Service Date: November 24, 1999

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

* * * * *

IN THE MATTER of the Application of	)	UTILITY DIVISION
MONTANA POWER COMPANY for	)	
Approval of its Electric Utility Restructuring	)	DOCKET NO. D97.7.90
Transition Plan Filed Pursuant to Senate Bill 390.	)	ORDER NO. 5986m

ORDER ON MONTANA POWER COMPANY'S DEMONSTRATION OF TRANSITION COSTS AND TIER 2 ISSUES

Background

1. On July 1, 1999, Montana Power Company filed its application with the Montana Public Service Commission for approval of the Tier 2/Generation Sale Issues of its transition plan to customer choice and electric industry restructuring pursuant to Senate Bill 390 (1997), Title 69, Chapter 8, Montana Code Annotated (MCA). The Commission issued Order No. 5986j (Tier 2 Procedural Order), based on a closing date of September 1, 1999 (¶ 2 e) for the sale of Montana Power Company's (MPC) generation assets on July 6, 1999. In Order No. 5986j, the Commission stated that if the sale closing is delayed, the Commission could adjust the dates on its own motion or at the request of parties.

2. On August 30, 1999, MPC informed the Commission that MPC anticipated the closing of the sale of the generation assets to occur in mid- to late October, 1999. At a duly noticed work session on August 31, 1999, the Commission on its own motion suspended the Procedural Schedule on the Tier 2 issues.

3. The Commission further determined that it required briefing of legal issues in the Tier 2 proceeding to forestall problems and legal challenges on the Commission's jurisdiction and implementation of Title 69, Chapter 8, Montana Code Annotated (MCA). The Commission directed the parties to file initial briefs on September 23, 1999, with the opportunity to file reply briefs on September 30, 1999. The briefs were to address whether MPC's proposal for tracking mechanisms after the final order on the transition plan complies with Senate Bill 390, and

whether market power and MPC's revenue requirement are relevant issues that must be addressed in the Tier 2 proceeding.

4. At a duly noticed work session on November 16, 1999, the Commission determined that MPC must amend its transition plan filing on the Tier 2 issues, excluding its accounting mechanisms intended to track and adjust transition costs after the final order. The Commission also determined that revenue requirements and market power are necessary issues in the Tier 2 proceeding to the extent set forth in this Order.

FINDINGS AND DISCUSSION

5. Pursuant to § 69-8-202(1), MCA, a vertically integrated public utility (electric) is required to submit to the Commission a transition plan demonstrating that it satisfies all the requirements in Senate Bill 390. Section 69-8-211(2), MCA requires the Commission to determine the utility's transition costs based on an affirmative showing. The transition costs as determined by the Commission must reflect all reasonable mitigation, and the utility must reasonably demonstrate the net value of its generation-related assets, liabilities and electricity supply costs. Pursuant to § 69-8-211(5), MCA, Commission approval of transition costs and collection of those costs through transition charges settles all transition cost claims.

6. MPC's Tier 2 filing on July 1, 1999 proposed an accounting mechanism to modify transition charges on an on-going basis to reflect future mitigation and changes in market prices. The Commission directed parties to brief the issue of whether Senate Bill 390 requires the Commission to establish once and for all, in the final order on MPC’s transition plan, the amount of transition costs that MPC may recover from its ratepayers. In the briefs, the Commission asked parties to address whether the law allows continuing adjustments to the Competitive Transition Charge after the final order on the transition plan. The Commission also asked whether MPC's Tier 2 filing satisfies the transition cost estimation, mitigation and recovery provisions in Senate Bill 390, and if not, in what way the filing is deficient.

7. Some parties disagree on whether market power and MPC's revenue requirement are relevant issues that must be addressed in the Tier 2 proceeding. The Commission requested that parties brief the issues of market power and MPC's revenue requirement in the context of this proceeding.

SUMMARY OF BRIEFS

8. The Commission received briefs from Montana Power Company (MPC), Department of Environmental Quality (DEQ), Large Customer Group (LCG), Montana Consumer Counsel (MCC), Big Sky Power LLC, and Montana Energy Brokers. MPC also filed a reply brief.

