on page 2 of the same document. One of the things is we're looking for them to make a firm commitment to make available to us a thousand two hundred to sixteen hundred megawatts capacity through the end of the century. The other thing is that they would have to make a commitment for long-term firm obligations by Bonneville consistent with our long-term firm obligations.
As a third item, we've also asked them, made this whole offering contingent on this, that we get a higher priority for the secondary to help us with risk management. Now, given that underpinning that Bonneville has
to make some commitments to us, then before options or alternatives are, let's say, somewhat in the ballpark with the caveat that if, in fact, we're successful in

other areas, we can terminate or modify any of the options with 24 hours written notice, Bonneville as well as the idea that the term of the offer extends for a period of a maximum of 6 months.
With those caveats, I'd be willing to discuss each of the three or four alternatives. (Tr. pp. 42 and 43)

There is no question that PP&L has a substantial amount of excess capacity. The Company is acting in a rational manner in attempting to take advantage of future firm sale opportunities. Watson testified at the hearing that 250 megawatts could be sold (Tr. p. 48).

89. These marketing efforts by PP&L are strong evidence in and of themselves that the Colstrip Unit 3 capacity is excess and is not needed by PP&L customers. PP&L contends, however, that even though it has marketed capacity and is looking to market even more, Colstrip Unit 3's capacity is still "used and useful," and should be rate based.

90. The arguments that PP&L has made to support its own finding of "used and useful" for Colstrip are discussed below.

Economic Dispatch

91. One of PP&L's rationales for its conclusion that Colstrip Unit is "used and useful" is the fact that since January, 1984, PP&L has, at times, used its Unit 3 power instead of power from its Centralia and Jim Bridger plants. This operational decision is based on the fact that Colstrip Unit 3's variable running costs are cheaper than those two plants.

92. PP&L is thus operating its electric system in accordance with the generally accepted principle of economic dispatch. This principle can be defined as a utility's decision to operate a generating plant with the cheapest variable operating costs, whenever possible, before operating plants

with higher variable operating costs. Obviously the principle ignores the fixed costs of the plants in making a decision to operate one plant before the other.

Since Colstrip Unit 3 is being operated pursuant to economic dispatch, PP&L contends that Unit 3 is therefore "used and useful," and its investment in the Unit must be rate based.

93. The principle of economic dispatch ignores the basic fixed investment costs of a plant, costs which are of primary concern in a determination of whether that investment should be included in rate base. Even though PP&L emphasized that Colstrip Unit 3 has lower variable costs than two of PP&L's other plants, thus resulting in power expense savings, the fact remains that PP&L has asked the Commission for a $766,000 increase to cover the expenses of including Colstrip Unit 3 in rate base.

94. PP&L's contention ignores the fact that the Commission must look to whether or not a utility's investment in plant energy capability is "used and useful." If, as PP&L contends, all a utility has to show the Commission to prove the plant is '!used and useful" is that the plant in question has had its "on" button pushed, and is generating power, the utility, rather than the Commission, would be determining whether an investment is included in rate base. The utility would simply make an operational decision to activate the plant's "on" button, and the utility's plant investment would have to be rate based.

95. PP&L witness Watson also contended that Colstrip Unit 3 is "used and useful" because "in the short-term from an operational standpoint, Colstrip will lower the Company's cost of service by allowing wholesale power sales. . . ". (Exh. 10, p. 5).

96. If the Commission did allow Unit 3 into rate base, PP&L's

cost of service would necessarily increase. For PP&L to state-that wholesale power sales, i.e. off-system sales, will lower the Company's cost of service ignores the simple fact that the total cost of service would be greater if Unit 3 is rate based than it would be if the Unit were excluded. Since the Commission has found Unit 3 not "used and useful, " PP&L's cost of service does not increase to reflect the Unit, therefore, PP&L's ratepayers will not pay increased rates. The Commission's exclusion of the Unit 3 investment from rate base allows PP&L to dispose of the Unit's capacity through off-system sales. In the future, if PP&L can show that the Unit is then "used and useful," it can also again apply to the Commission for rate base treatment of its investment.

