IDAHO ATTORNEY GENERAL'S ANNUAL REPORT

OPINIONS

SELECTED INFORMAL GUIDELINES

AND

CERTIFICATES OF REVIEW

FOR THE YEAR

1999

Alan G. Lance
Attorney General

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1999 Idaho Att'y Gen. Ann. Rpt. 171

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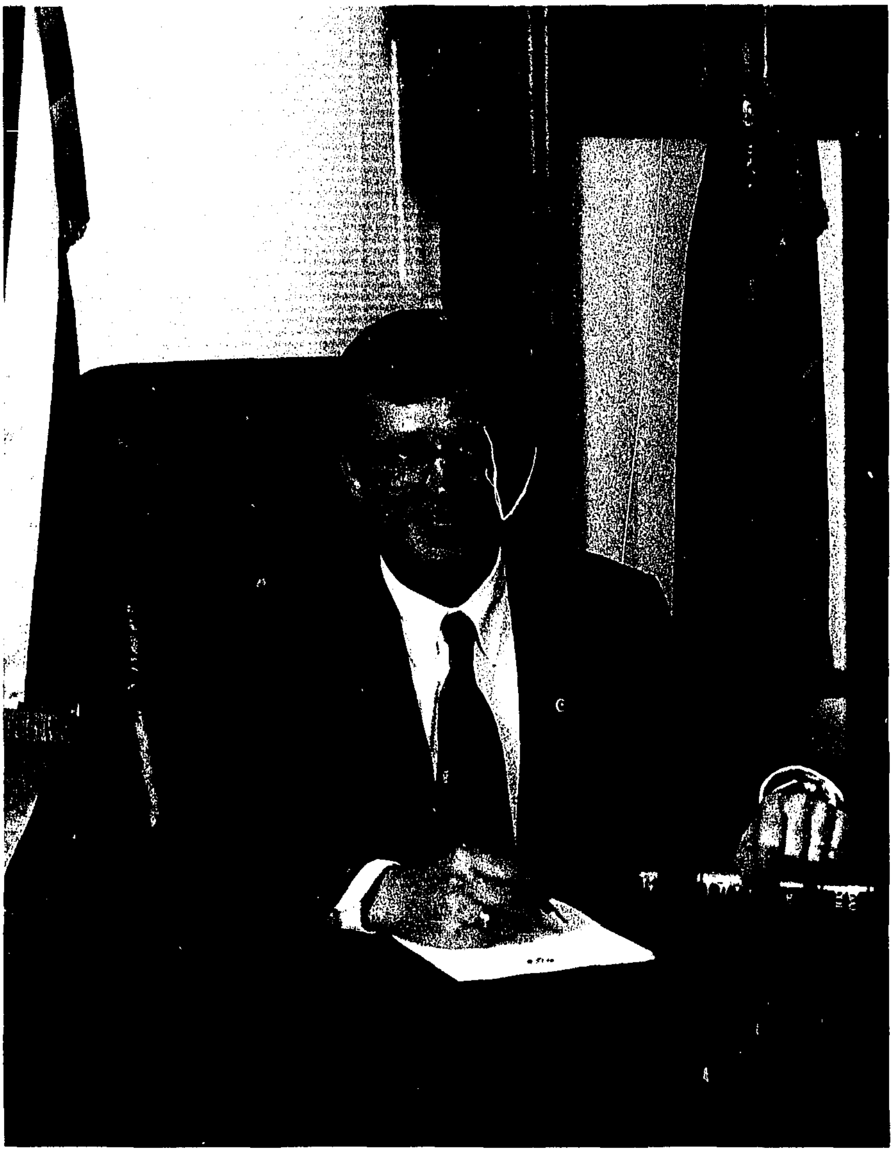

Alan G. Lance
Attorney General

INTRODUCTION

Dear Fellow Idahoans:

I am pleased to present to you the Idaho Attorney General's Annual Report for 1999. This volume contains the legal opinions, guidelines and certificates of review which were issued during 1999 by my office at the request of the state elected officials and other state entities we represent. This year we have also included cumulative indexes going back to 1993.

The Office of the Attorney General is the largest law office in the State of Idaho. The Idaho Constitution and Idaho Code require the Attorney General to provide legal representation to state departments, boards and commissions, and state elected officials. My office's specific duties and powers are set forth in 948 sections of the Idaho Code, Idaho administrative rules, and Idaho court rules. The 178 highly skilled and professional employees in my office carry out these duties on a daily basis at the request of our client, the largest employer in the State of Idaho.

The ability to call upon the broad expertise and skills available in my office is perhaps one of the most enjoyable aspects of serving as your Attorney General. With attorneys and legal staff experienced in virtually all areas of law, I am able to bring considerable scrutiny and analysis to bear upon the major issues facing Idaho. This volume of the Annual Report contains one of the best examples of how my office can provide definitive legal analysis for our clients before policy decisions are made that will impact the lives of all Idahoans.

The Special Report on Electric Utilities Restructuring is a comprehensive report written by a core team of Deputy Attorneys General for one of our clients, the Legislature's interim committee to study electric utility restructuring. The interim committee was created to look at the policy question of whether electric utilities should be restructured or deregulated. The issue was, and still is, a national issue. With relatively low power rates and other western states eyeing Idaho's water and hydropower capacity, my core team was assigned to deliver a report which would identify all legal issues and policy options available to the interim committee.

I assigned Deputy Attorneys General from four of my six legal divisions to the core team. Substantial legal experience in public utilities law, contract law, administrative law, consumer protection law, antitrust law, and constitutional law was aimed at helping the Legislature to make an informed decision on this extremely important issue. The report was ultimately provided to all Legislators and will continue to assist them in the coming years, as this issue will no doubt be ongoing. I asked that the Special Report be reproduced in this volume so all Idahoans will have easier access to the information that will help guide our elected officials in making their decisions.

I look forward to serving my sixth year as your Attorney General. I expect another busy and successful year representing the legal interests and rights of the State of Idaho.

Alan G. Lance

ALAN G. LANCE
Attorney General

OFFICE OF THE ATTORNEY GENERAL
ALAN G. LANCE
ATTORNEY GENERAL

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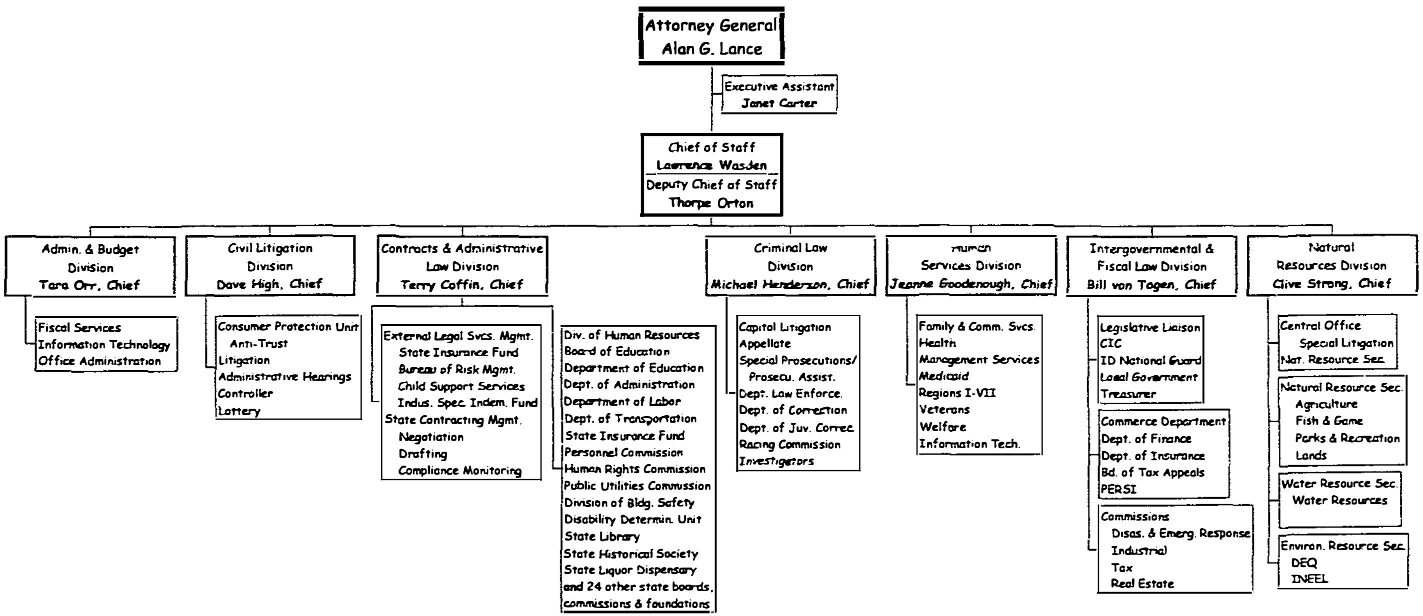
Office of the Idaho Attorney General
Organizational Chart - 1999



SPECIAL REPORT

ELECTRIC UTILITIES RESTRUCTURING

I.

INTRODUCTION—ORIGINS AND PURPOSE OF REPORT

In 1997, the 54th Idaho Legislature passed House Concurrent Resolution No. 2 (HCR 2) authorizing the appointment of an Interim Committee to study electric utility restructuring. The resolution authorized the appointment of "a committee to undertake and review the potential restructuring of the electrical utility industry from both the statewide perspective and the national perspective. The committee is directed to involve representatives of industry, agricultural groups, small businesses, consumers of electricity and conservation interests."

A primary concern of the legislature in passing HCR 2, and in creating the Interim Committee, was to study electric restructuring issues in an effort to avoid unintended consequences. The resolution states that significant unintended consequences could occur if deregulation is not carefully thought out and planned. The legislature was concerned that implementing deregulation, if it authorizes, must be "managed properly."

On February 6, 1998, in response to a request from the Interim Committee, Attorney General Alan G. Lance formed a Working Group within the Office of Attorney General (OAG) to assist the Interim Committee. This Working Group was charged with the responsibility to study the issues, the options available to the legislature regarding electric utility restructuring, and to deliver a report to the Interim Committee chairmen.

The Working Group was made up of attorneys from within the OAG who have expertise in the areas of electric utility law, electricity buy-sell agreements, water law, consumer law, and bonding issues. Since its formation, the Working Group has studied the issues related to electric deregulation generally, the experiences of other states that have deregulated or restructured electric utilities, as well as issues and challenges of electric deregulation that are unique to Idaho. The Working Group has heard from representatives of electric suppliers, consumer groups, agricultural interests, and industries that are heavily reliant upon electric power.[1] These groups shared their perspective and made known their concerns and recommendations relating to deregulation.

This Report is the product of the Working Group's eleven months of study. Not only did the Working Group hear from the producers, sellers, and users of electricity, but also it sifted through thousands of pages of data, studies, and reports.[2] Inquiries were made of other states that have adopted or considered restructuring. It contains an in-depth study of the electric system in Idaho as well as each of its component parts. It also discusses issues that are unique to Idaho and, in particular, the prominence of water among the state's many natural resources. This Report reviews the challenges presented by deregulation generally, and how those challenges have been addressed by other states. It also discusses Idaho's unique issues. Finally, this Report makes observations to the legislature regarding deregulation. These observations are based upon the conclusions of our study, comments from electrical users and the electrical industry, and the experiences of other states. Perhaps, most importantly, the observations made in this Report reflect the change of circumstances that have taken place since 1996 and 1997. At that time, it appeared imminent that Congress would mandate some form of electric deregulation. Federal deregulation, however, has not occurred and is no longer a certainty. Idaho now has the luxury of continuing to observe and study other states that have pursued deregulation. Consequently, this Report concludes that Idaho should not take any significant steps, at this time, toward restructuring the electric industry.

II.

EXECUTIVE SUMMARY

The dilemma presented by electric restructuring or deregulation is not unlike the lesson of Humpty Dumpty. Once deregulation is undertaken, "all the king's horses and all the king's men" will be unable to put the present electrical system back together again.

Although deregulating is simpler than re-regulating, it, too, presents unique challenges. The electrical structure is complex, consisting of generating facilities, transmission facilities, and distribution facilities. Any system, whether it exists in a regulated or a deregulated environment, must have adequate capacity to meet peak demands. The burden of deregulation must not fall unfairly upon companies that maintain the transmission portion of the network, or those who maintain the distribution portion of the network. New vendors of electrical power must share in the responsibility of maintaining the existing structure so that it continues to meet the needs of a modern, technological and electric-dependent society. The problem of stranded costs, as well as stranded benefits, of long-standing utilities must be addressed.

Idaho's reliance on hydroelectric power presents unique challenges with respect to deregulation. Generation of hydroelectric power requires the use or appropriation of a public resource, that resource being the state's water. It is important that any development of this resource is for the benefit of the state and it's people. The importance of the development of water for the benefit of the state and its citizens is reflected in both the state's statutes and constitution. Because of the reliance of electric generation upon this important state resource, electric deregulation in Idaho also involves issues of state sovereignty and the state's ability to control the development of a resource that belongs to all Idahoans.

Idaho's reliance upon hydroelectric power generation has benefited this state with some of the lowest electric rates in the nation. Studies predict that, while national electric deregulation may bring about lower electric rates for most of the United States, electric rates in states such as Idaho will undoubtedly increase. Any effort toward restructuring the electric utility industry must avoid, or at least minimize, any adverse effects on consumers.

To date, fourteen other states have adopted electric restructuring in some form. Other states have considered deregulation but, to date, have declined to deregulate. Two years ago it appeared that imminent congressional mandates would require Idaho to adopt deregulation in some form. It now appears that it will be some time before Congress adopts any meaningful national deregulation legislation. The Congressional reprieve allows Idaho the opportunity to observe the experience of the fourteen states that have restructured and to determine whether deregulation will benefit Idaho.

If the legislature should decide to pass some form of deregulation legislation, it must first and foremost avoid a result where the benefit of our water resources are, in effect, exported out of state with none of the benefit remaining in Idaho to contribute to our economy or to the well-being of our citizens. Idaho's water resources belong to Idaho and her people and the benefits of those resources must flow to the state and its citizens. Deregulation must address the protection of Idaho's water resources and recognize the unique position and importance of water to the economy and well being of the State. Second, if there is a restructuring of the electric industry of the state, the legislature must ensure that all customers, especially rural and residential customers, be afforded a stable electric supply at reasonable and affordable rates. Third, there must also be consumer protection from fraudulent and deceptive marketing practices similar to those that have occurred since telephone deregulation. Consumer protection must include consumer education, which gives to electric customers understandable information regarding the options presented by deregulation and information in a standard format that allows, and even invites, comparison. Finally, there are many other issues – too numerous to list here – that must be addressed if deregulation is to occur. This Report discusses many of these issues.

III.

BASIC OPERATING STRUCTURE AND HISTORY OF THE ELECTRIC INDUSTRY

A. Overview of Electric System Segments

Power systems consist of an integrated set of facilities that permit electrical energy to be generated, transmitted to, and utilized by a customer. The three common segments to such systems include: 1) generation; 2) transmission; and 3) distribution facilities. Given the growth of wholesale power markets, certain basic transmission services, termed "ancillary services," must also be provided in connection with the transmission of electricity. Additionally, the prospect of local retail competition has created pressure for the disaggregation, or "unbundling," of formerly integrated end user customer services and rates, including those pertaining to energy (on a stand alone basis), meter reading, billing and collection, and so on. In order to provide a foundation for the analysis in this Report, this section briefly discusses these and other basic elements of the electric system structure and operations. Additional information is available from the source materials cited in the footnotes.