Montana Power Company

9. MPC stated that it proposed tracking and accounting mechanisms as a way of fairly and accurately addressing transition and other costs and revenues that may not be known until after the Commission issues a final order. According to MPC, Senate Bill 390 is flexible enough to accommodate MPC's proposals. If appropriate focus is placed on the "manifest objects" of the statute, one can reasonably fit prospective collection of transition costs into the statutory framework.

10. MPC cited § 69-8-102(3), MCA, which states that the interests of Montana customers must be protected and the financial integrity of utilities must be fostered. MPC asserted that this provision gives the Commission the flexibility to allow ongoing adjustments as necessary to transition costs, and that doing so would provide the best opportunity to protect the interests of both consumers and utilities. According to MPC. § 69-8-211, MCA ties regulatory asset-related and hydro/thermal-related transition costs to the effective date of the Commission's final order, but QF-related transition costs do not need to be fully accounted for. MPC asserted that while § 69-8-211(5) mandates a settlement of transition costs, it does not preclude the settlement from incorporating a collection of costs over time.

11. MPC also maintained that since § 69-8-202(3), MCA allows a utility to waive the requirement for the Commission to issue a final order within 9 months of the utility's transition plan filing, MPC could theoretically waive the requirement for many years. MPC stated that although Senate Bill 390 does contemplate a sale of assets, it does not specifically address multiple closings or the many other issues surrounding its current sale to PP&L Global. MPC recommended that the Commission interpret the statutes in a way that will achieve the social purposes for which Senate Bill 390 was enacted and read Senate Bill 390 in its entirety when gauging legislative intent. MPC stated that there is nothing in Senate Bill 390 that requires it to

have mitigated and determined all transition costs at the time it files its transition plan.

12. MPC asserted that Senate Bill 390 does not require a revenue requirement analysis for the purpose of changing rates. MPC maintained that Senate Bill 390 implements a rate moratorium that freezes rates – rates can neither go up nor go down. Thus, MPC claims that a revenue requirements analysis aimed at changing rates is not needed.

13. MPC stated that market power issues are not legally or factually a relevant issue in its transition plan case. Senate Bill 390 does not require the Commission to analyze market power in the context of a transition plan. The Commission has previously indicated that metering and billing issues will be examined in a Notice of Inquiry. If there are market power issues related to metering and billing, these issues should be addressed in that proceeding. MPC stated that after the sale it would not be able to exert market power in the electricity supply market. PP&L Global and other suppliers are not parties to the transition plan proceeding. MPC does not believe the Commission can intelligently review market power issues without the participation of those who will supply the market.

Large Customer Group

14. Large Customer Group (LCG) stated that Senate Bill 390 requires the Commission to settle all transition cost claims in a final order approving, modifying or denying MPC's transition plan. A Commission determination of the amount of transition costs as part of its approval of a transition plan is fundamental to the purpose of introducing customer choice and developing competitive electricity markets. LCG asserted that MPC’s Tier 2 filing failed to affirmatively demonstrate the transition cost claims associated with the nine categories for which it seeks accounting orders. LCG maintained that the Commission cannot allow the claimed costs if MPC does not prove the amounts in this transition plan proceeding.

15. LCG stated that §§ 69-8-202 and 69-8-211, MCA require MPC to file a transition plan that demonstrates that it has met all the requirements of Senate Bill 390, including an affirmative showing of any claimed transition costs, citing. These statutes then require the Commission to determine those transition costs and issue a final order. According to LCG, nowhere does Senate Bill 390 authorize the Commission to defer its obligation to determine transition costs until some future time or subsequent filing as proposed by MPC. LCG stated that

MPC is asking the Commission to approve a transition plan that does not include a net determination of transition costs and does not settle all transition cost claims.