97. The Commission, at the time a plant is requested by a utility to be added to the rate base, must decide whether the plant is used and useful. In addition to whether or not the output of the plant is needed, there are other issues; the reasonableness of the costs of the plant and the total cost per KW generated by the plant. After all of these factors have been considered, it is the Commission that makes the decision about how much of the plant, if any, is added to rate base.

System Reliability

98. PP&L has also claimed that all of Colstrip Unit No. 3's generating capacity is "used and useful, " because it adds reliability to PP&L's system. Specifically, Mr. Steinberg stated in his direct testimony that Unit No. 3 had been used during the week of December 18-24, 1983 when PP&L's system and its Montana's service territory set new peak demand records.

99. The reliability of the system during the week of December 18-24, 1983, was enhanced due to Colstrip 3 being on line, according to Steinberg. This line of argument is not persuasive to the Commission. In the first instance, the

Company does not plan on the basis of colder than normal weather. Next, it is illogical to imply that Colstrip 3 is being added to the system to meet peak. The fact that Colstrip 3 is a baseload energy plant is not in question. Lastly, on the point of reliability during this period, it is well known that the region had peak surplus during the period. Therefore, the reliability issue is not germane.

100. The Commission finds any reliance upon the extremely cold weather in this period to show the need for more resources to be unjustified. In evaluating loads and resources, both the Company and the Commission rely on the concept of normalization. MCC cross-examined Steinberg on this subject:

Q. Mr. Steinberg, the October of '83 load resource study of the Company, I'd like to focus on that for a little bit. Could you tell me if that assumes what I might call normal weather?

A. Yes, it does.

Q. Let's put it this way, you normally experience your peak on a winter day; is that correct?

A. Yes, sir.

Q. The resource load study would assume what I guess I could call a normal cold weather winter?

A. With regard to peak demand, the peak that we used is an expected value, that is, the probability of exceeding that is 50% and the probability of it being lower is also 50%.

Q. With the change that you have made on page 4 of your testimony, are you now saying that without considering the California firm sale, the actual realized peak was

some 303 megawatts over and above the projected peak?

A. For what year?

Q. The '83/'84 operating year.

A. Yes.

Q. The 200 megawatt firm sale to California is included in the Resource Load Study of October, '83, is it not?

A. Yes, sir, it is.

Q. I guess to be more precise, it was some 503 megawatts over what was projected to occur?

A. Yes.

Q. Can you quantify how much of that can be attributable to colder than expected weather?

A. I don't have the precise analysis, but I would imagine that a goodly portion of it would be due to the extreme cold temperatures. (Tr. pp. 350, 351)

101. Reliance on weather conditions which were dramatically colder than normal is inappropriate, given the importance and reliance attributed to normal weather conditions in the ratemaking process.

Peak Resources and Loads

102. PP&L also contended that Copeland's conclusion that Colstrip Unit No. 3 is not "used and useful," based on his finding that PP&L's projected peak resources exceed projected peak loads, should be discounted. Copeland stated that, under the Pacific Northwest Coordination Agreement's reserve requirements, PP&L's peak resources exceed peak loads and

peak reserve requirements. PP&L's Steinberg criticized Copeland's use of the Agreement's reserve requirements because "the reserve requirements specified by the Agreement should not be used as the exclusive measure of excess capacity since they exclude load forecast uncertainty and system operation considerations. " (Exh. 13, p. 4). It is true that Copeland relied on only one form of reserve requirement which was provided to him by the Company. The Commission is satisfied that the reserves required under the Pacific Northwest Coordination Agreement are more than adequate. In future cases, the other reserves mentioned by Steinberg should be fully explained and quantified.

AFUDC Treatment

103. During the Colstrip Unit 3 construction period, the Commission has allowed PP&L to accrue AFUDC. The basic function of AFUDC treatment is to fully compensate a utility's investors for providing capital during a plant's construction period in advance of receiving a return when a plant is completed. Pursuant to Accounting Order No. 5028b in this Docket, the Commission allowed PP&L to continue to accrue AFUDC on Unit 3 and related facilities after the January 10, 1984 commercial operation date for the Unit, pending the Commission's final decision in this Docket.