1. Generation

Generation is the production of electrical energy. Most generation in the United States results from the process of electromagnetic induction.[3] This process, discovered by Michael Faraday in 1831, is based on the relative motion of an electric conductor and a magnetic field. A large magnet, attached to the end of a rotating shaft, is positioned to turn inside a fixed ring created from a long, continuous piece of wire. As the magnet rotates, it creates or induces an electric current into the wire as it passes by, thereby generating electricity that flows into the electrical network.[4]

Rotation can be produced in several ways. In a typical steam turbine, fuel (i.e., coal, oil, wood, waste, nuclear) is burned, or solar radiation is utilized,[5] to boil water. The resulting steam is channeled to and spins a turbine blade. The turbine blade is attached to the shaft to which the magnet is also attached and, thus, the magnet rotates with the turbine. In the case of hydroelectric generation, the force of falling water turns a waterwheel or turbine, in turn rotating the magnet. The combustion gases from burning natural gas will/can also turn a turbine, similar to the dynamics of a jet aircraft engine. Likewise, wind blowing against a blade can create rotation.[6]

Consumers want power when they need it, and their needs vary from moment to moment. Electricity, unlike natural gas, cannot be effectively produced and stored for any period in anticipation of demand. Therefore, utilities historically have had to build generating plants sufficient to meet maximum demands for power, even though such maximum levels might occur only periodically. As a result, not all generating plants may be in operation at a particular point in time. Further, not all output available from those plants that are in operation will actually be used.

Generation is generally measured in terms of capacity and capability (output). Capacity addresses the quantity of power produced or required at an instant of time and is measured in kilowatts (kW) or megawatts (mW). A capacity rating for a generator (e.g., 100 mW) generally refers to the amount of electricity the generator can produce at any one moment. Capability (output) refers to the amount of electricity produced or required over a defined period of time and is measured in kilowatt-hours (kWh) or megawatt-hours (mWh). If the above generator were utilized for an entire day at the rated capacity, it would produce an output of 2400 mWh. Even if the customer only requires 2400 mWh of output for some but not all 24-hour days, the utility is required to have facilities with that generating capacity at all times. The average residential consumer has his or her meter read and currently pays for energy service in terms of kWh of usage, measured in terms of cents/kWh.[7]

Capacity can be separately characterized as peaking and reserve. Peaking capacity is that generation capacity available to meet consumer needs during periods of highest demand. Such periods may occur and be measured in terms of daily, weekly or seasonal peaks. For example, peak demand for residential customers oftentimes occurs in the late afternoon, coinciding with the end of the normal workday, meal preparation, and after school. Reserve capacity generally refers to the generating capacity available to meet scheduled or unscheduled outages, though it can also include capacity to meet peak or abnormally high demands. Utilities are required to maintain defined levels of reserves in order to meet the public interest requirements inherent in uninterrupted electric power. Reserves may be characterized as either "hot" or "spinning," which refers to a generating unit that is brought up to operating temperature and conditions and is connected to the system for prompt delivery of energy; or as "cold," where the generating unit is not maintained at operating temperature or otherwise must go through some start-up process before being connected to the system and becoming available to supply electricity.[8]

2. Transmission

Unlike telecommunications, electricity must be delivered from the generating sites to the consumer's premises through physical interconnection.[9] The system for achieving this delivery consists of wires and cables integrated into local and regional networks, which are generally interconnected nationwide.[10] For reasons both physical and legal, this system is generally bifurcated and discussed in terms of transmission and distribution.

A transmission system includes high-voltage lines, composed of copper or aluminum wires as conductors, which are usually carried on steel towers. Theory and experience demonstrate that the most efficient and cost-effective way to deliver electricity over long distances is to increase (step up) the voltage of the electricity.[11] Power plants generate voltages of 4,600 to 20,000 volts. Transformers increase the voltage level for transmission lines to the range of 37,000 to 765,000 volts. These voltage levels (which are reduced or stepped down at the interface with local distribution networks) are a primary attribute of transmission facilities. Investor-owned utilities or state and federal power authorities own most high-voltage transmission lines.[12]

Unlike a telecommunications network, transmission in an electric system is in a continuously dynamic state. Customer demands for electricity fluctuate from moment to moment (as lights are turned on and off, air conditioners or heaters cycle on and off, and so on). Whereas the telecommunications network is designed to permit some blockage or busy signals, the electric network must meet fluctuating demand on an essentially instantaneous basis.

Several factors make meeting this fluctuating demand a challenge. Principles of conservation of energy require that the sum of the electrical generation from all generators must equal the total amount of power used by all customers at every moment of time. Insufficient generation can lead to brown out conditions and damage to electrical equipment. Excess generation can rapidly lead to overloads, triggering outages. "Busy signals" are not well tolerated in an electric network.

Further factors require dynamic coordination of electric transmission and system loading. Electricity does not necessarily flow directly from one defined point in the system to another, but may take circuitous paths depending upon how intervening lines are loaded at any point in time. Frequency and voltage of power being transmitted must be synchronized among all generators connected to the system. Additionally, long distance power transmission entails loss of voltage, termed "reactive losses." Such losses must be compensated with the addition of reactive power to keep voltage from dropping below tolerance levels at various points in the system.

Thus, a reliable transmission and power supply involves maintaining the balance of supply and demand within narrow tolerances on a continuous basis, synchronizing all generation, and making good transmission losses of voltage—all on a network that generally does not permit transmission of power from a specific generation site to a specific customer site.[13] Substantial coordination is required to satisfy these requirements and to maintain reliability in the network. Historically, representatives of the interconnected utility systems formed organizations and groups (with varying degrees of formality) to provide such coordination. The North American power system presently is divided into five major interconnected areas, nine regional reliability councils, and 157 control areas (a geographic area with an energy control center bounded by interconnected metering and telemetry).[14]

Aside from differences in voltage, physical characteristics of the plant, and so on, the differentiation in characterizing facilities as transmission or distribution may have significant legal consequences. The Energy Policy Act of 1992 (EPAct) sought to promote competition in the electric generation and supply markets by promoting wholesale competition, i.e., the "sale of electric energy to any person for resale."[15] With respect to generation, this congressional goal was achieved through provisions encouraging market entry by non-traditional, non-utility generators. With respect to transmission, the EPAct gave the Federal Energy Regulatory Commission (FERC) authority to order utilities to provide open and comparable access to their transmission systems to all electric generators. This "open access" permits power producers, who lack transmission facilities, to contract directly with wholesale customers (municipalities and cooperatives) in distant locations for electric service, using the intervening transmission facilities of one or more utilities. Thus, wholesale consumers (normally distribution suppliers) are no longer restricted to obtaining electric energy from the local utility that also owns the transmission facility for delivering electricity. This ability to competitively sell and transmit wholesale generation is sometimes referred to as "wholesale wheeling."[16]

But federal law applies only to interstate commerce:

> The provisions of this Part shall apply to the transmission of electric energy in interstate commerce and to the sale of electric energy at wholesale in interstate commerce, but . . . shall

> not apply to any other sale of electric energy . . . . The [FERC] shall have jurisdiction over all facilities for such transmission or sale of electric energy, but shall not have jurisdiction . . . over facilities used in local distribution or only for the transmission of electric energy in intrastate commerce . . . .[17]

The consequences of the EPAct are that FERC can regulate interstate transmission and any associated wholesale wheeling, but has no authority over local distribution facilities and cannot compel "retail wheeling" (direct sales to end users). The EPAct does not appear to directly address the issue of what constitutes local distribution as opposed to interstate transmission facilities. This jurisdictional dichotomy and associated definitional uncertainties have created stresses for state policies concerning electric restructuring.

3. Distribution

The point at which voltage is stepped down to a level at or below 37,000 volts is often considered the demarcation between transmission and distribution in the system. Distribution entails the delivery of electricity to the end user or ultimate consumer premises, usually at the level of 120 or 240 volts required for lighting, home appliances, etc. The physical plant of the distribution system consists of primary lines, distribution substation/transformers, secondary lines, and regulating and protective equipment (such as substation circuit breakers to guard against overload). Distribution is generally, though not always, associated with a defined geographic area (such as a town). There are more than 3,000 separate electrical distribution systems in the United States of which the largest 200 systems provide approximately 90% of the industry's generating capability and serve nearly 80% of the nation's customers. Many of the remaining systems have little or no generation or transmission facilities of their own and function as distribution suppliers of electricity.

There are four distinct ownership types of electric distribution systems.[18] First, there are the private or investor-owned systems (approximately 250 systems account for approximately 75% of the Nation's generating capability). Being intrastate in nature, investor-owned distribution suppliers are generally regulated by state public utilities or corporation commissions. Second, is the state, municipal, and local publicly owned systems (more than 2,000 systems accounting for about 11% of the industries generating capability). Third, are the electric cooperatives (about 900 systems with approximately 6% of the nation's generating capability). Rural electric cooperatives cover approximately 75% of the landmass of the United States and serve about five customers per mile of distribution line. Public distribution and electric cooperative systems are managed by their respective controlling entities.

Finally, there are the federal power marketing agencies that account for approximately 11% of the nation's electrical supply. These agencies market the hydroelectric power from multipurpose water projects operated by the U.S. Army Corps of Engineers and the Bureau of Reclamation. The various types of public water projects include flood control, navigation, irrigation, recreation, and power production. Among others, these agencies include the Bonneville Power Administration (BPA) in the Northwest, and the Tennessee Valley Administration (TVA) in the Southeast. BPA is the only federal marketing agency with "utility responsibility" to meet the needs of public agencies and rural electric cooperatives.[19]

The point of jurisdictional demarcation between transmission and distribution is not always clear. For example, some commercial end user customers (such as manufacturers) may arrange for direct delivery of electricity to their premises at voltages higher than those associated with residential service. Such commercial customers may supply and maintain their own interconnection/transformer facilities, rather than utilizing those of a utility. In such cases, the variations between primary and secondary distribution and primary distribution and transmission may not always be clear. In its signal Order No. 888,[20] FERC proposed seven "indicators" to be used in evaluating whether particular facilities are transmission or local distribution (as applied to vertically integrated utilities):

1. Local distribution facilities are normally in close proximity to retail customers.
2. Local distribution facilities are primarily radial in character.
3. Power flows into local distribution systems; it rarely, if ever, flows out.
4. When power enters a local distribution system, it is not reconsigned or transported on to some other market.

5. Power entering a local distribution system is consumed in a comparatively restricted geographic area.
6. Meters are placed at the transmission/local distribution interface to measure flows into the local distribution system.
7. Local distribution systems will be of reduced voltage.[21]

The distinction and point of demarcation between transmission and local distribution impacts the scope and efficacy of state policy enactments, including any contemplated by the State of Idaho.

4. Ancillary Services

The advent of open access transmission and wholesale wheeling, under FERC Order No. 888, implicates the dynamic system processes described above concerning "Transmission." New, non-utility generators and wholesale customers seeking to benefit from wholesale wheeling require the ability to obtain certain services needed to provide basic transmission—these services are known collectively as "ancillary services." Such services "range from actions taken to effect the transaction (such as scheduling and dispatching services) to services that are necessary to maintain the integrity of the transmission system during a transaction (such as load following and reactive power support). Other ancillary services are needed to correct for the effects associated with undertaking a transaction (such as energy imbalance service)."[22] In its Order No. 888, FERC has defined six ancillary services:

1. Scheduling;
2. Reactive Supply and Voltage Control from Generation Sources Service;
3. Regulation and Frequency Response Service;
4. Energy Imbalance Service;
5. Operating Reserve—Spinning Reserve Service; and
6. Operating Reserve—Supplemental Reserve Service.[23]

These services permit non-utility users to use the transmission system without degradation to the integrity and reliability of network operations. The availability of such services also equalizes the competitive playing field by removing some of the handicaps that would otherwise hamper or prevent a competitive generator from accessing remote wholesale customers.

5. Unbundled Services

Historically, the typical local electric utility offered electricity as part of an integrated or "bundled" service offering that included: 1) the electric energy itself; 2) delivery of that energy to the customer's premises; 3) meter reading; 4) billing; 5) customer services (inquiries, repair, etc.); and 6) other services. If wholesale competition (which, as noted above, involves only the sale of electric energy for resale to a third party) is extended into the local distribution market (i.e., sale of electric energy to the ultimate consumer or end user), "retail wheeling" or "direct access" occurs. In such a competitive market, electric energy may be sold to end users separately from other services (electricity becomes "unbundled"). Those other services themselves may or may not also be competitively provided.

Retail wheeling or retail competition can raise multiple issues. Utility costs and rate processes generally are not geared to reflect unbundling and pricing of discreet services. Multi-party access to the local distribution system requires operational, financial, and rate making adjustments (in concept, not unlike ancillary services requirements pertaining to wholesale wheeling and transmission). The local distribution system itself (like the transmission system) is a bottleneck facility and, thus, issues concerning equal access, ownership, and operation also arise at this level. Retail wheeling may also raise consumer information, universal service, and consumer protection issues. For example, the duty to provide electricity to any customer ("default provider" or "provider of last resort" issues). (See page 52).

B. The History of Electric Industry Restructuring

A brief history of the development and evolution of the electric industry provides a context for assessing the applicability and desirability of various restructuring options. More detailed information is available in the materials cited in the footnotes.

1. 1900 - 1940: Small Competitors to Large Holding Companies

"Customer choice" is not a new concept. In its earliest period, some electric service provisioning was a very competitive business.

> It is a bit of historical irony that the electric services industry that matured in the United States, marked by the presence of vertically integrated monopolies, began at the dawn of this century as a competitive scramble. The first governmental entities that came into contact with the infant industry were at the municipal level. While the initial pattern was not uniform, it was common for multiple franchises to be granted with the consequence that in Chicago there were 29 rival electric companies. I am less certain of the number in San Francisco, but I recently attended a reception in a large mansion in Pacific Heights where I was treated to an interesting glimpse into the city's past. My host informed me that the house had been constructed in 1899 and had survived the great earthquake and fire. He took me on a tour below stairs to what had once been the chief butler's room. There we found evidence of seven rival sets of distribution lines. Apparently, the household steward had literal choice in selecting the source of the early electric service.[24]

In the Pacific Northwest, such competition often involved multiple small entities, literally proceeding on a door-to-door basis:

> About 1890 a 75-horsepower Thomason-Houston dynamo was purchased to generate current for incandescent lamps, and [Thad] Trullinger [owner of the sawmill acquiring the dynamo for its own power] went out for residential as well as commercial business. The first ten or twelve houses were wired free to get customers on line.[25]

Southern Idaho had similar experiences. In 1900, owners of the Trade Dollar Consolidated Mining and Milling Company contracted for the construction of a hydroelectric dam at Swan Falls on the Snake River. When completed in 1901, the dam supplied electricity to the Trade Dollar Mine some 28 miles away in Silver City. The electricity powered stamping mills, air compressors, drills, and water pumps. The run-of-the-river dam eventually provided electricity to the towns of Murphy, Silver City, and Dewey.[26]

Initial competition gave way, however, to consolidated and integrated operations.[27] Amalgamating customers and serving areas provided a basis for utilizing larger generators. Larger generators meant greater efficiency, hence reduced costs. As utilities expanded the scope of their operations, improved their reliability, and reduced the cost of service per unit, industrial customers shifted away from self-provisioning and became utility customers, as well.[28]

This operational consolidation was amplified in the 1920s by financial consolidation as electric utility holding companies formed and expanded. By the late 1920s, vast holding companies occupied a dominant position in the industry. At one point, the 16 largest electric power holding companies controlled more than 75% of all U.S. generation.[29] Operating in interstate commerce, however, these holding companies largely escaped regulation by the states, whose authority was confined to the operating subsidiaries. High leveraging, self-dealing, and other questionable practices, made the holding companies vulnerable to economic downdrafts. The stock market collapse in 1929 and the subsequent Depression brought about the collapse of some holding company structures and the reorganization and regulation of the residual industry under the Public Utilities Holding Company Act of 1935 (PUHCA).

2. <u>1940 - 1965: Big Is Better</u>

"Great changes came about in the Pacific Northwest power situation during the 1940s because of the impact of World War II and a huge expansion of aluminum production . . . . Magnesium, carbide and other types of electro-industry, together with hundreds of welding machines in shipyards, contributed to the regional power load."[30]

The demands of war production helped revitalize the industry after the turmoil of the 1930s and began an expansion of the electric industry that was to carry forward to the end of the 1960s. In the post-World War II period, electric utilities entered into a period of sustained, relatively stable and substantial growth. Between 1940 and 1970, output grew from 118 to 1,400 billion kWh.[31] This growth derived from multiple sources.