16. LCG asserted that Senate Bill 390 provides the Commission with flexibility in the treatment of transition costs only narrowly and explicitly with respect to the length of the transition cost recovery periods. LCG observed that the legislature could have, but did not, grant the Commission similar discretion to postpone a determination of what qualifies as a transition cost and the amount of recovery. LCG also noted that Senate Bill 390 specifically prohibits MPC from recovering transition costs through any means not authorized by Senate Bill 390. LCG stated that the Montana Supreme Court has previously concluded that any reasonable doubt as to the grant of a particular power to the Commission will be resolved against the existence of that power. Because Senate Bill 390 does not expressly authorize the Commission to defer a determination of transition costs, LCG asserted the Commission has no power to go beyond the statute at MPC's request.

17. According to LCG, the Commission's determination of transition costs as part of the approval of a transition plan provides the foundation for intelligent customer choice and the development of competitive electricity markets. Uncertainty about the amount of transition costs is detrimental to customers and undermines fundamental objectives of Senate Bill 390. LCG noted that MPC has the burden to affirmatively demonstrate its transition costs, and the value of all generation-related assets and liabilities and electricity supply costs must be reasonably demonstrable and considered on a net basis. § 69-8-211(2)(b), MCA. LCG asserted that all three methods of determining value provided by Senate Bill 390 (market estimation, appraisal, competitive bid sale), whether used alone or in combination, contemplate a fixed and definite valuation. A net valuation is not possible absent a definite determination of the value of both assets and costs.

18. LCG believed that the Commission should include revenue requirement and market power issues in the Tier 2 proceeding. Title 69, Chapter 3, MCA authorizes the Commission to inquire into the reasonableness of MPC's services and charges, and MPC's revenues and costs are relevant to that inquiry. In the Order on Tier 1 Issues (Order No. 5986d), the Commission stated its intent to conduct a later hearing on market power and revenue

requirements. LCG maintained that MPC was aware of the issue and could have requested reconsideration of Order No. 5986d, but did not. MPC may not disregard the requirement of Order No. 5986d after more than a year has passed.

19. LCG stated that market power is both a legal and a factual issue. Senate Bill 390 provides that customers should have the freedom to choose their suppliers of electricity and related services in a competitive market. MPC's generation asset sale does not necessarily remove MPC's ability to exercise market power in markets for a variety of potentially competitive services. LCG asserted that accurate identification of MPC's costs associated with particular services and functions is critical to market power issues, as well as to the reasonableness of the Company's charges for still regulated services.

Montana Consumer Counsel

20. MCC noted that the Commission's Notice requesting briefing cites several provisions of Senate Bill 390 which may be read to require a final transition cost determination in the final restructuring order, including §§ 69-8-202(1), 69-8-211(2) and (5), MCA. MCC stated that while it generally does not favor trackers, the Commission should have the opportunity to consider MPC's proposals and decide, after a contested case proceeding, whether approving the proposed trackers is in the public interest. MCC stated that nothing in Senate Bill 390 explicitly prohibits tracking mechanisms, but the open-ended nature of the tracking mechanisms proposed by MPC do not "fit well into the overall scheme of the legislation" and cannot be clearly reconciled with several specific requirements.

21. Senate Bill 390 requires that transition costs reflect all reasonable mitigation. But with MPC's tracking proposals, this requirement would necessarily remain an open issue in the Commission's final order, since the ultimate result of mitigation efforts will be unknown. MCC observed that MPC has not attempted to demonstrate the value of the liabilities it proposes to track, as required in § 69-8-211(2)(b), MCA. That Senate Bill 390 requires such a demonstration, and identifies several methods for determining the value, indicates to MCC that Senate Bill 390 envisioned a known value for transition costs prior to approval of the recovery. If the Commission does not approve the amount of transition costs prior to conclusion of the

tracker filings, MCC believes MPC's authority to collect transition charges could be "thrown into question."

22. MCC stated that there can be no serious question that revenue requirement is relevant to the issues involved with the Commission's consideration of MPC's restructuring plan. MCC noted that MPC itself filed a revenue requirement analysis that it asserted could demonstrate a $16.9 million revenue deficiency. MCC asserted that Senate Bill 390 does not in any way prohibit the Commission from reviewing revenue requirements. Revenue requirement analysis is relevant and essential to many restructuring issues, such as stranded cost estimation.