104. With the conclusion that the Colstrip Unit 3 capacity is not "actually used and useful, " the Commission finds that AFUDC treatment is not appropriate in this Docket. This conclusion rests both with the testimony in this Docket, and in the Commission's own experience with the Montana-Dakota Utilities Company (MDU).

105. In MDU's Docket No. 81.1. 2, the Commission afforded AFUDC treatment for MDU's investment associated with the Coyote plant, that was excluded from rate base. No party opposed the AFUDC treatment in that Docket.

106. The Commission's experience with MDU suggests that the utility was better off with AFUDC treatment, than it would have been if rate base treatment of the plant investment had been afforded. In ratepayer terms this meant that ratepayers paid more for AFUDC treatment than they would have if rate base treatment had been afforded. The Commission does not believe that the "actually used and useful" standard is intended to achieve such a result.

107. In responding to questions regarding Docket No. 81.1.2, MCC witness Copeland disagreed with the Commission's AFUDC treatment of the Coyote plant, stating that such treatment "does not actually involve a sharing of costs between investors and ratepayers; in fact investors fully recover their costs. " (Exh. A, p. 21)

108. In this Docket, MCC witness Copeland opposed affording any AFUDC treatment to PP&L, if the Commission found that Unit 3 should be excluded in its entirety from rate base, i.e. if the Commission accepted Copeland's Option 1 As Copeland explained in his direct testimony:

Ordinarily, any revenues received from off-system sales are credited to the cost of service. Under Option 1, however, these revenues would flow to the benefit of the firm and its investors. Thus, under this Option, all the risk and all of the return from the marketing of capacity not required to meet jurisdictional load inures to the firm and its investors. This is an appropriate application of, the principle that the right to gain follows the risk of
loss. (Exh. A; p.l5)

109. When a utility's stockholders choose to invest in a plant, they take the risk that their plant investment might not be included in rate base, i.e. that the Commission may find that the investment is not "used and useful."
When the Commission makes such a finding, as it has in this

Docket, the utility then can dispose of the particular plant's capacity in whatever way it can. If PP&L is able to market Unit 3's capacity through off-system sale,- then PP&L and its stockholders will reap all the revenues generated from those sales.

110. PP&L's ratepayers, on the other hand, also run risks. If PP&L's Unit 3 plant investment had been found "used and useful," PP&L ratepayers would pay increased rates to cover the costs of that investment. If, as in
this Docket, the plant investment is found to be not used and useful, PP&L's ratepayers run the risk that if PP&L is able to generate significant amounts of revenues from disposal of the plant's capacity, none of those revenues will be used to reduce PP&L's cost of service to the ultimate benefit of the ratepayers.

111. PP&L has argued that Copeland's Option 1 is "an unreasonable and logically inconsistent proposal given that his major premise is that the Company has excess capacity. If the Company does have excess capacity, the possibility of disposing of all output through off-system sales opportunities is small. " (Exh. 12, p. 4)

112. The Commission is very much aware of the existing Northwest Regional power surplus and the market reality for off-system sales. PP&L has, however, by its own testimony in this Docket, made it very clear that it is pursuing numerous avenues to market its excess. Whether or not these efforts are successful, ~t still remains that it is the stockholder who has 'taken the risk of whether his investment in plant capacity will be recouped. If the efforts fail, the stockholder takes a loss; if the efforts are successful, the stockholder stands to make a significant gain on his investment.
The Commission also reminds PP&L that the Commission finds that PP&L has significant excess on its system, even with the elimination of Colstrip's 70 MW. The Commission is continuing

to allow PP&L to continue to receive the benefits of a firm sales normalization adjustment for that remaining excess. As stated in Docket No. 82.4.28, the Commission will continue to review PP&L's excess capacity situation.

113. PP&L has also contended that "since system sales for resale are not assigned to a specific plant, Option 1 is untenable and unworkable." (Exh. 12, p. 4) Again PP&L ignores the fact that the Commission considers a utility's investments as discreet separate investments, for which the Commission must determine, one by one, whether or not the investment is "used and useful."

While PP&L may choose to market its excess as a system sale, rather than as a Colstrip power sale, it is not unreasonable for the Commission to assume that PP&L is able to assign costs and revenues to off-system sales. Such allocations could be presented by PP&L in its next application for consideration by the Commission.