First, the post-war period saw a substantial increase in the electrification of the country. An expanded industrial base and a prosperous economy expanded demand for electrical energy. Second, improvements in the generating process permitted larger generating facilities with a concomitant decrease in per unit production costs due to realization of economies of scale. Declines in retail electric energy costs and expansion of electrification and general economic activity were mutually reinforcing trends. Bigger plants produced bigger economies; big was better, especially for consumers. Between 1906 and 1970, the average price of power to residences declined from ten cents per kWh to about 2.6 cents, before any adjustment for inflation.[32]

Although economic fluctuations occurred, this period generally saw continued demand and sales growth. Such growth was considered a constant, and predicted as such. Plant construction continued, based upon such predictions and the economies of scale inherent in the large-plant construction necessary to meet those predictions. Continued electrification of rural areas and effective marketing of electric, laborsaving appliances to consumers contributed to this upward trend. Expanded sales provided cash flow to finance new construction projects. Real costs to consumers continued to decline as electric usage increased and economies in generation continued to materialize.[33]

3. Post-1965: The Times, They Are a Changing

The relative calm and predictability associated with the electric industry began to fade in the latter part of the 1960s. Several trends, not always initially recognized, combined to create turmoil in a once staid business. Among those of note:

a. Declining economies of scale—Benefits resulting from economies of scale in generation gradually tapered off. Improvements in operating efficiencies became harder to acquire as larger units became more technically complex in design and construction, more expensive to maintain, and failed (in some instances) to fully meet anticipated cost-benefit goals in terms of operating savings. This trend was exacerbated by some of the other factors described below.

b. Increases in construction costs—Increasingly larger plants required increasing amounts of capital. As and when the cost of capital increased (as it did in the 1970s), so did the cost of construction. Further, increases in generating plant size required longer periods of construction. This lengthened the period before such plants could be put into service and therefore into the rate base, thus increasing the carrying costs of construction and exacerbating the cost of construction problem. Increasing regulation of construction, including environmental concerns, imposed new complexities and further increased the time from design to service inception, making construction more expensive still. In the case of certain nuclear plants, construction was terminated in mid-process and investment was written down. This increased the perception of risk attending generation construction, increased the cost of capital, and increased project carrying costs and the ultimate costs of construction.

c. Increases in fuel prices—Large plants require large quantities of fuel, dependably supplied. Such economies in bulk fuel purchases as might be obtained could be swamped by significant increases in the cost of fuel. Between 1971 and 1983, oil fuel costs rose by a factor of ten, natural gas prices increased by a factor of seven, and the cost of coal increased by a factor of four.[34] Such increases far-outstripped quantity purchase discounts. In some circumstances, some utilities locked in high fuel rates through long-term fuel supply contracts in an effort to forestall even higher fuel costs in the future. These contracts subsequently posed cost issues when market prices for fuel declined rather than increased.

d. Unanticipated demand changes—The effects of increases in electric industry capital and operating costs eventually found their way into the rates paid by consumers. Rate increases, coupled with other factors such as energy conservation programs and environmentalism, produced relative declines in consumer consumption atypical of the historical pattern and not fully anticipated by the industry. The historical pattern of steady growth stopped, trapping many utilities between a relatively (or absolutely) declining sales curve and an increasing cost curve. The theory of large-plants-for-large-demand aggravated the situation as demand growth dwindled. Further, the long construction periods inherent in large plants made it difficult for utilities to turn the construction battleship around immediately in response to such changes in demand.

These trends became manifest in a series of events that have become milestones marking the path to today's restructuring initiatives. These events contributed to a change in public perspective concerning electric utilities and the electric industry. That change in perspective, in turn, contributed to changes in governmental policies concerning the industry. Combined with other factors, such as technological evolution, these events formed the historical antecedents for the current restructuring reviews now occurring in many states.[35]

a. 1965 Northeast Blackout—On November 2, 1965, a relatively minor equipment failure in a backup transmission relay switch spawned a cascading series of power surges and disconnections, blacking out large segments of the Northeast United States and depriving approximately 30 million people, including the capital market center of New York City, of power. The dimensions of the outage impacted public perception of the reliability of power and called into question then-current management and regulatory practices.

b. 1972 - 1973 Arab Oil Embargo—As a result of the Arab-Israeli conflict in the Yom Kippur War, the Organization of Petroleum Exporting Countries (OPEC) curtailed oil shipments and substantially boosted the cost of oil and petroleum-derived products. Increases in fuel costs for oil-fired generation translated into higher rates for electricity. Higher rates resulted in decreased demand and reinforced a shift to conservation in electric consumption. As noted above, declines in demand adversely impacted electric industry planning, cash flows, prior period construction decisions, etc.

c. 1974 Con Edison Dividend Moratorium—In April 1974, Consolidated Edison, a major Northeast utility, omitted payment of a dividend. This omission called into question basic market assumptions about the financial condition and policies of electric utilities. In conjunction with other factors, these concerns lead to a market reevaluation of the electric industry and steady decline in the market price of electric stocks. Declining stock prices and an increase in perceived risk in the industry lead to higher costs of capital and a more limited market for utility offerings; this in turn contributed to the problem of higher construction costs, as noted above.

d. 1979 Three Mile Island Nuclear Incident—Failure in the cooling system of a General Public Utilities subsidiary's nuclear plant at Three Mile Island reinforced a growing public concern for the consequences of catastrophic failure of a nuclear generator. In the wake of the incident, public interest activism reinforced regulatory concerns for plant operation and safety. Licensing of new nuclear facilities was suspended; existing construction was subjected to further review and new requirements, all of which served to increase the complexity, duration, and cost of construction. Eventually, some nuclear plants were abandoned; others were sold or retired after short operating lives.

e. 1983 WPPSS Default—The Washington Public Power Supply System was a municipal agency created to build power-generating facilities, the output of which was to be sold to various public power agencies. WPPSS contracted to construct five nuclear plants as the sources of such generation. As a result of the events and the trends described above, costs and duration for construction increased. Some construction was cancelled; other projects halted when cash flows dried up. In June 1983, a court decision adverse to investors triggered a default by the State of Washington on the WPPSS bonds. This resulted in significant losses to bondholders, in reassessment of utility risk in the debt and equity markets, and in adverse impact on public perception of the power industry. In Asson v. City of Burley, the Idaho Supreme Court ruled that various Idaho cities had exceeded

> their constitutional authority by incurring long-term indebtedness without voter approval or statutory authority. 105 Idaho 432, 670 P.2d 839 (1983).

With this historical and structural overview, we now turn to Idaho-specific circumstances.

IV.

THE IDAHO ELECTRIC INDUSTRY

A. Overview of System

1. Distribution Suppliers

Idaho consumers are currently served by three types of distribution suppliers: 1) the private or investor-owned utilities; 2) the electric cooperatives; and 3) the municipal suppliers. More than 80% of all Idaho customers are served by four investor-owned public utilities: 1) Idaho Power, serving about 340,000 customers in southeastern Idaho; Washington Water Power,[36] serving approximately 100,000 customers in northern Idaho; Utah Power & Light Company (UP&L - PacifiCorp),[37] serving more than 50,000 customers in southeastern Idaho; and Atlanta Power Company serving Atlanta, Idaho. Investor-owned electric utilities are "owned" by stockholders and managed by a Board of Directors. These public utilities are operated for profit and are regulated by the Idaho Public Utilities Commission (PUC) under state law.[38] See the map in Exhibit No. 1 for the location of their service territories.

The second type of distribution supplier is the electric cooperative. There are twelve member-owned electric cooperatives in Idaho.[39] Cooperatives were originally formed to supply electricity to rural areas of the nation by obtaining federal low-interest loans from the Rural Electrification Administration (REA). The REA was created in 1935 by President Franklin Roosevelt's executive order.[40] Cooperatives are member-owned and are not operated for profit.

The third form of distribution supplier in Idaho is the municipal electricity department or supplier. Electricity is provided as a public service by the local municipality and is subject to the municipality's control and management. There are eleven municipal electric suppliers in Idaho.[41] The rates charged by electric cooperatives and municipal suppliers are set by their respective authorities and are not subject to the jurisdiction of the PUC.[42] See Exhibit No. 2.

2. Generation Suppliers

Idaho's investor-owned utilities each generate electricity needed to supply their distribution customers. With the exception of Atlanta Power (entirely hydro), these public utilities predominantly generate power from hydropower facilities and thermal power (gas/oil/coal) facilities or acquire power under contract from PURPA generating facilities.[43] No Idaho supplier generates power from nuclear plants. Idaho Power has 16 hydro facilities with a capacity of 1,700 mW and three coal-fired steam facilities with an installed capacity of 1,000 mW. Most of the company's hydro facilities are located on the Snake River with its three Hells Canyon dams representing about 66% of the company's hydroelectric generation. All its thermal plans are located out of state. Approximately 7% of its power sold is derived from PURPA contracts.

Washington Water Power has nine hydropower facilities and five steam generators. WWP has steam capacity of 711 mW and hydro capacity of 1,570 mW. About 8% of WWP's power sold is from PURPA contracts. UP&L (a division of PacifiCorp) has about 50 hydro facilities and 17 steam generators in its multistate system. Its thermal plants have a capacity of about 7,600 mW, while its dams possess a capacity of approximately 1,078 mW. About 2% of its power sold is from PURPA contracts. Although Idaho's generators possess thermal facilities, only WWP has a thermal generating plant in Idaho.[44] The mix of generating resources of the three investor-owned utilities is shown below.

	Generation		(in mills)	
	Hydro	Thermal	Hydro	Thermal
Idaho Power	69%	31%	1.8	19.1
Water Power	66%	34%	1.5	19.6
UP&L	11%			

1996 National Average Costs 5.95

Sources: FERC Form No. 1; Energy On Line

Few of Idaho's electric cooperatives or municipalities generate their own hydropower.45 Most of these public distribution suppliers obtain their energy from the federal BPA. BPA markets nearly half of the Northwest's energy supply from the 29 dams located in the Columbia River Power system. Dams operated by the Bureau of Reclamation and the Army Corps of Engineers have a generation capacity of about 16,000 mW.46 BPA also controls 75% of the region's transmission lines. On average, BPA delivers approximately 12% of the electricity consumed in Idaho via the cooperatives or municipalities distribution suppliers. In a 'normal' water year, about 60% of the electricity consumed in Idaho is produced by hydro facilities. During drought years, nearly 60% of Idaho's electrical energy is met from out-of-state sources.[47]

B. Current Economic Aspects of Idaho Electric Service

1. Consumer Classifications and Rates

a. *Customer Classes.* Similarly situated customers are normally grouped into customer "classes." This ensures that each customer in the class is assessed the same rate for electrical service. Typically, the type and character of electric service is similar to all the customers in a particular class. The cost of serving a particular class is recovered by the rates applicable to the services provided to members of the class. This recovery mechanism is commonly referred to as "rate averaging." Idaho's electric suppliers generally recognize five categories of customers:

i. Residential: The largest class of customers is residential. Although this is the largest class in terms of number of customers, it does not necessarily represent the class or group of customers that uses the greatest amount of electricity. Idaho residential customers enjoy the lowest electrical rates in the nation.[48]

ii. Commercial: Commercial customers form the next type of customer class. These typically involve business operations or other kinds of commercial enterprises.

iii. Industrial: Industrial customers generally use larger quantities of electric power in a manufacturing or industrial process. As indicated in Exhibit No. 3. Idaho Power has just over 100 industrial customers, but they collectively consume more energy than nearly 300,000 residential customers.

iv. Irrigation: Most irrigation power in Idaho is supplied by Idaho Power or UP&L. Approximately 15% of Idaho Power's energy is used for irrigation at an average rate of 3.84 cents/kWh, while UP&L's irrigation load is about 30% of its fixed power sales with rates ranging from 3.65 to 6.62 cents/kWh. Exhibit No. 4. These customers are normally irrigating agricultural land with electric pumps. Service is usually seasonal.

v. Special Contracts: The last type of customer isn't a class but represents individual "special contract" customers. These customers are usually the largest utility customers normally engaged in industrial or manufacturing operations. In some cases, these customers consume by themselves loads accounting for a significant portion of all jurisdictional energy. For example, Idaho Power's four largest customers represent approximately 22% of its Idaho load. In addition, WWP's largest customer is Potlatch Corporation that represents approximately 25% of the northern Idaho utility's load. Contracts between the utility and its largest customer must be approved by the PUC to ensure that other customer classes are not detrimentally affected. Idaho Code § 61-502. Special contract customers include FMC, Micron, Simplot, INEEL, Potlatch, Monsanto, and Nu-West. These customers generally obtain power at lower rates for several reasons such as interruptible service, lower cost of service, and a fairly constant level of demand.

b. *Rates*. The PUC uses a host of factors when setting the rates for customer classes. The primarily factor is each individual utility's cost of serving its customer classes, followed by factors (in no particular order of importance) such as: the quality of electricity used, the nature of the use, the time of use, the pattern of operation, the contribution to peak load, the cost of storage, and other economic incentives. An example of how these factors relate to various classes may be helpful. Even though FMC and all 12,000 of Idaho Power's irrigation customers consume equivalently the same amount of energy, FMC represents a single point of delivery versus 12,000 points of delivery. FMC also uses "interruptible" power, while irrigators may receive "firm" power. In addition, FMC's demand for power is evenly spread across the entire year versus just the irrigation season. The seasonal use of power for irrigation contributes to peak loads on the system. Idaho State Homebuilders v. Washington Water Power, 107 Idaho 415, 680 P.2d 350 (1984).

As previously mentioned, the single greatest factor contributing to low Idaho rates is the fact that hydro power represents the greatest amount of generation and that hydro power is in some respects the "cheapest" form of energy to generate. See Exhibit Nos. 5 and 6. In 1997, for example, Idaho customers had the lowest average price for electricity in the United States at 3.87 cents per kWh. In contrast, Hawaii had the highest average price in the nation of 12.49 cents per kWh, while the average price for all electrical customers in the United States was 6.85 cents kWh.[49] In addition, Idaho Power was recently declared the most efficient utility in the United States with WWP ranking number five.[50]

As viewed in Exhibit Nos. 7 and 8, Idaho customers pay the lowest rates in the Pacific or Mountain States. In comparison, California residential customers pay approximately 2? times the Idaho residential rate.

A common concern expressed by many is that Idaho's low retail may be in jeopardy if retail competition is introduced. As expected, several studies have been undertaken to examine this very question. Some studies predict higher prices in the northwest (and Idaho) if restructuring occurs, while other studies claim that retail competition will cause prices to reduce even further. This Report makes no attempt to evaluate these studies. We merely note that this is an area of contention that should be carefully reviewed. See Appendix.

C. Current Regulation of Idaho Electric Industry

1. Federal Law

a. *Federal Power Act—Historical Background.* In 1890, Congress passed legislation prohibiting the construction of obstructions to navigation without the approval of the Secretary of War. This legislation was superceded by the Rivers and Harbors Act of 1899 that, in part, made it unlawful to build dams on navigable rivers without the consent of Congress and the approval of the Corp of Engineers. In 1920, Congress enacted the Federal Water Power Act (now known as the Federal Power Act), 16 U.S.C. §§ 791a-825r, vesting authority over the licensing of construction and operation of dams and other hydroelectric projects in the FERC. Idaho Power Co. v. State by and through the Dept. of Water Resources, 104 Idaho 575, 661 P.2d 741 (1983). Besides licensing and inspecting hydroelectric projects, FERC regulates the interstate transmission of natural gas, oil by pipeline, and electricity. FERC also exerts jurisdiction over power generation sold to other utilities at wholesale.

b. *Federal Power Act—Relicensing*. FERC administers a licensing program for major non-federal hydropower facilities. A FERC license is issued for a fixed period of time, not to exceed 50 years for new construction to 30 years for relicensing of projects without new facilities or large mitigation expenses. The licenses must be renewed if the project is to continue operating after the expiration of its initial license.