23. MCC asserted that the Commission explicitly stated in its Notice of Public Hearing issued April 6, 1998 that it would conduct a later hearing on revenue requirements. MCC believes MPC's concern may be with the relevance of revenue requirement analysis for the purpose of changing rates. If this is the case, the real issue is the rate moratorium issue and whether the Commission can change rates. MCC stated that although Senate Bill 390 precludes the Commission from increasing rates, nothing prohibits the Commission from reducing rates where justified.

Department of Environmental Quality

24. DEQ stated that Senate Bill 390 does not allow for continuing adjustments to the competitive transition charge after the Commission issues the final order on the transition plan. DEQ asserted that Senate Bill 390 requires that all transition costs/benefits related to the value of generation-related assets and liabilities and electricity supply costs be determined in, and recovered through, the Commission's final order on the transition plan. Once this occurs, all transition cost claims will have been resolved.

25. According to DEQ, to support its proposals MPC relies on § 69-8-211(4), MCA, which allows for varying transition cost recovery periods. DEQ asserted that MPC's approach "rests on a narrow construction of one provision in a broad statutory scheme designed to accomplish significant and far-ranging public policy objectives." The subsection MPC relied on does not address when or how the amount of transition costs is determined, but only the period over which that amount, once determined, may be recovered. DEQ asserted that under Senate Bill 390, transition costs are determined once by the Commission at the time of the

Commission's final order on MPC's transition plan. While Senate Bill 390 allows for adjustments to the transition charges to reflect different recovery periods, actual recovery experience and to account for financing through transition bonds, according to DEQ, none of these adjustments involve changing the amount of transition costs determined by the Commission in its final order.

26. DEQ believed that Senate Bill 390 is intended to fairly allocate the risks of restructuring between the utility and its customers. Under Senate Bill 390, consumers are entitled to the benefits of competitive markets as soon as administratively feasible. § 69-8-102(2), MCA. DEQ asserted that MPC's proposal to recover its transition costs over time as they occur and are more certain will discourage competition and force consumers to bear a disproportionate share of the risks associated with restructuring. DEQ maintained that this is inconsistent with the public policy embodied in Senate Bill 390.

27. DEQ asserted that the idea of using tracking mechanisms with true-ups was rejected by the various interests involved in drafting Senate Bill 390. Parties were concerned that a similar approach used in California had frustrated the development of competition because suppliers faced a moving target. DEQ also asserted that MPC "vigorously opposed" the idea of tracking mechanisms and that the Commission should reject the Company's attempt to now rewrite the provisions of Senate Bill 390.

28. DEQ stated that MPC should be required to produce revenue requirement information in this proceeding to satisfy Senate Bill 390's requirements for functional separation. A primary purpose of functional separation is to prevent the formerly vertically integrated utility from using its monopoly functions to advantage other parts of the company that are engaged in competitive activities. DEQ asserted that in order to evaluate MPC's proposed distribution tariffs the Commission and parties must examine underlying cost numbers. DEQ maintained that MPC must provide updated revenue requirement information to implement Senate Bill 390 and ensure that customers ultimately see rates that reflect MPC's costs.

29. DEQ stated that the market power issues in this proceeding involve the ability of a regulated monopoly to offer services that are also offered competitively by others and to use its monopoly position to forestall the development of competition. DEQ asserted that the best

example in this proceeding is metering and billing. DEQ repeated its request that the Commission reconsider its decision in Order No. 5986d to defer functional separation issues related to metering and billing and address these issues now. DEQ noted that it has been over one year since the Commission issued Order 5986d and no Notice of Inquiry has been established to address metering and billing issues. DEQ stated that it is critical for the Commission to address market power issues related to metering and billing as part of the final approval of MPC's transition plan. The questions of billing and metering are associated with a larger issue, which is the line between regulated and unregulated services. Market power issues related to the separation of regulated and unregulated services, such as metering and billing, have the potential to significantly affect the early results of restructuring.