114. Further PP&L alleges that Option 1 "implies that the recovery of Colstrip fixed costs would be delayed with no recognition of how much higher fixed costs would have been if the plant were placed in service at a later date. " (Exh. 12, p. 4)

Obviously given that the Commission has found that Unit 3 is not "used and useful, " the fixed costs associated with the Unit will not be recovered by PP&L through increased rates. Whether or not PP&L is able to recover the Unit's fixed costs through the marketing of the capacity will depend on PP&L's success in making off-system sales.

115. Since the Unit is not "used and useful," PP&L cannot expect that the Commission will allow it to accrue AFUDC to recover costs associated with a Unit that is not providing service to PP&L's ratepayers.

PART D

BLACK HILLS POWER AND LIGHT COMPANY
POWER SALES AGREEMENT

116. PP&L entered into a Power Sales Agreement (Agreement) with the Black Hills Power and Light Company (Black Hills) to sell and deliver 75 MW of capacity and associated energy to Black Hills for a period of 40 years. PP&L was able to enter into such a long-term supply agreement due to its current excess power supply situation. Black Hills entered into the Agreement because the power to be supplied would allow Black Hills to defer construction of its planned 75 MW generating plant. The Agreement became effective as of January, 1984.

117. On February 14, 1984, PP&L representatives met with the Commission to explain the Agreement, and to seek "comfort" from the Commission concerning whether or not the Commission would find the Agreement beneficial to Montana ratepayers. PP&L sought this long-term Agreement with Black Hills in order to firm up a portion of its power supply surplus. The Commission informed PP&L that it would formally consider the Agreement as part of this Docket No . 83.10.71, and issued a " Notice of Commission Action" dated March 1, 1984 so informing the parties.

118. The Agreement is an interstate wholesale firm power sale for resale by PP&L to Black Hills, and as such is subject to the pricing jurisdiction of the Federal Energy Regulatory Commission (FERC). In April, 1984, the FERC approved the Agreement's pricing mechanism which used Colstrip Unit 3, PP&L's highest cost generating plant, as the pricing basis.

119. In his Rebuttal Testimony, PP&L witness Watson summarized the basic provisions of the Agreement which:

. . calls for purchase of 15 MW of capacity in 1984, increasing by 15 MW each year to 1988, at which time the purchase is 75 MW per year for the remainder of the 40 year term. The annual load factor is limited to a range of 40 to 80 percent. The pricing for the first four and

one-half years reflects current market surplus realities. The estimated rates per kilowatt hour, assuming an 80 percent load factor, are 37 mills, 67 mills, and 94 mills in 1984, 1990, and 2000 respectively. The price for the first four and one-half years exceeds the Company's current FERC authorized wholesale rate and a FERC filing relative to the contract has been made. (Exh. 12, PP. 7, 8).

120. The Commission is fully aware of the Northwest Region's power surplus, and the difficulties faced by all regional area utilities in attempting to sell their surplus power in what is a buyer's market. In view of that market reality, and in view of PP&L's substantial power surplus, the efforts by PP&L to consummate this firm power agreement are actions that the Commission finds commendable.

121. MCC witness, Copeland, addressed the Black Hills Agreement in his direct testimony stating that such power sale agreements, negotiated during a buyer's market, can cause problems in how the utility spreads the cost responsibility. Copeland stated that this cost responsibility problem exists under the Black Hills Agreement because during the first five years of the Agreement, PP&L recovers only one-half of the Colstrip-equivalent fixed costs. Copeland testified that:

The Company seeks to assign responsibility for the shortfall to its retail ratepayers from wholesale power sales by including all capacity in its rate base and crediting them with revenues received from the sale of excess capacity. If the revenues are inadequate to recover incremental costs, as they are in the case of the Black Hills contract, then retail ratepayers will subsidize the firm for its inability to recover costs in the bulk power market. While it is true that retail ratepayers would be worse off if no sales for resale were made, that is only because the Company seeks to

incorporate all of the excess capacity in its rate base regardless of the level of revenues received from wholesale power sales. (Exh. A, pp. 12, 13)

122. PP&L contends that the Agreement benefits ratepayers because:

The sale allows the Company (PP&L) to increase its firm load immediately, to receive a price above the current market price, to make a sale at a price higher than the Company's filed FERC wholesale rate, and to mitigate future retail revenue requirements. (Exh. 12, p. 7)

123. In its review of the Agreement, the Commission must consider whether the Agreement is beneficial to PP&L ratepayers when the Agreement will not fully recover the Colstrip-based fixed costs for the first five years.