The Federal Power Act charges FERC with balancing power and non-power values in its licensing decisions. In 1986, the Electrical Consumer Protection Act revised the licensing process to give much greater weight to environmental concerns. FERC must develop specific measures to benefit fish and wildlife, recreation, water quality, and other uses that have been affected by hydropower development. FERC has the obligation to "adequately and equitably protect, mitigate damages to, and enhance, fish and wildlife." 16 U.S.C. § 797(e).

Between 1999 and 2010, twenty large hydropower projects in Idaho are due for relicensing. These projects have a total installed capacity of 2,300 mW and generate approximately 1,320 average megawatts (AmW) of energy per year. One AmW of energy is sufficient to serve the needs of approximately 630 households. The total annual energy produced at these projects is equivalent to more than half of the energy consumed in Idaho by all consumers.

The relicensing process is particularly significant for Idaho Power Company. Projects due for relicensing represent 87% of Idaho Power's hydropower generating capacity. The stakes for WWP are also substantial. The Cabinet Gorge and Noxon Rapids projects together produce approximately 47% of WWP's peak generating capacity. Both projects are due for relicensing in early 2001. Relicensing is less important for PacifiCorp because its Bear River projects are relatively small and comprise only a tiny fraction of PacifiCorp's overall generation.

In determining whether to relicense a project, FERC is required by law to consider a broad array of environmental values and to carefully balance the competing uses of a waterway. The Federal Power Act makes it clear that relicensing represents a new decision regarding environmental requirements at each project rather than a continuation of the status quo.

The relicensing process is rigorous and time consuming. The owners of projects due for relicensing are required to consult the public as well as government agencies regarding environmental studies and measures to mitigate for the projects' impacts on fish, wildlife, recreation, and other public values.

The economic impact of relicensing is difficult to predict because relicensing costs depend on issues unique to each project. However, a study by the Electric Power Research Institute (EPRI) sheds some light on general trends.[51] The EPRI study found that costs for 36 hydropower projects relicensed between 1993 and 1995 varied significantly. For projects with an installed capacity of 12 mW or greater, costs ranged from roughly $100 to $130 per installed kW of capacity. The categories of costs considered in the report included: 1) capital costs for items such as recreational facilities and new installations to protect fish and wildlife; 2) annual operations and maintenance costs associated with PM&E measures; and 3) annual energy costs due to operational changes. The results of the EPRI study should not be viewed as predicting the outcome of any particular relicensing proceeding. Nevertheless, the study suggests that relicensing could be a significant, but not dominant, factor affecting the economics of particular hydropower projects.

Indian tribes also play an important role in regulation of hydropower facilities under the Act. Several tribes in Idaho have expressed a strong interest in hydropower development and operations based on their assertion of off-reservation hunting and fishing rights reserved by treaty. The Act requires FERC to consider, in all licensing decisions, the recommendations (including fish and wildlife recommendations) of Indian tribes affected by the project. 16 U.S.C. § 803(a)(2)(B).

The extent of FERC's jurisdiction in the area of water rights has been a subject of much tension between the states and FERC. This issue is discussed more fully in the "State Water Law" section beginning at page 24.

c. *Clean Water Act.* In addition to the Federal Power Act, hydropower facilities are subject to the Clean Water Act (CWA). Section 401 of the CWA requires that, prior to issuing a license, FERC must receive a certification from the state water quality agency that the proposed project complies with state water quality standards. The authority under Section 401 represents one of the few opportunities for the states to regulate federally licensed hydropower facilities.

The United States Supreme Court has interpreted Section 401 to permit states to require that hydropower operators not only meet specific numeric water quality criteria but also protect beneficial uses designated by a state's water quality standards. PUD No. 1 of Jefferson County v. Washington Dept. of Ecology, 511 U.S. 700 (1994). The Supreme Court specifically held that nothing in the CWA prevents a state from requiring minimum streamflow conditions in a Section 401 certification.

d. *Public Utility Regulatory Policies Act (PURPA).* In 1978, the United States was faced with an energy shortage caused ostensibly by the Arab oil embargo. At the time, the generation of electricity consumed more than 25% of all energy resources used in the United States. Based in part upon their reliance on oil and gas, electric utilities were plagued with increasing costs and decreasing efficiency in the use of their generating facilities. "Congress accordingly determined that conservation by electric utilities of oil and natural gas was essential to the success of any effort to lessen the country's dependence on foreign oil, to avoid a repetition of the shortage of natural gas that had been experienced in 1977, and to control consumer costs." Afton Energy v. Idaho Power Company, 107 Idaho 781, 783, 693 P.2d 427, 429 (1984) quoting FERC v. Mississippi, 456 U.S. 742 (1982).

To encourage the promotion and development of renewable energy technologies, Congress enacted PURPA. Section 210 of the PURPA requires that electric utilities offer to purchase the electric power produced by co-generators or small power producers, thereby reducing the nation's reliance on oil and natural gas. PURPA and its FERC implementing rules require that utilities purchase power from co-generators for acquiring electric power, either purchased from another source or through its own production. 18 C.F.R. § 292.101(b)(6). Avoided costs are costs that the utility would otherwise incur. They are to be just and reasonable to the electric utility's consumers and not discriminate against qualifying co-generators. Rosebud Enterprises v. Idaho PUC, 128 Idaho 609, 917 P.2d 766 (1996). In calculating the Idaho avoided cost rates it was presumed that utilities would need to build expensive coal-fired plants if they were to produce the power themselves. As portrayed in the table on page 17, a substantial portion of power is produced by low-cost hydro facilities.[52] Thus, when the existing costs of generation is compared to the avoided costs, the utilities "avoided cost rates" are much higher than the average rate of their existing generation costs.

e. *EPAct.* The EPAct was a vast piece of legislation with multiple objectives. 42 U.S.C. §§ 13201, et. seq. As previously mentioned, the EPAct encourages greater competition into the wholesale electric power generation. Another provision of the EPAct provided the FERC with greater authority and latitude with respective mandatory transmission of power, or "wheeling." The EPAct also laid the groundwork for FERC jurisdiction over transmission. However, the EPAct specifically prohibited the FERC from ordering retail wheeling.

f. *FERC Order No. 888.* FERC Order No. 888 and its successors (Nos. 888A, B, and C) sought to open transmission systems to all wholesale buyers and sellers under regulated terms and conditions guaranteeing equal access. Order No. 888, issued in 1996, required each public utility that owned transmission systems to file an "open access" transmission tariff that met certain detailed standards of non-discrimination and pricing. In its order, the FERC recognized that increased competition could cause some existing generating utilities to lose sales making it impossible for these entities to fully recover their investments. Consequently, the FERC decided that electric utilities offering transmission access were entitled to collect the costs of generating plants that could not be recovered from the competitive wholesale market-stranded costs.[53]

2. <u>State Law</u>

a. *Public Utilities Law.* As previously mentioned, the PUC regulates the four investor-owned electric utilities serving more than 80% of all customers in Idaho. The cooperatives and municipalities are self-regulating. The PUC was created in 1913 "to supervise and regulate every public utility in the state and to do all things necessary to carry out the spirit and intent of the provisions of [the Public Utilities Law]."[54] The Idaho Public Utilities Law was modeled upon the California Public Utilities Law.[55] Electric public utilities are under a statutory duty to furnish and provide such service as shall promote the safety, health, comfort, and convenience of their customers and the public. Idaho Code § 61-302.

Title 61 of the Idaho Code sets out the statutory standards under which the PUC regulates the conduct of electric utilities in Idaho. Among other duties, the PUC:

- Issues "franchises"—specifically referred to as "certificates of public convenience and necessity"—authorizing electric corporations to offer service in Idaho. Idaho Code § 61-526. The certificates permit the investor-owned utilities subject to the PUC's jurisdiction to operate in specific service territories.

- Sets the "just and reasonable" rates for electric service. Idaho Code § 61-502.

- Insures that utilities only charge the rates authorized and on file with the PUC. Idaho Code § 61-310.

- Establishes rules for safety and other utility practices/services. Idaho Code §§ 61-303 and 515.

b. *The Stabilization Act.* The Electric Supplier Stabilization Act (ESSA) was enacted by the Idaho Legislature in 1970. Its purpose is to "promote harmony among and between electric suppliers furnishing electricity within the state of Idaho, prohibit the 'pirating' of customers of another supplier, discourage duplication of electric facilities, and stabilize the territories and customers served with electricity by such suppliers." Idaho Code § 61-332. The ESSA establishes a regulatory scheme for determining which distribution supplier serves customers in Idaho.[56] It specifically prohibits electric suppliers from providing service to a current or former customer of another distribution supplier without the written consent of the other supplier. The ESSA also contains rules for determining which supplier may serve a new customer:

Where only one supplier has an existing line within 1,320 feet of the customer, or where two or more suppliers have existing service lines within that distance, the supplier having the closest line "has the right to provide service." Idaho Code § 61-322C(2), (3).

If no supplier has a service line within that distance or if two or more electric suppliers have lines which are equal distance from the new customer, then the customer has the right to choose among potential electric suppliers. Idaho Code §§ 61-332C(1) and (4).

c. *Transfer of Electric Facilities*. In 1951, the legislature enacted several statutes limiting the right of any electric utility to sell or transfer any property used in the generation, transmission, distribution or supply of electric power without the specific approval of the PUC. Idaho Code §§ 61-327 and 61-328. The failure to acquire the approval of the PUC has extreme consequences including the property escheating[57] to the state of Idaho and the possibility of criminal penalties. Idaho Code §§ 61-329 and 61-331. Idaho Code § 61-328 contains the standards that the PUC uses to evaluate any sale or transfer of investor-owned electric utility property. The PUC may only approve the transfer if it finds that :

1. The applicant has the intent and financial ability to operate and maintain utility property;
2. The public interest will not be adversely affected; and
3. The transaction will not cause an increase in the cost of rates of electric service.

The PUC shall not authorize a transaction if the sale or transfer of the property violates any of "the prohibitions set forth in this Act [above]." Idaho Code § 61-328.

d. *State Water Law.* Throughout most of the nation, electric utility restructuring is viewed solely as an economic issue. This is so because much of the nation's electricity is generated by facilities using fuels that serve a single purpose—creation of electricity. Thus, electricity is viewed as a commodity whose cost will be driven down by open competition. This paradigm does not apply to Idaho.

At present, approximately 60% of Idaho's electricity comes from hydropower generation. The fuel that turns the turbines to generate this electricity is also the waters of the state, which are essential to every other aspect of our lives. Thus, electric utility restructuring in Idaho is a multi-faceted natural resource issue. In recognition of this fact, Idaho water law contains a carefully crafted balance between use of water for hydropower and other uses. Political leaders of Idaho would be remiss if they failed to consider the implications of electric utility restructuring on this statutory scheme.

The root of Idaho's current regulation of the use of water for hydropower purposes extends back to 1927. As the hydropower industry began to take hold, state leaders were concerned that power companies might appropriate the entire flow of rivers and thereby monopolize the waters of Idaho. Thus, Article 15, § 3 of the Idaho Constitution was amended to expressly provide that the state "may regulate and limit the use [of water] for power purposes."

One of the first implementations of this provision occurred with the construction of Idaho Power Company's Hells Canyon Complex. In the 1940s, the United States proposed to build the high Hells Canyon Dam. Idaho Power and its supporters claimed that the Federal Government would assert a superior right to upstream water. In what can best be described as a social contract with the citizens of Idaho, Idaho Power agreed that if it were given the right to build dams in Hells Canyon, it would subordinate its right to use water for the generation of hydropower to all upstream consumptive uses. With this assurance, Idaho political leaders aligned with Idaho Power and its proposed project prevailed over the federal proposal. the FERC licenses issued to Idaho Power contained a provision expressly subordinating its use of water for hydropower purposes to all upstream consumptive uses. Unfortunately, not all of Idaho Power's FERC licenses and state water right licenses for hydropower purposes were amended to include this subordination provision.

In the 1970s, Idaho Power, in response to an increasing demand for electricity, proposed the development of a coal-fired facility. Seizing upon the absence of a subordination provision in the water right licenses for the Swan Falls[58] hydroelectric facility, 32 customers filed a petition with the PUC in 1977 asserting that the Company had failed to protect its water rights against upstream depletions. They argued that the increasing amount of land under irrigation in southern Idaho resulted in a decrease of the Snake River flows at Swan Falls. In response, the Company filed suit to protect its water rights from diminution. Much to the surprise of the Company and state officials, the Idaho Supreme Court held that the provisions of the Hells Canyon FERC license did not subordinate the Company's Swan Falls water rights and remanded the case for trial on the issue of whether the Company had lost a portion of the Swan Falls rights through other affirmative defenses. Idaho Power, 104 Idaho at 575, 586-88, 661 P.2d at 741, 752-54.

After extended litigation on remand, the Governor, the Attorney General, and Idaho Power Company engaged in extended negotiations that resulted in what is commonly referred to as the Swan Falls Agreement in 1984. This agreement provided the framework for the current statutory balance between the use of water for hydropower purposes and other beneficial uses.[59]

Idaho Code § 42-203B expressly provides that the State's existing water rights are subordinated to upstream consumptive uses. this subordination may occur by one of two methods. First, hydropower water rights may be subordinated by agreement. The Swan Falls Agreement is such an agreement. Idaho Code § 42-203B(5). It subordinates all of Idaho Power Company's hydropower water rights in excess of 3,900 cfs from April 1 to October 31 and 5,600 cfs from November 1 to March 31 to upstream consumptive uses.[60] Under section 42-203B, the Governor holds the subordinated portion of the water right in trust for the benefit of Idaho Power Company and the citizens of Idaho. A person desiring to appropriate trust water must satisfy certain public interest criteria. Idaho Code § 42-203-C. This public interest criteria provides a mechanism for balancing the sue of water for hydropower purposes versus other beneficial uses. Second, section 42-203B(3) provides that hydropower water rights not defined by an agreement are subordinated down to the amount of any state minimum stream flow. The implementation of this provision has not been tested.

The Swan Falls Agreement also led to enactment of Idaho Code § 61-502B, which provides that any gain upon the sale of a public utility's water right(s) used for the generation of electricity shall accrue to the benefit of the customers. This provision reflects the fact that water is a multi-purpose resource and that ratepayers have a right to the benefits generated by this public resource.

As noted previously, the Federal Government has assumed an expansive role in the area of hydropower regulation under the Federal Power Act. Section 27 of the Act provides that:

> Nothing contained in this chapter shall be construed as affecting or intending to affect or in any way to interfere with the laws of the respective States relating to the control, appropriation, use, or distribution of water used in irrigation or for municipal or other uses, or any vested right acquired therein.

While on its face, this provision appears to be an expansive statement of federal deference to state water law, the United States Supreme Court has limited its reach. In California v. FERC, 496 U.S. 490 (1990), the Court considered whether section 27 reserved to California the authority to set minimum stream flows below FERC licensed projects. Citing a prior opinion, the Court stated:

> The effect of § 27, in protecting state laws from supersedure, is limited to laws as to the control, appropriation, use or distribution of water in irrigation or for municipal or other users of the same nature.

Id. at 498, citing First Iowa Hydro-Elec. Coop. v. Federal Power Commission, 328 U.S. 152, 175-76 (1946). Further confusion regarding the scope of section 27 arises from Federal Power Commission (FPC) v. Oregon, 340 U.S. 435 (1955). Some have argued that FPC stands for the proposition that FERC projects located on reserved lands of the United States are exempt from state water law. While such a reading does not comport with the narrow holding of the case, FPC in combination with First Iowa and California, raise significant questions regarding the respective authorities of the State and FERC in the area of regulation of use of water for hydropower purposes.