Big Sky Power

30. Big Sky Power asserted that § 69-8-211(5), MCA requires that Commission approval and utility collection of transition costs settles all transition cost claims by a utility. Webster's dictionary defines "settle" as "to place so as to stay," and "to fix or resolve conclusively, to establish or secure permanently, to become fixed resolved or established." Therefore, Big Sky Power concluded that Senate Bill 390 requires that once the Commission approves transition costs, and MPC begins collecting those costs, no further modification to the transition charges can occur. Big Sky Power asserted that continually adjusting the transition charges would introduce volatility in the "price to beat," making it difficult for electricity suppliers and customers to negotiate contracts.

31. Big Sky Power asserted that MPC's Tier 2 filing is essentially a rate case. The Commission should ascertain the revenue requirement for each of MPC's non-generation regulated services to develop a price to beat that is equal to the total regulated cost and the total bundled rate customers are paying. If the revenue requirement for the regulated portion of the rate is not accurate, MPC would either over- or under-recover regulated costs when customers switch to a different supplier. Over-collection of regulated costs translates into an artificially low price to beat and negatively impacts the development of competition.

32. Big Sky Power expressed concern that MPC's transition service agreement with PP&L Global would create market power since other competitive suppliers would not have

access to wholesale power from PP&L. Big Sky Power asserted that PP&L should be required to sell power to all competitive suppliers in MPC's service territory under the same terms it has agreed to sell to MPC. Big Sky Power stated that market power must be addressed in the Tier 2 proceeding.

Montana Energy Brokers

33. Montana Energy Brokers did not address the legal questions posed in the Commission's September 2, 1999 Notice, but commented on MPC's proposed transmission unbundling and allocation methodology, which is a factual issue that can be addressed in the contested case, not a legal issue.

Montana Power Company Reply Brief

34. In its reply brief, MPC stated that certain parties, particularly LCG and DEQ, ignored the concepts of flexibility and balance and are attempting to harm MPC. MPC cited Senator Fred Thomas's opening statement at a Senate Taxation Committee hearing on Senate Bill 390 in which he discussed the balance struck among parties involved in drafting Senate Bill 390. MPC maintained that the reality is that some costs and revenues, particularly those related to QF contracts, are not definitively known. According to MPC, the answer to this problem is to construct a path that leads to the balance the legislature was seeking.

35. MPC disagreed with LCG's and DEQ's arguments that the Commission must determine net, verifiable costs in its final order. MPC stated that the legislature did not intend to leave potentially millions of dollars on the table when it required that the interests of consumers should be protected and the financial integrity of utilities should be fostered. However, this could be the result if the Commission determines that QF-related transition costs are $400 million in its final order, and in seven years MPC might buy out a contract that results in a $10 million savings. MPC asserted that its proposal to track transition costs is the only way to truly determine "known and measurable costs." MPC reiterated its belief that Senate Bill 390 is flexible enough to allow the Commission to approve a tracking mechanism. MPC stated that historical documentation on the drafting of Senate Bill 390 does not help resolve this issue. MPC identified a letter in the legislative history from Mr. Don Quander, representing LCG, that

argued for a cut-off date for calculating stranded costs but found no other documents suggesting that other parties either supported or opposed a true-up approach.

36. MPC disagreed with DEQ that a tracking approach would be inconsistent with the public policy underlying Senate Bill 390 and discourage competition. MPC questioned how more certain costs could be inconsistent with state policy and consumers paying accurate costs could be associated with an unfair share of risks.

37. MPC reasserted its position that a revenue requirement case for the purpose of decreasing rates would violate the rate moratorium provisions of Senate Bill 390. MPC noted that the legislative history indicates that the legislature intended a rate freeze. Senators Thomas and Foster used the words “rate freeze” when discussing the provision, even though state witnesses used the words “rate cap.”

38. MPC suggested that LCG, DEQ and Big Sky Power do not understand the nature of transition costs when they claim that MPC’s tracking proposals would discourage competition. MPC asserted that transition costs have nothing to do with a competitive market since they are costs that already exist. Everyone pays the transition charges, whether they receive bundled service from MPC or switch to an alternative supplier.