124. The Commission, based upon its analysis of the various proposals for treating excess capacity, finds that no revenue increase is warranted in this Docket. In addition, no carrying charges or AFUDC (See Finding of Fact No. 103 et seq.) are to be accrued due to the large surplus which is expected to continue into the future. Since Colstrip 3 is not used and useful, all revenues from the Black Hills contract should be credited to shareholders to provide a partial return on the plant found to be excess capacity.

125. Since the Black Hills Agreement is the most recent sale of firm power by PP&L, it is a reasonable proxy for the price of a first power contract. There is no evidence that a higher price could have been achieved in light of current market conditions. While the Commission supports the concept of aggressively marketing surplus power, the failure to recover all costs in the early years of the agreement points out the reality of a region which is awash in surplus power.

126. The Commission is very concerned about the elimination

of this expensive regional surplus. PP&L's decision to rely on purchases of BPA surplus, conservation, and co-generation rather than construct new coal-fired generating plants is a positive decision. Reliance on this mix of new resources will hopefully provide adequate resources at a price which reflects the energy competitive market.

PART E
PLANT COSTS

127. With the exclusion of PP&L's investment in Colstrip Unit 3 in this Docket, it was unnecessary for the Commission to make any findings concerning whether the costs associated with the Unit and its common plant facilities were reasonable.

128. In the future, it is possible that the Commission will again be confronted with a request that all of or some portion of Colstrip Unit 3 be included in PP&L's rate base. Should the Commission, at that time, find that any portion of Unit 3 is used and useful, the Commission will have to determine the amount of PP&L's investment in Unit 3 that should be allowed into rate base.

129. The Commission cautions PP&L that it will not accept an application that simply seeks to have PP&L's investment in Unit 3 passed through to ratepayers in a similar manner to a tracker rate proceeding. It is the burden of the Applicant to show the Commission that the costs the utility seeks to have rate based are indeed reasonable. PP&L's reply brief statement that no evidence was presented to question whether any of the common plant facilities costs should be disallowed, suggests that PP&L misunderstands who has the burden of proof.

Further, in view of the Colstrip Project owners decision to delay commercial operation of Colstrip Unit 4 for nine months, should PP&L seek inclusion of Unit 3 prior to that

time, PP&L should address questions concerning rate treatment for the two Units' common plant facilities and transmission lines.

PART F
BPA PASS-THROUGH

130. On October 21, 1983, PP&L filed with the Commission an application for authority to adopt new rates and charges for electric service furnished in the State of Montana. The application provided, in part, for rates estimated to produce approximately $467,000 of additional annual revenue, resulting in a 1.9 percent increase in annual revenues. Rates across customer classes were calculated to rise approximately .086 cents per kilowatt-hour.

131. The proposed increase reflects additional costs of $467,000 to be incurred by PP&L, as a result of Bonneville Power Administration wholesale rates increases which became effective November 1, 1983. PP&L purchases a significant portion of its energy from BPA.

132. On October 31, 1a83, PP&L submitted information to the Commission which resulted in an adjustment to PP&L's revenue request. According to PP&L, the Federal Energy Regulatory Commission (FERC) had not yet approved BPA's requested increase in transmission rates. As a result, the portion of PP&L's BPA pass-through request concerning increased transmission rates was withdrawn by PP&L pending approval of the new BPA transmission rates. The Commission accepted the withdrawal of that portion of the Company's request. When the FERC actually approved new BPA transmission rates, PP&L could then file with the Commission any necessary rate adjustment request.