The current electric regulatory scheme has, in part, minimized the potential conflict between FERC and states over regulation of water by limiting the unrestricted sale of electric power (i.e., hydropower) within established service areas. In a deregulated environment where there will be no limits on where electricity may be sold, it is reasonable to expect that utilities will test the limits of state regulation of water for hydropower purposes. Because the United States Supreme Court has held that water is an article in commerce, Sporhase v. Nebraska, 458 U.S. 941 (1982), new owners of the hydroelectric facilities may seek to abandon their predecessors' practice of subordinating hydropower water rights to upstream consumptive uses. Indeed, this scenario is being played out in the state of Montana at the present time. See Exhibit No. 9.

While, as a practical matter, Idaho water law and the Swan Falls Agreement provide many protections against out-of-state exportation of water, it is equally clear that, in a deregulated environment, current state water laws alone are not sufficient to ensure Idahoans the benefit of power generated by Idaho rivers. Indeed, because of the Supreme Court's interpretation of Section 27 of the Federal

Power Act, electrical restructuring raises significant questions regarding whether Idaho will be able to protect the delicate balance it has struck between use of water for hydropower and other beneficial uses. "In a state where most of the generation is hydro based and where water rights and the use of water is so embedded in the livelihood of the state and its citizens, the potential impacts on water rights and water use must be addressed." Exhibit 10, Idaho Water Users Association, Deregulation of the Electric Utility Industry: Some Basic Water Related Issues, at 5 (February 1997).

Aside from the interplay between state and federal law over the use of water for hydropower purposes, there are many social issues that will arise from any deregulation of electric utilities in Idaho. Many of these issues are set forth in the report prepared by the Water Users. *Id.* As did the Water Users, we conclude that these issues must be answered as a predicate to any deregulation of electric utilities.

3. Idaho Court Decisions

a. *Blomquist Case.* After the Public Utilities Laws were enacted, the Idaho Supreme Court was asked to review the constitutionality of the Act. In Idaho Power & Light Company v. Blomquist, the Court found that there was nothing in the Idaho Constitution that prohibited the legislature from enacting laws prohibiting competition between public utility corporations. 26 Idaho 222, 141 P. 1083 (1914). The Court specifically stated that the constitutional "police power . . . is sufficiently broad and comprehensive to enable the legislature to regulate public utilities in order to promote the health, comfort, safety and welfare of society." *Id.* at 242. Quoting from another case, the Court observed that the legislature had adopted:

> regulation and control as our reliance against the evil effects of monopoly, rather than competitive action between two or more corporations, where such competition will greatly increase the aggregate cost of supplying the needs of the public, and perhaps cause other serious inconveniences . . . . The state, through the regularly constituted authorities, has taken complete control of these corporations so far as is necessary to prevent the abuses of monopoly. Our statutes are founded on the assumption that, to have two or more competing companies running lines of gas-pipe and conduits for electric wires through the same streets would often greatly increase the necessary cost of furnishing light, as well as cause great inconvenience to the public and to individuals from the unnecessary digging up of the streets from time to time, and the interference with pavements, street railroad tracks, water pipes and other structures . . . .

Id. at 240.

The Court also noted that the legislature clearly delegated authority to the PUC to fix rates and service. The Court stated that the PUC "must consider many facts, and must determine those questions in fairness to the public as well as to the public utility." *Id.* at 255-56. Contrary to the assertion of some of the parties, the Court found that the regulation of utilities does not create unrestricted monopolies but a monopoly that is governed and controlled by law and not permitted to charge more than just and reasonable rates.

b. *Standard of Review.* In Intermountain Gas Company v. Idaho PUC, the Supreme Court set out the standard to be applied when reviewing appeals from the Commission. The Court stated:

> Our purpose is not to analyze each step of the rate-setting process to determine whether the regulatory agency was correct in its decision, but to look at the overall effect of the rate fixed to determine whether the return to the utility is reasonable and just. As the Supreme Court of the United States stated, in Federal Power Commission v. Hope Natural Gas Co., 320 U.S. 591, "It is not the theory but the impact of the rate order which counts. If the total effect of the rate order cannot be said to be unjust and unreasonable, judicial inquiry under the Act is at an end. The fact that the method employed to reach the result may contain infirmities is not then important . . . ."

97 Idaho 113, 120, 540 P.2d 775, 782 (1975); Utah Power & Light Company v. Idaho PUC, 102 Idaho 282, 629 P.2d 678 (1981).

c. *PURPA Cases*. On several occasions, the Idaho Supreme Court has reaffirmed the Commission's authority to implement the policies of the PURPA. The United States Supreme Court has held that it is constitutional that the PUC enforce PURPA standards promulgated by the FERC. FERC v. Mississippi, 456 U.S. 742 (2982); Rosebud Enterprises v. Idaho PUC, 128 Idaho 609, 917 P.2d 766 (1996); Afton Energy v. Idaho Power Company, 107 Idaho 781, 693 P.2d 427 (1984).

d. *Disbursement of Sales Premium*. When investor-owned utilities sell utility assets above book value, case law provides that ratepayers receive the benefits of the transaction. In Boise Water Corp. v. Idaho PUC, 99 Idaho 158, 161-62, 578 P.2d 1089, 1092-93 (1978), the Idaho Supreme Court held that ratepayers are entitled to the above book proceeds for the sale of depreciable property. Miles v. Idaho Power, 116 Idaho 635, 778 P.2d 757 (1989). As mentioned elsewhere, Idaho Code § 61-502 also provides that the gain (or profits) upon sale of a utility's water right(s) used for generation "shall accrue to the benefit of the ratepayers."

e. *Snake River Antitrust Case*. In late 1996, the newly formed Snake River Valley Electric Association sued UP&L (PacifiCorp) alleging that the utility had violated federal antitrust laws by preventing the Association from providing electric power to PacifiCorp's existing customers and to the potential 'new' customers in the area surrounding Idaho Falls. PacifiCorp defended against the action arguing that it should be immune from federal antitrust liability under the State Action Immunity Doctrine first laid out in Parker v. Brown, 317 U.S. 341 (1943). More specifically, PacifiCorp argued that its conformance to the ESSA shields it from federal antitrust liability.

In April 1997, the federal District Court issued a memorandum decision and holding that the ESSA did not grant antitrust immunity to PacifiCorp. Using United States Supreme Court precedent, the District Court noted that State Action Immunity would only be conferred upon PacifiCorp if: 1) the ESSA clearly articulated and affirmly expressed state policy permitting anti-competitive conduct by regulated parties; and 2) that the state "actively supervised" the anti-competitive actions of private parties to ensure that the state's interest are being met. California Retail Liquor Dealers Ass'n. v. Midcal Aluminum, 445 U.S. 97 (1980). While the Court held that the ESSA clearly articulated the state policy that allowed PacifiCorp to prohibit access to its current customers, the Court concluded that the Company had not demonstrated as a matter of law that the state of Idaho actively supervised the implementation of that policy by private suppliers of electric power. The Attorney General then entered the case and asked the Court to reconsider its decision.

In April 1998, the Court reversed itself and found that the ESSA did confer antitrust immunity upon PacifiCorp's actions. Snake River Valley Electric Ass'n v. PacifiCorp, Slip. Decision and Order No. 96-0308-E-BLW (April 20, 1998). In essence, the District Court found that the second prong of the Midcal test (active supervision) was indeed met. The Court cited three main reasons for granting summary judgment to the state. First, the Court noted that the United States Supreme Court had recognized at least twice in dicta that a state statute may satisfy the "active supervision" requirement by specifically restraining competition. In essence, the Court recognized that the ESSA absolutely prohibits the pirating of current and former electric customers. The Court characterized the

ESSA as "self-policing" because it leaves no discretion for anti-competitive conduct.

Second, the Court took judicial notice of the state's evidence showing four ESSA cases in Idaho courts. The Court observed that "the tally of [four] Idaho court cases involving ESSA" was exactly the number of decisions in a recent antitrust case from California where the Ninth Circuit found that four PUC decisions satisfied the active supervision test. Nugget Hydroelectric Company v. Pacific Gas & Electric Company, 981 F.2d 429 (9th Cir. 1992).

Third, the Court accepted the state's argument that it would be inequitable and illogical to require the ESSA to be violated in multiple instances before State Action Immunity could be conferred. The Court observed that the ESSA "so unambiguously forbids competition in broad circumstances that it is reasonable to assume that private entities have no difficulty understanding the statute well enough to comply."

4. PUC Decisions

a. *Power Cost Adjustment Mechanisms.* For Idaho's two utilities that are predominantly hydro generators, the PUC approved a power cost adjustment (PCA) mechanism. The PCA mechanism reflects the annual variation in Idaho Power's and WWP's cost of supplying electricity as a result of changing stream flow conditions at the companies' hydro facilities. The PCA mechanism also contains other adjustments including PURPA contract purchases. The annual PCA rate adjustment is added to or subtracted from the utilities' approved rate base depending on the stream flows as calculated by the National Weather Service. Generally, in years with good stream flows, rates go down because the water supply is abundant and the utilities are able to generate sufficient power at their hydro facilities. Conversely, in "poor" water years, rates go up because the supply of water will be below the established average.

WWP's PCA mechanism was first established in 1989 in Order No. 22816. Since its inception, the company's Idaho customers have received five rebates (where rates are lowered from a base level) and three surcharges (where customer rates are increased from the base level). One of the advantages of the PCA mechanism is that it mitigates significant weather-related impacts in the company's operations. WWP has recently requested that the PUC terminate the PCA mechanism. PUC Order No. 27464. Idaho Power's PCA was initiated in 1992. Since that time, there have been three rebates and there have been three surcharges. Since their inceptions, the companies' PCA mechanisms have undergone various revisions to reflect changes in costs and other load factors.

b. *The PUC's Preliminary Investigation*. In 1996, the PUC undertook an investigation to examine changes occurring in the electric industry. The purpose was to identify issues facing Idaho's electric utilities as states embroiled initiate electric restructuring. In its findings released in August 1996, the PUC expressed concern regarding the effect that "competition" will have on the majority of Idaho's customers. The PUC noted several reasons why the state should move cautiously in examining electric restructuring. First, the PUC stated that customers on the average pay some of the lowest electric rates in the nation. "While some of Idaho's larger customers may be able to obtain lower rates through contract sales with other energy suppliers due to their size in buying power, we find that there is evidence suggesting that the majority of Idaho's ratepayers may experience an increase in rates over the long term." Order No. 26555 at 3.

Second, the PUC expressed concern that full or partial deregulation of the electric industry may result in the diminution of the quality of service Idaho ratepayers currently enjoy. The 1996 power outages in the western United States should serve as a reminder about the importance of maintaining reliability in the delivery of electric service.

Finally, the PUC also expressed concern that if large customers were to leave the distribution system, then smaller residential and business customers may ultimately pay higher rates. This occurs because the remaining customers would shoulder costs formerly recovered from the larger customers.

c. *Unbundled Cost Cases*. In July 1997, the PUC initiated an inquiry to examine the "unbundled costs" of Idaho's electrical suppliers pursuant to Idaho Code §§ 61-338 and 61-339. Unbundled costs represented the separated and categorized costs of supplying electric power to customers in Idaho including the costs of generation, transmission, distribution, and other public purposes.

- Generation costs—included both fixed costs (primarily return on investment and depreciation) and variable costs including fuel, purchased power, and operating and maintenance expenses). The PUC also included the costs of alternative energy sources, demand-side management, and fish mitigation costs in this category.

- Transmission and distribution—costs included in this category are generally described as the costs for transmission and distribution facilities, metering, meter reading, billing, and other customer services.

- Public purpose costs included—universal service (which does not currently exist) and low-income assistance.

- The three large investor-owned utilities are to annually update its unbundled cost report on or before July of every year. PUC Order Nos. 27211, 27676, 27678, and 27679.

d. *FMC-Idaho Power Contract.* In April 1998, the PUC approved a new contract between Idaho Power and its largest customer, FMC. Historically, the largest customers of an electric utility have been provided service under a "special contract."[61] Special contracts allow a utility and its largest customers to customize services and rates to better suit the requirements of both. As the case with any special contract, the PUC's responsibility is to determine or apportion the costs of serving that customer and establish the rates necessary to recover the costs. PUC Order Nos. 27551 and 27463.

The April contract replaced a 25-year-old contract previously entered into in 1973. Under the 1973 contract, Idaho Power supplied FMC with interruptible electric power in two blocks—120 mW of primary power and 120 mW of secondary power. Under the old contract, when the power was interrupted by Idaho Power, then the utility would use its "best efforts" to replace the power from other sources. In the last six years, this replacement power cost Idaho Power an average of $3.1 million per year.

Under the new contract, power is still provided in two blocks—the first being 120 mW and the second being 130 mW. However, the first block is a fixed-priced, "take or pay contract." In other words, Idaho Power recovers its full cost of providing power whether FMC uses the power or not. The second block of pricing is supplied by Idaho Power only upon FMC's written request. The price of power supplied for the second block is established by the existing market price. FMC pays all transmission and transaction costs required to deliver the second block of power. If FMC calls for the second block of power and then is unable to utilize that power (e.g., because one of its phosphate furnaces is down), FMC notifies Idaho Power that the utility may sell the power elsewhere or use it to serve other customers. All costs associated with such transactions are borne by FMC. If Idaho Power sustains a loss by selling the second block of power, then FMC pays the shortfall. If Idaho Power can dispose of the second block of power at a profit, then the profits are shared 75% for FMC and 25% for Idaho Power after FMC pays all transaction costs. At all times, the power is purchased by and sold by Idaho Power.

In approving the contract, the PUC found that the new contract represents a substantial rate increase over the old contract. The PUC also acknowledged that the utility would avoid the annual cost of $3.1 million for replacement power and the "take or pay" provision for the first block of power will fully recover Idaho Power's costs. Turning to the second block, the PUC specifically found that FMC will not use the provisions "as an entrepreneur enterprise." The resale provision for the second block is only intended to allow FMC to mitigate the effects of buying power in advance that it no longer needs. To ensure that this provision is being honored, the PUC ordered Idaho Power to report the sales and prices associated with the second block. If it appears that the resale provisions are being misused, then the PUC specifically retains the authority to re-examine this issue.

Some argued that FMC's ability to call for power and have Idaho Power sell unused power is the equivalent of retail competition. However, the PUC noted that at all times Idaho Power was recovering its full cost of serving FMC and Idaho Power retained ownership of all power. In its first report (Fall 1998), Idaho Power stated that only a small amount of second block power was sold since the contract was approved and FMC did not profit from the sales.

e. *Pilot Projects and Market Rate Experiments.* During the last three years, the PUC has encouraged the investor-owned utilities to be responsive to customers' requests for different rate structures and services. In its preliminary investigation mentioned above, the PUC encouraged utilities and interested groups to continue making innovative proposals. Order No. 26555. In response, WWP and Idaho Power have both implemented several experimental projects subject to PUC monitoring.

In April 1997, the PUC approved WWP's pilot programs known as More Options for Power Service (MOPS) and MOPS II. Under the MOPS programs, residential, commercial, and agricultural customers in WWP's northern Idaho service area were allowed to purchase capacity and energy from a list of eligible suppliers. In MOPS II, customers were provided with access to a number of energy service alternatives including partial wood generated power, partial wind generated power, 100% wood power generation, and 100% wind power generation. Order Nos. 27351 and 26884. In April 1997, the PUC approved Idaho Power's "market-based pricing service pilot program" in which larger business customer could have all or as little as one-third of their load priced at market prices. Of the ten customers eligible to participate in the program, no customers actually opted to participate in the pilot program. Order No. 26872.

V.