39. MPC re-emphasized that the issue of MPC’s potential to exercise market power in electricity supply markets is moot, given the sale of its generation plants. In response to Big Sky Power’s assertion that MPC’s buy-back contract with PP&L Global means there is no power available for competitors, MPC stated that 25 percent of its load is being served from other sources, which suggests there is a surplus in Montana. MPC stated that Big Sky Power’s suggestion that PP&L Global be required to sell power to all retail competitors in MPC’s service area is unworkable because the Commission does not regulate PP&L Global.

40. MPC stated that it is inappropriate for DEQ and LCG to ask the Commission to reconsider its previous decision to address market power related to metering and billing issues without offering new evidence and arguments. Given the Commissions previous decision to initiate an NOI on metering and billing issues, MPC believes market power with respect to these functions should be addressed in that proceeding.

COMMISSION DECISION

Transition cost tracking mechanisms

41. MPC identified legitimate reasons for tracking certain transition costs, especially QF-related transition costs. In all matters before it, the Commission strives to balance the interests of customers and shareholders. In this particular case, the goal is to maximize the likelihood that customers do not pay more transition costs than they should while treating shareholders fairly. MPC's transition cost tracking proposal might facilitate this outcome. MCC correctly observed that the Commission *should* have the ability to examine MPC's proposals and determine, after a contested case hearing, whether the public interest is served by those proposals. However, what the Commission has the ability to do is constrained by what the law allows it to do. A straightforward reading of Senate Bill 390 in its entirety suggests that MPC's transition cost tracking proposal is not consistent with the legislature's intent.

42. On the issue of transition costs, the tone of finality in the restructuring laws is undeniable. The statute paints a very detailed picture of the restructuring process, including specific utility requirements, Commission determinations and timelines. The process begins with the filing of a transition plan on July 1, 1997 that demonstrates that MPC meets all requirements in Senate Bill 390, including an affirmative showing of claimed transition costs. §§ 69-8-202(1) and 69-8-211(2), MCA. The Commission is required to process MPC's transition plan under the contested case provisions of Title 2, Chapter 4, MCA and issue a final order within 9 months of the day the plan was filed. § 69-8-202(3) and (4), MCA. To accomplish the functional separation of supply from regulated transmission and distribution functions, MPC must remove its generation assets from the rate base on the effective date of the Commission's final order. § 69-8-202, MCA. The Commission must approve an amount of transition costs and establish transition charges and a transition cost recovery period. § 69-8-211(3) and (4), MCA. The transition period, including large customer choice and pilot programs, and the transition cost recovery period must begin on July 1, 1998. §§ 69-8-103(25) and (27), 69-8-104(1) and 69-8-201(1), MCA.

43. The statutory schemata included the very specific requirement that July 1, 1998 is the date on which the transition period begins and transition costs start being recovered through

transition charges determined by the Commission over a transition cost recovery period determined by the Commission. The legislature contemplated that the Commission would complete its contested case on MPC's transition plan and issue a final order establishing an amount of transition costs, recovered through specific transition charges, by July 1, 1998.

44. MPC emphasized in its briefs that the Commission should employ balance and flexibility in implementing Senate Bill 390. To the extent the law permits, the Commission has been flexible. Given the prescriptive nature of the statutes, the Commission has accommodated MPC in allowing a substantial delay in the transition plan case to allow MPC to close its generation asset sale. Now nineteen months into the transition period, neither customers nor potential suppliers have a clear picture of the supply price they need to beat in the marketplace. Only in the last months have customers started to see the different components of their electricity service unbundled on their bills. However, accommodating MPC's transition cost tracking proposal requires stretching the law beyond its limits.

45. In its reply brief, MPC asserted that its tracking proposals provide the best opportunity to determine known and measurable costs. Reply Brief, p. 4. MPC questioned how more certain costs could be considered inconsistent with state policy. This question is answered in MPC's initial brief where it stated that the legislature never thought that MPC would sell its assets, "…Senate Bill 390 does not explicitly account for multiple closings and the myriad of other details surrounding a sale…" Initial Brief, p. 5 The legislature's intent with respect to how to treat transition costs in the context of a generation asset sale cannot be known because it is not the path envisioned when the statutes were enacted. However, as already explained, the legislature's intent with respect to the treatment of transition costs under the presumed path is clear and unmistakable.