PP&L further submitted that the resulting adjusted annual revenue increase was in the amount of $322,000 or 1.3 percent. The combined effect of the BPA wholesale rate

increase, and the associated decrease in the Schedule 98 credit resulted in an adjusted net annual revenue increase to total retail sales in the amount of $632,000.

133. On October 31, 1983, the Commission approved Interim Order No. 5028, which granted PP&L interim relief in the amount of approximately $322,000. This amount reflected the exclusion of the BPA transmission rates portion of the pass-through request.

134. On January 30, 1984, PP&L filed with the Commission a rate increase application to reflect the increase associated with the BPA transmission rates previously disallowed by the Commission. PP&L stated that on or about January 25, 1984, FERC approved the BPA transmission rate increase, effective February 1, 1984. This increase will cause the Company's costs, allocated to Montana, to increase by $145,000 or 0.6 percent based on the 12 months ended December 31, 1982.

135. The Company is also proposing to modify the Schedule 98 billing credit to the Company's Montana domestic and rural customers resulting from the Company's Residential Purchase and Sale Agreement (Exchange Agreement) with BPA, authorized by the Pacific Northwest Electric Power Planning and Conservation Act (Regional Act). The proposed Schedule 98 credit is 0.826 cents per kilowatt-hour applicable to Residential Service Schedule 16 customers, and 0.769 cents per kilowatt-hour applicable to qualifying customers served on Schedules 13, 25, 35, 40, and 42. The combined effect of the BPA Transmission Rate increase and the associated increase in the amount of the Schedule 98 credit results in a net annual revenue increase to total retail sales of $82,000 or 0.4 percent. The Commission found that these adjusted Schedule 98 tariff rates are proper, based on that interim proceeding.

136. Since the Commission found that the increased expense is, to a large extent, a known and measurable change and lies

beyond the direct control of the Applicant, the Commission determined that additional interim relief in the amount of $145,000 was appropriate. This reflection of FERC approved BPA transmission rates, on an interim basis, was approved in Interim Order No. 5028, dated February 6, 1984.

137. During the hearing, Mr. Steinberg of PP&L, was cross-examined by Commission staff attorney Ms. Winebrenner:

Q. Earlier, I'd asked Mr. Pearson some questions. First of all, one of the ones that he deferred to you was concerning the BPA pass-through portion in this docket filing. I would like to know what the current status is of the BPA transmission rates that were temporarily approved, it's my understanding, by FERC and that we have granted PP&L in its interim.

A. Yes. In an order dated February 10, 1984, the FERC approved, on the interim basis, the transmission rates for a 4-month period with the proviso that if Bonneville made a compliance filing within four-month period, that the interim period would be extended until the FERC had a chance to review and offer an opinion on Bonneville's filings. Bonneville did make their filing on June 1st, and FERC is in the process of reviewing the filing. (Tr. p. 156)

138. In granting the interim relief with Interim Order Nos. 5028 and 5028a, the Commission determined that PP&L is using correct accounting procedures, pursuant to Commission directive in Order No. 4916, Docket No. 82.6.41, regarding accrued benefits with interest, and deferred implementation of increased Schedule 98 benefits to residential customers. Based on this proceeding, the Commission determined the adjusted Schedule 98 tariff rates to be proper as proposed by PP&L.

139. During this Docket's public hearing, no evidence was

introduced which indicated that the revenues granted for the increase in rates from BPA were not justified. The Commission, therefore, finds making permanent the revenues granted and rates approved in Interim Order Nos. 5028 and 5028a to be proper in this proceeding. However, should the FERC in a final order disallow the BPA transmission rates, which comprise $145,000 of the pass-through portion of this filing, PP&L must accordingly inform the Commission, and rebate this amount along with interest at 13.75 percent, the currently authorized rate of return on equity.

PART G
COST-OF-SERVICE
AND
RATE DESIGN

140. Due to this Docket's overlap with Docket No. 83.5.36, cost-of service and rate design concerns were purposely ignored. The BPA passthrough ($322,000) and the FERC approved BPA transmission rate increase ($145,000) were included, on an interim basis, in the final order in Docket No . 83.5.36 (Order No. 5009a).