CURRENT CONSIDERATIONS IMPACTING RESTRUCTURING

The trends and milestone events noted above found reflection in changes in law and regulation affecting the electric industry. Together with advances in technology, these factors eventually altered market structure and market participation in the electric business, giving rise to a significant presence of non-utility generators and creating the basis for the competitive supply of electricity at wholesale. Competitive generation and wholesale wheeling form the predicate for retail electric competition.[62]

A. Changes in Federal Law

The transformation of the electric industry driven by the events described above was reflected in, and reinforced by, changes in federal law. Among the major federal enactments impacting the electric industry in this period were:

- The Public Utilities Regulatory Policies Act of 1978 (PURPA), noted earlier, created or promoted a new class of non-utility generators (small power producers and co-generators). PURPA facilitated the economic survival of these generators by requiring electric utilities to buy their output at a price based upon the cost avoided by the purchasing utility in not having to construct its own generating plants.

- The EPAct granted exemption from the Public Utility Holding Company Act (PUHCA) for certain electric wholesale generators (EWGs), thus promoting diversification in the construction and ownership of generating facilities. Additionally, the EPAct mandated FERC authority to promote wholesale wheeling through open and comparable access to the interstate transmission network. Open access, by providing non-utility generators with the competitively neutral ability to reach distant customers, constitutes a key element in competitive generation.

B. Changes in Technology

As noted above,[63] until the early 1970s, a bigger-is-cheaper approach to power plant construction prevailed in the industry, driven by the perceived economies available from large-scale facilities. Since then, technological improvements in generator construction and operation have produced smaller gas turbine units in the 100 to 200 mW range with average costs and operating efficiencies equivalent to larger units.[64] Combined-cycle gas turbines reach maximum efficiency at 400 mW, while aero-derivative turbines can be efficient at 10 mW levels.[65] Smaller units tend to require shorter lead-times for construction, can be sited strategically with respect to the transmission network or customer marketplace, and can be added incrementally as forecasted needs materialize.

Technological improvements affect non-generation aspects of the industry, as well. Operationally, advances in computing and in telecommunications equipment and networks significantly enhance the real-time operational control of the network. They also improve network reliability, including the effective integration of utility and non-utility generated power in the network. From a policy perspective, advances in information and communications capability make possible the real-time information systems essential to competitive wholesale energy markets:

- Open access non-discriminatory transmission service requires that information about the transmission system must be made available to all transmission customers at the same time . . . .

- The Standards and Protocols, which we are adopting together with this final rule, require Transmission Providers to make their OASIS [Open Access Same-Time Information System] nodes accessible through the Internet . . . . We are requiring that nodes must support the use of Internet tools. The specific tools are described in the Standards and Protocols. OASIS users will access nodes using World Wide Web (WWW) browsers.[66]

Such changes in technology alter the ways in which the industry produces and transmits electricity and, thus, affect the structure of the industry itself.

C. Changes in Market Structure

Because law and technology have changed, the nature of the marketplace has also changed for buyer and seller. New, non-utility entities have proliferated and now participate in various market areas. Some generate electricity as independent producers.[67] Others occupy the middle ground between generators and wholesale customers, performing in the roles of energy marketers and brokers.[68] Municipalities and cooperatives and, in states where retail competition is authorized, end users are banding together to aggregate demand and to negotiate for the best price, terms, and conditions for energy delivery and related services.[69] Such market changes can cause (or require) utilities to make adjustments in their operations and structures to accommodate or respond to new participants and to new market structures.

D. Disintegration of Vertical Organization

Historical justifications for the vertical integration of the typical electric utility include economic (economies of scale and scope) and operational (need for real-time control and integration in a dynamic network) considerations. The legal, technological, and market changes identified above tend to erode the basis for these justifications, at least with respect to generation. The technology of new generating plants produces efficiencies well below the historical level of multi-1000 mW central plants.[70] The legal encouragement provided by PURPA and EPAct has created a class of independent generators who construct and market the output of such plants. The development of network monitoring, open access, and real-time information systems permits integration of non-utility generated power without apparent threat to operating parameters. The emergence of marketers and power brokers provides effective vehicles for the sale and delivery of competitive generation to customers in the marketplace.

These intra-industry factors fostering competition find reinforcement from external developments. Other once-integrated, noncompetitive industries—airlines, trucking, gas pipelines, and telecommunications—have been restructured or deregulated (or both) in the past 20 years. Natural gas production was deregulated in 1978, though transmission and distribution remained regulated (subject to federal and state jurisdiction, respectively). In telecommunications, competitive long-distance services (AT&T) were severed from monopoly local exchange services (Bell operating companies) in 1982. In 1996, local exchange and exchange access functions were converted to competition, as well, by changes in federal law.[71] Although the specific results achieved in these other areas remain subject to debate, these efforts clearly manifest the political affinity for competition over monopoly, which carries over into the current electric restructuring debate.

The same pro-competitive economic, operational, and political considerations, however, do not extend to the transmission and distribution parts of the electric system. In virtually all jurisdictions, transmission and distribution functions and facilities continue to be viewed and regulated as natural monopolies. As FERC noted:

> The most likely route to market power in today's electric utility industry lies through ownership or control of transmission facilities. Usually, the source of market power is dominant or exclusive ownership of the facilities.[72]

Issues concerning market power affect policy considerations for both generation and transmission/distribution and are addressed later in this Report.

VI.

ELECTRIC RESTRUCTURING ISSUES

Any effort to restructure the electric industry raises many issues important to consumers, utilities, emerging market participants, financial markets, and Idaho's economy in general. As the Alaska Legislature noted in establishing a joint interim committee to look at restructuring issues:

> [T]he provision of adequate, reliable, and reasonably priced electrical energy is essential to the daily functions, safety, and economic well-being of Alaskans, their local communities, and the state; and
>
> . . . [E]lectric utility restructuring is a highly complex issue, carrying with it profound implications for all classes of electrical consumers; and
>
> . . . [T]he implications and ramifications of such restructuring deserve detailed, careful, and informed decision making by the Alaska State Legislature . . . [73]

Recognition of the nature and import of the major "implications and ramifications" is essential to informed, workable policy determinations.

In November 1997, Attorney General Lance urged the Interim Committee, examining electric restructuring, to consider several issues as it examined restructuring.[74] In particular, the Attorney General was concerned that introducing competition into the retail electric market place might jeopardize the low rates that Idaho customers currently enjoy. He noted that the outcome of several studies regarding the issue of costs had different conclusions. In addition, he stated that:

> Competition should not mean that rural, residential or low-income customers lose their electric service. Any transition to market-based competition must protect access at reasonable and affordable rates.
>
> Any deregulation must include measures to protect customers from deceptive and fraudulent marketing practices. Clear,

understandable consumer information must be made available to customers so that they may compare, if necessary, electric service alternatives.

Idaho's water rights must be protected. The current system of state regulation guarantees the people of Idaho the benefit of our hydroelectric facilities. Retail competition should not saddle Idahoans with the burdens associated with hydroelectric facilities.

Id.; See also Exhibit No. 12.

Electric restructuring is a complex task, presenting many arcane issues with substantial import for Idaho's electric customers as well as its economy. the list and discussion of issues below, while reasonably comprehensive, by no means exhausts either the number or the detail of matters likely to be raised when moving from a regulated to a competitive market fo· retail electric energy and associated services.

A. Cost Classifications

Any discussion of restructuring necessarily relates to costs. Under current regulatory precepts, costs of generating electricity are characterized in several different ways, depending upon the applicable frame of reference.

- Fixed vs. Variable—Fixed costs are those which do not change with changes in the quantity or volume of output (e.g., the rent paid on an office building). Variable costs change with changes in output (e.g., copper used to make wire). These terms have been occasionally equated to "Demand" and "Energy" or to "Sunk" and "Marginal" costs, but this may not be an accurate practice in every circumstance.

- Sunk vs. Marginal—Sunk costs are those made in a prior period, are not variable over time, and cannot be avoided by reducing output. Marginal costs vary with output and are thus avoidable costs (i.e., by reducing or ceasing output, an entity could avoid incurring such costs).

- Demand vs. Energy—A demand charge reflects the costs of maintaining the level of service required by customers. It is based on the highest level of kilowatts required by the customer during a specific period, and recovers some of the capital and operating costs incurred by the utility in creating and maintaining the capacity to meet the customer's needs (the customer's demand). An energy charge recovers operating costs, including those associated with cost of fuel for generation.

- Book vs. Economic Valuations—Virtually all policy debates concerning electric restructuring presume and utilize numerical data based upon the costs recorded by the utility pursuant to a Uniform System of Accounts or equivalent,[75] regulatory-imposed accounting scheme. These are termed book or embedded costs. With respect to measures of value, economic theory and case law recognize other basis for valuation, often referred to as "economic costs." The FCC, for example, has utilized the standard of "forward looking economic costs" extensively in its proceedings under the 1996 Telecommunications Act. Differences in cost recognition arising from the imposition of different cost theories can greatly impact the financial consequences of policy decisions for utilities, competitors, and consumers. They can also raise significant legal issues, such as confiscation of property and jurisdictional inconsistency.

- Pricing—Under regulation, costs tend to be priced on a basis of proved revenue requirements under the formula:

Total Revenues = Operating Expenses+Depreciation+Taxes+(RORxInvestment).

Where ROR (Rate of Return) is the percentage return a company is permitted to earn on its assets committed to the public's use, rates for electric service are then set to equal/total revenues required. However, prices for specific services under a regulatory rate design often reflect factors other than cost causation, such as uniform or "postage stamp" rates that reflect no variances for distance or volume factors. Market-based (non-regulatory) pricing may be more cost-causative, may emphasize different economic theories (marginal cost of production), and may be subject to other market conditions (e.g., pricing based upon elasticity of demand).

B. Stranded Costs

1. Historical Perspective and Background

As discussed earlier, investor-owned utilities typically generate, transmit, and distribute electricity on a vertically integrated basis, to customers located in defined, exclusive serving areas and subject to regulation by state commissions. Traditional utilities have an obligation to provide service to any customer desiring service in their service area. Regulation sets standards for quality, reliability, availability, and price of electric service. Statutory and case law protect the electric utility's opportunity to earn a reasonable return on capital invested to meet the requirements of regulated service.[76]

Restructuring and competition can change the underpinnings of this arrangement. Under competition, some (but not necessarily all) customers can effectively abandon their traditional source of generation in favor of new market alternatives. But, the costs incurred in building generating plants, as noted above, are long term in nature. If customers leave a utility's generating system without paying a share of those costs, the costs become "stranded" unless they can be recovered from remaining customers.[77] Such recovery becomes unlikely, as existing costs must be spread over declining volumes, thus tending toward increased rates. In a competitive market with competitive alternatives, consumers cannot be expected to pay such increased rates. As a practical matter, the utility's charges will be forced to the prevailing market rates, irrespective of the effects of such rate reductions on margins and rate of return.

"Stranded costs or investment" in generation refers to this decline in the economic value of generating facilities occasioned by the decline in the market price of electricity arising from restructuring and competition. By way of a simplified example: assume a regulated monopoly utility has $1 of investment in generating facilities and charges rates which include $0.10 per unit/per period as the reasonable return (10%) on that investment under regulation. With deregulation, new competitors using new technology requiring less investment ($0.50) can earn reasonable returns at rates reflecting

$0.05 per unit/per period (10% on this newer investment). If the utility reduces its rates to that level ($0.05), as it must to remain competitive, its return (10%) remains reasonable only as to an investment of $0.50. The other $0.50 of investment, unless some disposition is made somewhere, earns less than a reasonable return (here, 0%). Consequently, this portion of the investment has become stranded.[78]

"Negative stranded costs or investment" may also emerge. Instead of producing a decline in the economic value of generating facilities, competition may result in a net positive gain. Referring to the earlier simple example, it may be that the book value of the original $1 investment has declined to $0.25 (e.g., through depreciation), although the facility is fully functional. At the competitive market rate reflecting a return of $0.05 per unit/per period, the return on the residual book investment is 20%, implying an economic asset value of $0.50. The difference between the book and economic value (+$0.25) is sometimes termed a "negative stranded investment."[79] Some states both recognize the concept and require an offsetting of negative and positive values to determine the net amount of stranded cost recognizable for recovery.[80] For example, Montana Power Company recently sold most of its generating facilities for 155% of book value. In Maine, Bangor Hydro agreed to sell its hydro facilities for $89 million, when book value was about $50-$55 million.[81]

2. <u>Should Stranded Investments be Recoverable?</u>

As an initial matter, disagreement may exist whether stranded costs should be recognized at all. Theories [for] and [against] such recognition may be briefly summarized as follows:

- Social Compact Theory [For]—Under this theory, investor-owned utilities undertook various obligations imposed by regulation 1) beyond or different from those warranted by ordinary free market considerations; 2) in order to address the public interest; 3) with an expectation that they would have a reasonable opportunity to recover those investments over time; and 4) over that period, the opportunity to earn a reasonable return there-on, as well. This theory derives from U.S. Supreme Court cases (Federal Power Commission v. Hope Natural Gas Co., 320 U.S. 591(1944); Bluefield Water Works v. West Virginia Public Service Commission, 262 U.S. 679 (1923); Smyth v. Ames, 169 U.S. 466 (1898)), which recognize that a company "is entitled to ask [for] a fair return upon the value of that which it employs for the public convenience" (Smyth, supra). Idaho's Supreme Court has adopted this principle.[82] More recently, the Court reiterated similar concerns in terms of the reasonable expectations of investors in Duquesne Light Co. v. Barasch, 488 U.S. 299 (1989).

- Confiscation [For]—This theory asserts the right of private property and the obligation to pay compensation in the case of governmental takings (U.S. Const. Amend. V: ". . . nor shall private property be taken for public use, without just compensation."). Historically, such arguments were sometimes allied with the due process clause, as well (Id: ". . . nor be deprived of . . . property, without due process of law"; see Smyth v. Ames, supra).

- Basic risk of business [Against]—This theory asserts that all businesses are subject to the police powers of the state and to any necessary change in the exercise of those powers over time.[83] Where property remains in the owner's hands and can still be put to the production of income, no unlawful taking or confiscation occurs and no separate cost recognition or recovery is required. This is argued to be especially true of electric utilities, which have been on notice for some time that the regulatory environment is in a state of flux.

- Adverse competitive impacts [Against]—In the view of some, recognition of stranded costs will unfairly advantage the incumbent utilities who benefit from such cost recovery, as against new competitors who receive no such compensation. In this regard, the D.C. Circuit in Cajun Electric Power Cooperative, Inc. v. FERC, 28 F.3d 173 (D.C. Cir. 1994), suggested two competitive concerns. First, that stranded cost recovery could effect a tying between stranded cost charges and charges for bottleneck transmission facilities. Second, stranded cost charges could result in competitive asymmetry, whereby the incumbent utility could compete outside its territory without paying the stranded cost charge, but all competitors within its territory would pay the cost charge to it.

- Public Policy [Against]—This view asserts that recognition of stranded costs penalizes competitors and prudently run incumbent utilities for the efficiency of their operations, by rewarding inefficient utilities for past inefficiencies.

- Sharing principles [Intermediate]—This approach suggests that stranded cost recovery mechanisms should require that amounts recovered by a utility for stranded costs be shared with consumers under certain circumstances (for example, when expected levels of stranded cost are not realized or when offsetting benefits are realized).

- Forced costs [Intermediate]—Here, cost recovery would be permitted but limited to instances where affirmative regulatory mandates, initiated by the regulators, were the clear cause of the cost for which stranded recovery is sought. Some versions require such imposition to be over the active objection of the utility, as well.

3. Types and Characteristics of Stranded Costs

The pursuit of restructuring and competition in the states has led to an expanded scope of matters encompassed by stranded investment. Current inquiries and debates generally recognize three sources or types of stranded costs. They are:

1. Utility-owned generating facilities;
2. Long-term fuel and purchase power contracts, such as those arising from PURPA requirements;
3. Regulatory assets, including:
   Deferred taxes;
   Post-retirement employee benefits;
   Nuclear decommissioning costs; and
   Demand-side management (DSM) costs.[84]

Other types of costs may be also recognized for recovery purposes, depending upon the policies and goals of restructuring. For example, costs associated with environmental protection, natural resource preservation, and DSM address the public good. In a competitive market, however, unregulated sellers may choose not to incur these costs (such costs tend to produce no current income) and, thus, will obtain a price advantage over regulated utilities. As a result, the costs and the associated with these public benefits may, in a sense, become stranded.