46. Aside from interpreting the requirements in the statutes, it is important to have a clear understanding of the concept of transition costs and transition charges. MPC suggested in its Reply Brief that DEQ, LCG and Big Sky Power misunderstand the nature of transition costs and the fact that transition costs have nothing to do with a competitive market. Reply Brief, p. 10. This assertion is incorrect. How transition costs are established can affect whether

consumers and alternative suppliers find it attractive to participate in markets and, therefore, when, or whether, competition will emerge.

47. MPC's tariffed rates are designed to recover an embedded cost-based revenue requirement. One reason for calculating transition costs and establishing transition charges is to allow a utility with embedded costs that exceed market prices to price its supply services at a competitive level, while not forgoing recovery of some or all of the embedded costs allowed in the regulated environment. To accomplish this, the electricity supply-related portion of the bundled tariffed rates is separated, or unbundled, from the total rate. Then, the supply-related embedded costs that would not be recoverable in the competitive environment are identified and removed to a separate, nonbypassable transition charge. There is a one-time, direct relationship between the identification of transition costs and the level at which unbundled electricity supply-related rates are set for the rate moratorium period. Identifying the amount of transition costs simultaneously establishes the electricity supply price customers will use when shopping for alternative suppliers.

48. Overestimating the amount of a utility's transition costs will result in unbundled electricity supply-related rates that are too low. Incorrectly setting the utility's unbundled electricity supply-related rates could distort the development of efficient competition by affecting the entry decisions of suppliers and the choices of consumers. Furthermore, Senate Bill 390 requires that transition costs be estimated on a net basis. A net calculation of transition costs cannot occur if one piece is based on a net present value basis (value of generation assets) while other components are not valued at all (QF-related transition costs). DEQ and LCG were correct to question both the competition and netting impacts of MPC's transition cost tracking proposals. From the legislative intent expressed in the specific transition cost requirements in the statutes, the Commission finds that MPC's transition cost tracking proposals do not comply with Title 69, Chapter 8, MCA. The Commission finds that MPC must amend its Tier 2 filing with respect to transition costs and incorporate an approach that specifically demonstrates and identifies all transition costs it seeks to recover.

Market power

49. Section 69-8-403, MCA authorizes the Commission to decide if there is workable competition in electricity supply markets, but does not indicate what forum the Commission should use to make this determination. The statutes do not specifically require MPC to perform a market power analysis as part of its transition plan filing. Section 69-8-203(2), MCA requires a public utility to propose a method for assigning customers to an electricity supplier at the end of the transition period if the customers had not chosen on their own. (This section was modified by House Bill 211 (1999) to allow cities to apply to become default suppliers.) Market power was especially relevant to this provision when MPC intended to be an electricity supplier and could attempt to acquire a large portion of non-choosing customers through its choice of an assignment method. This particular concern is diminished unless MPC decides to re-enter the electricity supply business.

50. DEQ and LCG asserted that MPC could exert market power in energy service markets through its monopoly control of billing and metering functions. DEQ and LCG believed that the Commission should use the Tier 2 proceeding to examine MPC's costs to provide these functions and consider unbundling these functions to allow customers to obtain them from alternative providers. However, in Order 5986d the Commission ruled that it would consider issues related to whether metering and billing functions should be unbundled in a separate Notice of Inquiry. The Commission has already issued its decision on these matters in this proceeding. To now insert these issues back into the proceeding would deny MPC its right to ask the Commission for reconsideration and seek judicial review of the Order 5986d. Neither DEQ nor LCG asked the Commission to reconsider its decision in Order 5986d.