141. Subsequent to the Commission's final order in Docket No. 83.5.36, the Commission received several rate inquiries from irrigators. In turn, the Commission staff served rate design data requests upon PP&L witness Ms. Lorie Harris. In response, Harris proposed a separate Agricultural Pumping Service rate schedule (Exh. 11A). At the hearing, Harris testified that the State- of Montana is the only state in PP&L's jurisdiction that had combined Irrigation and General Service customers on to one rate schedule.

142. The Commission finds merit in Harris' proposal to separate, once more, Irrigation and General Service Customers onto two separate schedules. To this end, the Exhibit 11A schedule accompanying her Exhibit No. 9 is accepted. The Company, however, must submit detailed workpapers documenting revenues generated from all schedules.

MISCELLANEOUS

143. Pursuant to staff data request, PP&L was to provide the Commission with its response letter to the Bonneville Power Administration's February, 1984 letter. (See Finding of Fact No. 87 et seq.) Due to antitrust concerns, PP&L requested the response be covered by a protective order. At the hearing, cross-examination was conducted from the response, but the response was not made an exhibit.

The Commission finds that the information obtained on cross-examination during the hearing was adequate for its purposes in this Docket. The Commission will not issue a protective order, and the response will not be made an exhibit in this Docket.

CONCLUSION OF LAW

1. All Findings of Fact are hereby incorporated as Conclusions of Law.

2. The Applicant, Pacific Power and Light Company, furnishes electric service to consumers in Montana, and is a "public utility" under the regulatory jurisdiction of the Montana Public Service Commission. '69-3-101, MCA.

3. The Montana Public Service Commission properly exercises jurisdiction over Pacific Power and Light Company's rates and operations. '69-3-102, MCA,. and Title 69, Chapter 3, Part 3, MCA.

4. The Montana Public Service Commission has provided adequate public notice of all proceedings, and an opportunity to be heard to all interested parties in this Docket. '69-3-303, MCA, '69-3-104, MCA, and Title 2, Chapter 4, MCA.

5. The Montana Public Service Commission must determine

whether Pacific Power and Light Company's investment in Colstrip Unit No. 3 and its related facilities will be "actually used and useful for the convenience of the public. " '69-3-109, MCA. The Commission concludes that PP&L's Colstrip investment is not "used and useful, " and therefore, cannot be included as part of PP&L's rate base. This determination is not precluded by the Major Facility Siting Act, 75-20-201 et seq, MCA.

6. The rate level and rate structure approved herein are just, reasonable, and not unjustly discriminatory. '69-3-201, MCA and '69-3-330, MCA .

ORDER

THE MONTANA PUBLIC SERVICE COMMISSION HEREBY ORDERS:

1. The Pacific Power and Light Company's Motion to Strike is DENIED.

2. The Pacific Power and Light Company's application to increase rates to generate revenues of $766,000 to recover costs associated with Colstrip Unit 3 plant and related facilities is DENIED in total.

3. The Pacific Power and Light Company's application to increase rates to generate revenues in the amount of $467,000 to reflect increased Bonneville Power Administration rates, which were temporarily approved in Interim Order Nos. 5028 and 5028a, are GRANTED and made permanent.

If the Federal Energy Regulatory Commission should rule, however, that the Bonneville Power Administration's transmission rates should be disallowed, PP&L must so inform the Commission, and rebate the amount of $145,000 related to those transmission rates with 13.75 percent interest, the currently authorized PP&L rate of return on equity.

4. All other motions or objections made in the course of

these proceedings which are consistent with the findings, conclusions, and decision made herein should be granted; those inconsistent should be denied.

5. This Order is effective for service rendered on and after the 20th day of August, 1984.

DONE AND DATED this 20th day of August, 1984, by a vote of 3 - 0.

BY ORDER OF THE MONTANA PUBLIC SERVICE COMMISSION.

_____
HOWARD L. ELLIS, Commissioner, Presiding

_____
JOHN B. DRISCOLL, Commissioner

_____
CLYDE JARVIS Commissioner

ATTEST:

Madeline L. Cottrill, Secretary

(SEAL)

NOTE: Any interested party may request the Commission to reconsider this decision. A motion to reconsider must be filed within ten days. See 38.2.4806, ARM.