FERC and related judicial proceedings have identified several criteria for characterizing costs as stranded. These characteristics may be summarized as: 1) prudently incurred; 2) legitimate; 3) verifiable; and 4) accurately calculated. From a different perspective, economic analysis may describe the essential characteristics of stranded costs in such terms as: 1) sunk in a prior period (before deregulation, actual or impending); 2) stranded by the transition to competition; and 3) not marginal in nature (since marginal costs are avoidable).

4. <u>Measurement of Stranded Costs</u>

The measurement of stranded costs requires examination of the cost structure of each affected entity and econometric analysis of the affects of any given stranded cost recognition policy on resulting transition costs, residual utility investment, future utility revenues, and consumer price and choices. Stranded costs can be measured in several different ways, including:

a. Revenues Lost—The volume of energy produced by a generation facility times the anticipated market price of that energy per unit (under regulation) is compared to the same output times the anticipated price under competition. The differential (if any) represents the amount of cost stranded by the transition to competition. Such computations can be based on projections (determined up front or ex ante) or upon price changes experienced over time (determined during the course of implementation or ex post).

b. Market Valuation—The diminution in value of a generation facility is measured by decline in estimated market (sale) value of that asset, by present valuation of future revenue streams under competitive market conditions, or by other market-related analyses.

c. Cost of Service Valuation—Declines in values are determined by a regulatory type of cost of service analysis, based upon book costs, historical operating expense, and so on, adjusted for future anticipated changes in revenues, based in part upon the competitive pricing of energy.

d. Bid Price—If full divestiture of the generation facility is required, the difference, if any, between the price obtained at arm's length for the asset and the book value of the asset becomes the measure of stranded cost.

5. Mitigation of Stranded Costs

Under some approaches, any amount of stranded costs determined by any the above methods must be diminished by any counterbalancing or offsetting factors or events (mitigated). In other words, stranded costs are to be netted against negative stranded costs. For example:

a. Future Efficiencies—To the extent deregulation and competition permit or encourage changes in future operations of utility generation which result in lower costs of energy, those reductions are to be offset against the amount of stranded cost determined under the above theories.

b. Buydowns of Existing Obligations—To the extent a generator renegotiates or otherwise reduces future obligations arising from power purchase contracts, the amount of such beneficial reduction is to be applied to diminish the amount of stranded cost determined above.

c. Mitigation Sales—To the extent energy from a generating plant can be sold for any price in the market (without exceeding marginal costs), the amount of revenue generated by such sales is applied as an offset to the amount of stranded cost determined above.

d. Negative Stranded Costs—To the extent the market value of particular generation assets may exceed book cost (assuming a conforming methodology for developing the amount of stranded costs), the excess in whole or in part is to be applied to reduce the amount of stranded cost so determined (in effect, shared with consumers).[85] The allocation of such "stranded benefits" to consumers and shareholders may, in turn, raise other issues.

e. True-up of Stranded Costs—Depending upon the methodology selected for measuring stranded costs, actual factors occurring in the market may be periodically reviewed for conformity to those anticipated. For example, forecasted competitive market prices of X cents/kWh might be compared to actually experienced prices, Y cents/kWh. Any resulting overage would be credited against future stranded cost recovery, be made subject to refund, or otherwise be applied to diminish the total recovery amount available. Shortfalls may or may not be permitted to increase amounts recovered from stranded cost mechanism.

f. Recovery Period—Stranded cost recovery plans may provide for a maximum period during which the utility will be afforded a reasonable opportunity to recover stranded costs, after which no specific or special mechanisms for such recovery will be continued. For example, in California, utilities recover their stranded costs over five years.

6. <u>Mechanisms for Recovering Stranded Costs</u>

Several alternatives exist for recovering any amounts determined to be stranded. Mechanisms for recovery would include:

a. Exit Fee—Under FERC Order No. 888, the wholesale customer who departs from the utility's generation in order to buy from a competing wholesale source must pay an appropriate share of any resulting stranded cost as an exit fee from the vertically integrated system. This fee may be pro rated based upon estimations of total losses, or may be subject to future rebate as other customers depart from the anticipated (regulatory) load.

b. Non-bypassable Surcharge—Stranded investment costs may be allocated and recovered from surcharges to other rates. For example, a surcharge could be levied on transmission or distribution rates. Further, surcharges may be targeted to specific groups or segments of the industry (e.g., as an access charge on each end user, on the transmission or distribution provider, on the seller or purchaser, and so on.) The levying of such charges must maintain competitive neutrality in the marketplace and consumer equity; hence the need to ensure the charge cannot be bypassed by some competitors or consumer segments.

c. Accelerated Depreciation—To the extent consistent with other factors (e.g., the degree of separation required), stranded costs may be recovered by permitting a period of accelerated depreciation to be applied against utility-owned generation facilities.

d. Price Cap or Other Incentive Regulation—To the extent consistent with other factors (e.g., the degree and timing of deregulation), alternative forms of regulation may be invoked to permit utility management to recover stranded costs through a more flexible regulatory regime, such as price cap regulation.

In summary, stranded investment generally refers to generation, long-term power contracts, or other investments and commitments undertaken during regulation with the expectation that over the course of time (under continued regulation) a reasonable opportunity to recover such investments would be afforded. A change to competitive market operations can alter such expectations, particularly where deregulation removes historical cost recovery mechanisms and new market mechanisms do not afford equivalent recovery opportunities. The legitimacy of such expectations, the degree of recognition, and the means for recognition in the future are all issues of substantial consequence for those determining, implementing, operating under, or obtaining energy from a restructured industry.

C. Network Structure and Operations

The degree to which the control of monopoly transmission/distribution facilities must be separated from competitive generation in an integrated utility (e.g., a utility that owns generation, transmission, and distribution in a single enterprise) depends upon several considerations. First, there is the potential for use of the transmission facilities in an anti-competitive fashion (e.g., where the utility preferentially dispatches its own power to the detriment of a competitor). Second, there is the degree to which separating generation and transmission is necessary to advance other policy goals, such as improving the identification, quantification, and recovery of stranded costs.[86] Third, even if transmission and distribution remain regulated activities after separation, it may be desirable to implement some alternative form of regulation intended to promote more efficient and effective provisioning of such regulated services.

1. Vertical Disintegration

Some believe the combined ownership of generating, transmission, and distribution facilities may pose the actual or apparent opportunity for anti-competitive behavior. Generation is increasingly viewed as a competitive activity; transmission and distribution are generally regarded as monopoly activities. Several alternatives of addressing anti-competitive concerns or market power arising from such combinations would include:

a. Corporate Divestiture—Divestiture forces the utility to completely separate itself (in greater or lesser degree) from both the control of and the ownership of the generation facility. This can be accomplished, for example, by the required sale of the generating assets and retention of the transmission assets (or both or the reverse); by assigning the generating assets to a subsidiary company and selling or spinning off that company; by placing the assets in a separate operating trust; or by other means. The cost of such a requirement can be high directly (legal and financing fees, especially if the assets are indentured, as most are) and indirectly (loss of personnel, loss of internal cost sharing).

b. Fully Separated Affiliate (FSA)—The assets and operations are assigned to a separate legal entity. That entity is under the common ownership of the utility business, but control is attenuated by requiring separate directors and officers, separate accounting records, separate employee groups, separate information systems, and so on. Of importance, internal information flows between parent and subsidiary are adjusted to ensure that the subsidiary receives no preference in quality, quantity or timing of competitively valuable information relative to other competitors in the marketplace. This approach entails some expense and inefficiency on the part of the utility, but less than above. It may also afford less protection against anti-competitive behavior, depending upon other factors (such as the degree of ongoing regulatory antitrust oversight of the monopoly activity, the number and strength of the competitors in the market, and so on).

c. Accounting Safeguards—The assets and operations remain within the corporate entity, but are subjected to defined requirements for separate accounting records, separate operating personnel, separate office space, and so on. Currently, the Federal Communications Commission (FCC) utilizes this approach in defined circumstances in the telecommunications industry. The financial costs are less; but so, arguably, are the anti-competitive protections.

d. Integrated Systems Operator (ISO)—Either as part of the competitive separation issue, here, or in connection with "Transmission Restructuring," below, the actual real-time and day-to-day operations of the monopoly transmission network may be entrusted to a neutral third party termed the "integrated systems operator," also known as the regional transmission operator.[87] The authority of the ISO and the degree of utility participation/representation in the ISO are policy issues in part influenced by the degree to which separation (to avoid anti-competitive influences) is found appropriate.

Variations of the above (as well as other methodologies) can be developed, but the separation of generation from transmission implicates both competitive and efficiency issues of consequence to any public policy determination.

2. Generation

Generation is an extremely important issue to the State. Historically, significant state control attended construction and operation of generating facilities, and the pricing of energy derived therefrom. In several instances, however, practical authority is shared with FERC, particularly with respect to the licensing and re-licensing of certain hydroelectric facilities (see 16 U.S.C. § 797(e)). State control may be eroded further to the extent market forces, facilitated by policies of FERC and states other than Idaho, transform electric energy into a commodity available for sale nationwide in interstate commerce, at market-driven prices.

3. Transmission

Several states have favored or adopted competition in generation. Unlike generation, however, transmission is not yet practicably liable to facilities-based competition. Cost and environmental concerns make the building of large-scale, duplicative, competing transmission lines economically and legally impracticable. Transmission, therefore, is generally considered an essential facility or a "bottleneck facility" which, under applicable legal precedent, must be made available to competitors on a reasonable basis.[88] Since generation must get to the customers via transmission facilities, the current industry structure unavoidably amalgamates competitive with non-competitive activities. "Unbundling" utility prices, i.e., separating generation, transmission, and distribution costs, is often viewed as a necessary precursor to deregulation.

At the interstate wholesale level, FERC has determined that to the extent the transmission owner is a historically integrated electric utility and retains ownership of its transmission facilities, the principle of competitive neutrality requires several things.[89] First, the owning utility must make that facility available to competitive generators, a requirement termed "open access." Second, for such access the utility must charge competitors no more than it would charge itself for transporting similar amounts of electricity. In FERC's phraseology, such charges are to be "comparable," as are the other terms and conditions under which transmission is provided to transmission customers. While the utility may not actually charge itself in the cash-and-carry sense (depending upon the form of competitive regime imposed), it must impute as part of it costs of doing business the amount comparable to that actually being charged to competitors.[90] Third, included in the terms of comparability is a requirement to provide competitors with the same real-time information used by the utility in scheduling its own generation and in maintaining the operating parameters of the dynamic network described earlier.[91]

Relevant transmission issues would include:

a. Open Access Requirements—Competitors need the legal right, the physical ability, and the necessary real-time information in order to interconnect and to dispatch competitively generated power. Competitive restructuring plans generally consider and provide for mechanisms that assure these capabilities. The ISO or TransCo (if one is mandated) may be tasked to create and administer standards that effect these goals.

b. Monopoly Regulation—Since transmission facilities continue to be bottleneck in character (as discussed above, replication by would-be competitors is too impracticable), they require continued regulatory oversight as a monopoly. This requirement for continued regulation may: 1) affect the degree of "Separation" desired or required of a vertically integrated utility; and 2) provides the means for defining and enforcing "Open Access," discussed next.

c. Open Access Tariffs and Operating Information—To make effective use of physical access to the grid, a competitive generator requires: 1) terms and conditions of access; and 2) real-time information concerning the available capacity on that grid. These requirements permit competitors and consumers to make economic decisions concerning power sales and purchases and to secure the timely dispatch of power to carry out the sale. Under FERC formulation, transmission providers must file tariffs describing the particulars of the transmission service they will offer (these can be extensive, complex documents), which must reflect the same terms and conditions as those attending the utility's own use of the network ("comparability"). Under other formulations, the ISO performs the task of maintaining and publicizing the terms of access. Separately, FERC mandated an "Open Access Same-Time Information System" system ("OASIS") to provide open access transmission customers (including competitive generators but also brokers, marketers, etc.) with the same information concerning network availability as utilized by the utility itself.

d. Costing and Pricing—Setting the rates for transmission can involve many of the issues of cost verification, prudence, and rate design typically associated with the current regulation of vertically integrated utilities. In theory, the absolute level of such costs should not affect competitive neutrality (since all generators pay the same under open access). In at least one area (the separation or disaggregation of an integrated utility), the misallocation of such costs may adversely impact competition by fostering unfair economic advantage. Further, transmission rates may become the vehicle for stranded cost and other transitional cost recovery. Such transitional costs need to be bifurcated (i.e., analyzed separately) from the costs associated with transmission in order to avoid confusion and unintended policy effects.[92]

4. Local Distribution

Unlike wholesale, retail wheeling is a function of state jurisdiction and policy, but many of the considerations attending transmission at the federal level also apply to local distribution. Local distribution facilities also tend to be bottleneck in nature and owned or controlled by the vertically integrated utility which also owns the generation and transmission facilities.[93] Therefore, issues concerning transmission access may also arise with respect to local distribution access where retail-wheeling policies are contemplated.

Historically, distribution is subject to state jurisdiction, although some may argue that FERC Order No. 888 should be interpreted as impinging this jurisdiction. As noted earlier, Order No. 888 sets forth seven criteria for characterizing facilities as local distribution:

1. System is in close proximity to retail customers;
2. System exhibits radial architecture;
3. Power flows enter and rarely leave system;
4. Power in system is rarely reconsigned or transported elsewhere;
5. Power is consumed in restricted geographic area;
6. Meters are positioned at the transmission/distribution interface; and
7. System power operates at reduced voltage levels.

However, the EPAct and Order No. 888 address only interstate, wholesale wheeling. The statute to the states (see 16 U.S.C. § 824k(h)(1)) reserves local or retail distribution matters.

Retail wheeling raises many issues. Utility costs and rate processes may not be geared to reflect unbundling and pricing of discreet services. Multi-party access to the local distribution system requires extensive operational, financial, and rate making adjustments. The local distribution system itself (like the transmission system) is a bottleneck facility, and thus issues concerning equal access, ownership, and operation also arise at this level. The issues developed above concerning vertical integration, ISO functionality, and incentive regulation generally apply to local distribution matters as well.

D. Market Structure

In the past, the consumer purchased electricity as a delivered service, priced on a cents/kWh basis. Competition in generation will permit a wholesale consumer (at the interstate level) to purchase electrical energy and ancillary services separate from the regulated transmission service. Retail wheeling would permit the end user customer (at the local level) to buy electricity on an unbundled basis, separate from distribution and other customer services (e.g., meter reading).[94] These capabilities impact both buyers and sellers, and the product they buy and sell.

1. Seller Considerations

Disaggregation and open access permits new market participants to emerge, since exclusive, monopoly service areas and vertical integration are no longer bars to market entry. These new entrants typically come in three varieties:

> "Aggregator"—An individual or entity that combines the loads of multiple end-use customers in facilitating the sale and purchase of electrical energy, transmission, and other services on behalf of those customers;
>
> "Broker"—An individual or entity that arranges the sale and purchase of electric energy, transmission, and other services between buyers and sellers, but does not take title to any of the power sold; and
>
> "Marketer"—An individual or entity that buys electric energy, transmission, and other services from traditional utilities and other suppliers, and then resells those services at wholesale or, where retail competition is permitted, to an end-use customer.[95]

Current regulation often does not apply to these entities, which may not meet the applicable statutory definition of "utility." Accordingly, new legislation may be required to provide protection for consumers and basic rules for new market entrants in competitive markets.[96]

2. Buyer Considerations

Competitive changes can impact the consumer, as well as the seller, in ways beyond direct increases or decreases in rates. Customer service processes are an example. Existing mechanism for recording and billing usage are based upon an integrated service offering from one seller. Such mechanisms and processes may be inadequate for a market where different sellers provide different services. Market changes may also create pricing issues for traditional utilities, whose accounting systems and rate design respond to regulatory requirements rather than competitive market requirements. Current electric and telecommunications industry experience suggests that changing these structures to competition can be a complex matter.