51. The Commission is interested in a discussion that would assist in ultimately fulfilling the Commission's obligation to determine whether competition is workable. This discussion would address how market power should be defined, identified and monitored and the remedies, mitigation and preventive measures the Commission may use. None of the briefing parties mentioned these kinds of market power issues. Noticeably absent from the group of intervenors filing briefs were some of the suppliers active in the Montana retail supply market that would be most likely to have the ability to exercise market power. Nevertheless, the

Commission asks that MPC initiate this discussion by including in its amended Tier 2 filing testimony that addressing these market power issues.

Revenue Requirements

52. None of the parties who filed briefs on the issue of revenue requirements agreed with MPC's position. Implementation of restructuring demands as much effort as possible to set rates correctly as the industry transitions to competition in the supply of electricity.

53. Does Senate Bill 390 mandate a rate freeze or a rate cap? This issue emerged in the past, e.g., the testimony of MCC witness Mr. Clark. Most of the adjustments proposed by Mr. Clark are now moot as a result of MPC's generation sale. DEQ reads Senate Bill 390 to intend a moratorium on rate increases. MCC pointed out that there is nothing in Senate Bill 390 that prohibits rate reductions where justified.

54. The Commission provided clear and repeated notice to MPC that the issue of revenue requirements would be included in Tier 2 issues. (Notices dated April 6 and April 17, 1998.) MPC ignored this notice in its Reply Brief. MPC has been aware that the Commission intended to consider revenue requirements in Tier 2 for over a year.

55. The Commission finds that revenue requirements is an issue to be addressed in Tier 2 after the sale closes. Senate Bill 390 uses the term rate moratorium to protect customers against rate increases during the transition period. The Commission notes that LCG is correct that a utility is not allowed to recover costs higher than its actual costs under existing utility regulation. MPC is free to file rebuttal testimony which addresses any revenue requirement issues raised by parties in the case.

56. As a practical matter the scope of revenue requirement issues has narrowed considerably since Tier 1 testimony was filed. Many of Mr. Clark's adjustments were production-related and are likely made moot by MPC's generation sale.

CONCLUSIONS OF LAW

1. All Findings of Fact are incorporated in this Order as Conclusions of Law.

2. The Montana Public Service Commission exercises authority over public utilities and the electric utility industry restructuring pursuant to its authority under Title 69, particularly Chapters 3 and 8, MCA.

3. MPC furnishes electric service for consumers in the State of Montana and is a vertically integrated public utility under the regulatory jurisdiction of the Montana Public Service Commission. §§ 69-3-101 and 69-3-102, MCA.

4. The Commission has the general power to govern the modes of procedure, to prescribe rules of procedure, and to do all things necessary and convenient in the exercise of the powers conveyed on it pursuant to Title 69, Chapter 3, MCA, including rendering an order on legal issues in a docket involving a regulated public utility. § 69-3-103, MCA.

5. The Commission has the authority under Title 69, Chapter 8, MCA, to establish the procedures necessary in processing a public utility's application for approval of its transition plan on restructuring, including making legal determinations on the plan and directing a public utility to amend its plan to comply with Title 69, Chapter 8, MCA. § 69-8-202, MCA.

ORDER

WHEREFORE, the Commission issues the following order:

1. Montana Power Company shall amend its transition plan filed on July 1, 1999 on the generation sale and other issues in the Tier 2 proceeding with respect to transition costs. MPC shall incorporate an approach that specifically demonstrates and identifies all transition costs it seeks to recover.

2. MPC shall initiate discussion on market power issues as addressed in this Order by including in its amended Tier 2 filing testimony that addressing these market power issues.

3. Revenue requirements issues will be considered in Tier 2 after the close of the generation sale.

DONE AND DATED dated this 23rd day of November, 1999, by a vote of 5-0.

BY ORDER OF THE MONTANA PUBLIC SERVICE COMMISSION

DAVE FISHER, Chairman

NANCY MCCAFFREE, Vice Chair

BOB ANDERSON, Commissioner

GARY FELAND, Commissioner

BOB ROWE, Commissioner

ATTEST:

Kathlene M. Anderson
Commission Secretary

(SEAL)

NOTE: Any interested party may request the Commission to reconsider this decision. A motion to reconsider must be filed within ten (10) days. See ARM 38.2.4806.