Restructuring can alter what it is the consumer buys. Electric energy historically was delivered as an integrated service, paid for by the consumer as one charge on one bill. The costs of each component of the service (generation, transmission, distribution, ancillary services, and customer services) were bundled together by regulators and charged in a single cents/kWh rate. Competitive sales of electricity in a competitive market tend to disaggregate or unbundle these services into discreet service offerings, no longer proffered by a single source on a single bill. As with telecommunications, consumers may face choices and buying decisions for which their prior experience affords inadequate experience.

E. Market Power

The phrase "market power" has recently come to the fore in policy debates arising from electric restructuring. The phrase refers to the influence that any particular owner of generation capacity may be able to exert in a newly deregulated, competitive generation market. As described by the Competitive Policy Institute:

> But electric restructuring has an Achilles' heel. Its promised benefits—increased efficiency, lower prices and wider consumer choice—depend critically on the assumption that newly deregulated generation and retail services markets will actually be competitive so that market forces will discipline sellers.
>
> What can go wrong? Simply put, owners of deregulated generating plants and retail marketers of electricity could have market power. Generators in a region may be able to keep deregulated prices of electricity above competitive levels and earn supra-normal profits while depriving consumers of some of the benefits of restructuring. If deregulated retail marketers of electricity are shielded from the pressures of competition from other providers, the result will be predictable: consumers will pay too much for electricity.[97]

In other words, to the extent policy-makers choose competition as the vehicle of public policy, it may prove necessary to look more closely at the assumptions and conditions underlying competition. Deregulation is a part, but may not be the whole, of ensuring the conditions of effective competition. Other steps to reduce or control concentration in generation may also prove necessary.[98]

F. Consumer Issues

1. Background

Historically, the typical local electric utility offered electric energy as part of a "bundled" service offering which included: 1) the electric energy itself; 2) delivery of that energy to the customer's premises; 3) meter reading; 4) billing; 5) customer services; and other matters. Under local distribution competition, (retail wheeling or direct access,) electric energy is sold to end users separately from other services ("unbundled"). In theory, individual consumers obtain the ability to select their energy provider ("choice"), as they select their long distance company (and in some areas, can now select their local exchange service provider).

Burdens, however, may come with such benefits. Retail wheeling raises consumer information, universal service, and consumer protection issues. Consumers are used to one-stop shopping for electricity (unlike electrical appliances). As services become unbundled, confusion over the choices offered may be anticipated. Rates for some market segments may increase as unbundling occurs, since under competition rates are driven towards cost (cost causation, supply and demand). High cost low /volume customers may prove unattractive and therefore may be unserved or served at higher prices in a competitive market. Large volume customers (industrial and commercial) may receive more (or all) of the benefits of competition.

Basic service assumptions may change, as well. Consumers are generally used to dealing with the local electric company in a regulated context which emphasis customer service and responsibility. The appearance of unregulated, non-utility sellers of energy can obscure accountability for service provisioning, create consumer confusion, and result in abuse of consumer interests through improper business practices. While the majority of new entrants may well prove reliable (especially since customer loyalty and product identification are important elements of competitive service provisioning), new laws may be necessary to establish minimum codes of conduct and to extend minimum levels of supervision to market participants not subject to regulatory oversight as "utilities."

Achieving materially improved benefits to the consumer is a primary goal of and justification for public policy activity in the matter of electric restructuring. Although it is intregal to the American economic system, competition is not without its drawbacks from a consumer perspective. In seeking to improve consumer welfare, policy-makers must be concerned with unintended consequences adverse to the very people they seek to benefit. Several major consumer issues are discussed below.

2. Universal Service

The transition to competition may raise issues concerning the affordability and availability of minimum acceptable levels of service to all members of the public. In competitive markets, prices tend to be driven toward costs, in both an upward and downward direction. Prices for the same quantity of electricity can be different for different products, different market segments, and different customer classes. Customers in remote or high-cost areas; customers who offer relatively little revenue potential; and customers with undesirable economic characteristics (e.g., poor credit, poor housing) may not attract a seller in a competitive market. Additionally, deregulation may remove the basis for mandating service to such customers.

Ensuring the availability of affordable, quality service to all consumers requires consideration of several matters:

a. Provider of last resort—The existence of a competitive marketplace assumes that there are a number of willing sellers of electricity. If all consumers are to have access to electricity, someone must have the responsibility for providing, as a last recourse or an a default basis, system connection (connecting the customer premises and the distribution system) and energy provisioning (procuring and delivering to the end user electric energy in base amounts and at base quality levels sufficient to meet acceptable public interest standards).[99]

b. Basic service package—Public policy may establish a defined list of services/energy quantities/pricing schemes to meet needs otherwise not addressed by the marketplace, including "lifeline" service levels and rate support. For example, investor-owned public utilities in Idaho are prohibited from disconnecting electric or gas service in the winter months of December, January, and February for public health and safety reasons, but may disconnect for arrearages after the moratorium is past. IDAPA 31.21.01.306.

c. Rate support—A competitive market forces rates toward costs. Past regulation may have moved some rates above costs in order to sustain other rates at below cost levels (implicit subsidies). For example, some argue that it is more costly to serve the more sparsely populated portions of rural Idaho than the more urban areas. Under the concept of rate averaging, all similarly situated customers in a particular class pay the same rate averaged across all customers (e.g., residential) to meet the average costs of serving the entire class without regard to urban or rural location. Unbridled competition will tend to force abandonment of such practices, forcing costs associated with universal service to be recovered externally (if at all) through taxation or welfare mechanisms, or internally through surcharges on other services. See Idaho Code §§ 62-610 and 62-610A through -610F regarding telecommunications rate support.

3. Consumer Education and Protection

Protection of the public interest and effective functioning of the competitive marketplace are each promoted by consumer awareness. Prior experience with an integrated, regulated market may not fully prepare consumers for the new choices and new responsibilities inherent in competition. States that have transitioned to competition, specifically provide funding for educating consumers about the transformation of the industry.[100] As they seek revenue opportunities, new entities may appear in the market that do not have a record of service, experience, or commitment with respect to customers in the serving area. The public interest may require specific state efforts to anticipate these developments through such measures as:

- Determination of educational information in market transition (unbundling costs, introduction of choice, outcome if not switch suppliers);

- Identification of matters warranting consumer protective actions (e.g., customer slamming, misrepresentation, truth in advertising (labeling) standards, registration of market participants within the State, and so on);

- Delineation of an appropriate scope for protection and educational programs;

- Planning for the identification and recovery of costs associated with such programs (which could implicate other policy issues, such as competitive neutrality); and

- Determination of the appropriate monitoring and enforcement mechanisms (e.g., market v. antitrust issues, oversight agencies (OAG v. PUC).)

G. Financial Market Issues

Changes in industry structure and regulatory regimes may impact the ability of market participants to raise capital or the cost of that capital. Many relevant factors impact the perception or reality of risk (operating or financial), which in turn can result in increased cost of capital and concomitant increases in cost of service to the consumer. General financial market considerations would include:

1. Uncompensated Takings—Non-recovery of stranded costs, which result in write-downs on utility balance sheets and consequent non-recovery for investors.

2. Impairment of Contract—Disavowal of long term power contracts, which leaves alternative suppliers of generation (co-generators, IPPs) without revenue streams to pay back investors.

3. Transitional Certainty and Foreseeability—The degree to which restructuring allows a period of adjustment and reorientation to new conditions for market participants (existing and future), thereby influencing the likelihood that prior investments will or will not be recovered in some manner.

4. Securitization—The degree to which restructuring permits the quantification of future cost recovery in the present period and prescribes mechanisms which assure the recovery of that quantified amount over time. If so quantified, the right to receive those amounts can be vested as property and sold as a security ("securitization"). Key elements of securitization involve:

   - Creating a property right in revenue streams deriving from transition charges;

   - Making both the recovery amount and the recovery mechanism irrevocable with respect to future legislative action;

   - Separating the credit rating of the securitized property from that of the relevant utility; and

   - Insulating the securitized obligation from the full faith and credit of the state.

To the degree that, in any particular jurisdiction, generating or transmission facilities are predominantly owned by investor-owned utilities, policy decisions impacting market perception of the utilities as commercial activities can directly effect the present and long term costs and reliability of service provisioning.

H. Municipal Indebtedness

The City of Idaho Falls has financed two hydroelectric generating projects through the issuance of municipal bonds. In order to meet the debt service obligations for these two projects, the city has pledged revenues from the sale of electricity to retail customers and others. The original obligation created the bonds exceeding $90 million dollars and debt service payment continue until the year 2015. The city has no ability to write-off or defer any of these debts.

An assumption in issuance of the bonds was revenue from sales of electricity to captive retail customers as well as sales of electricity to other users. In a deregulated environment where retail customers are allowed the ability to purchase electricity on the open market, the city would quickly find itself in an untenable situation. This situation might be referred to as a "death spiral" where retail users of electricity purchase their electricity not from the city, but from other providers. The city would then be forced to raise electrical rates on the remaining customers in order to meet its debt service. This would cause the loss of more customers and require either a further raise in electrical rates or attempting to find revenue from other sources. The only alternative available to the city would be to raise revenue from property taxes or to reduce other city services.

In considering deregulation, the situation faced by the City of Idaho Falls must be considered. Alternatives for financing the debt service should be provided. Such alternatives might include allowing the city to assign debt obligations from the generating facilities to transmission facilities, or making provisions for the recovery of "stranded" or "transition" costs for resources with which above-market rates are associated. Finally, allowing the city to refinance its obligations over the entire life of the resource, which exceeds 30 years, might also be considered. This final measure would require amendment of the Idaho Constitution.

I. Public Purpose Program

In addition to stranded costs, other costs determined to arise in connection with the change of industry structure may be identified and recovered through the vehicle of a transition charge. Such costs could arise in connection with specific public interest programs including: clean water or air; fisheries restoration; renewable resources; energy efficiency and conservations; low-income assistance; and research.[101]

Specific provision for the recovery of such costs may prove necessary in a competitive market because competition tends to force cost reduction wherever practicable. Public purpose programs, such as universal service, environmental protection, fisheries restoration, long-term research and development, and many other such programs, while socially beneficial, do not generate present cash flows and earnings. As a former California Commissioner expressed it:

> As it begins to address these issues, I respectfully suggest to the [California] Legislature that the era of the investor-owned utility as cooperating agent in, what one commentator has termed, the "stealth pursuit of social and environmental goals" is over. In a world of competitive choice, rather than captive ratepayers, utilities can be expected to show stout resistance to the inclusion within their competitive offerings of any costs that are not borne by their non-utility rivals.[102]

Accordingly, policy makers should take into account the viability of existing support mechanisms for such programs. Where restructuring erodes the basis for particular cost recovery approaches, new approaches must be fashioned or the supported programs altered, reduced, or terminated.

The discussion in this section hopefully reveals the complexity and the inter-relationship among various restructuring issues in general. It should not be overlooked that at least two other major issues – water rights and whether Idaho customer rates will be adversely affected – have not been evaluated.

VII.

RESTRUCTURING IN MONTANA AND CALIFORNIA

Virtually all states have considered or are examining electric industry restructuring. As of October 1, 1998 a minority of states (about 14) appear to have adopted some form of deregulation. Other states are considering such measures. At the other end of the spectrum, several states appear to have made determinations not to materially alter existing industry structures or to formally defer further action, pending the results of activities in other jurisdictions.[103] Two states – California and Montana – bear particular scrutiny. California because of its affect on the regional market and the deregulation structures it created, and Montana because of its proximity and hydropower similarity.

A. The Montana Experience

1. Legislation

In 1997, the Montana Legislature enacted Senate Bill 390, restructuring the Montana electric industry. Under the Montana statutory scheme, retail competition would be made available to customers on a "rolling" basis with the largest customers being able to choose their electric supplier first, and eventually all customers having the same opportunity. All customers of investor-owned utilities are to be able to choose their electric supplier no later than July 1, 2002, subject to a two-year extension at the discretion of the Montana Public Service Commission (PSC).[104] In transitioning the industry from a regulatory to a competitive market, all investor-owned utilities are to file "transition plans" with the Montana PSC at least one year prior to the implementation of retail competition. The Montana PSC must review the transition plans and may adjust the implementation dates. See Appendix. Beginning July 1, 1998, all investor-owned utilities were to establish pilot choice programs to determine the best way to introduce retail competition.

Investor-owned utilities must "functionally separate" their generation, transmission, and distribution operations. The functional separation may be accomplished in a number of different ways including accounting safeguards, structural reorganization, or actual divestiture of assets. The Montana PSC was prohibited from ordering divestiture of generating assets and cannot prohibit a utility from voluntarily divesting its assets. Rural electric cooperatives were given the choice of opting in or opting out of retail competition. If they opt out, cooperatives may not offer services to customers of other suppliers. In addition, utilities with fewer than 50 customers were also excused from certain retail competition activities.

Other significant components of the bill included:

a. Stranded costs—investor-owned utilities are allowed to recover their "transition costs." These costs include the net unmitigatable above-market costs of generation, deferred charges, PURPA contracts, transitioning costs, and the costs of issuing transition bonds. Transition costs are to be recovered through a non-bypassable charge levied upon all customers (except those customers with new loads greater than 1,000 kW first served after December 31, 1996).

b. Rate freeze—beginning July 1, 1998, there is a two-year rate moratorium for all investor-owned utility customers. For customers who do not have choice as of July 1, 1998, rates cannot be increased except for transmission and distribution rates subject to Commission approval. Exemptions to the rate freeze include increases for universal system benefits, state and federal taxes, or an extraordinary event.

c. Universal systems benefit program—the benefits program charge will be paid by all utility customers to fund energy conservation, renewables, and low-cost income energy assistant programs.

d. PSC jurisdiction—the PSC shall continue to regulate retail transmission and distribution systems. The PSC must continue its regulatory oversight to ensure that competition is sufficient to prohibit anti-competitive pricing and practices. The PSC shall also license all electric suppliers, issue reliability and safety standards, implement consumer protection measures, and approve the issuance of transition bonds by utilities.[105] See Appendix.

2. PacifiCorp's Sale of Its Distribution System

Following passage of Montana's restructuring legislation, PacifiCorp put its Montana distribution facilities (serving about 36,000 Montana customers) up for sale. After reviewing bids, PacifiCorp elected to sell its distribution system to Flathead Electric Cooperative and PacifiCorp proposed to retain all the "above book" profits from the sale. The Montana PSC and the Montana Consumer Counsel obtained a preliminary injunction prohibiting PacifiCorp from completing the transaction until the Montana PSC reviewed the terms and conditions of the sale.

The Montana PSC eventually approved the sale by adopting the Consumer Counsel's recommendation that approximately half of the above book proceeds ($4 million) be returned to customers in the form of refunds and system improvements. More specifically, $1.25 million of the sales proceeds were to be used for system improvements in PacifiCorp's existing urban service areas and remaining the $2.75 million would be returned to residential and small commercial customers in the form of refunds. Although the Montana PSC could not find the exact amount of the net gain on the sale, it nonetheless noted that customers will benefit from a significant portion of the net gain.[106]

3. Montana Power's Sale of Its Generating Facilities

In December 1997, Montana Power Company (MPC) announced its intention to divest its generating assets and offering these assets for sale. In November 1998, MPC entered into an agreement with PP&L Global for the sale of most of its generating facilities and certain transmission facilities. PP&L owns generating plants and distribution systems in several states and foreign countries.[107] Global declined to purchase MPC's Milltown dam currently impounding polluted sediments. The sale price of approximately $988 million is estimated to be approximately 1.55 above MPC's book value. The exact closing price of the transaction depends upon the sale of MPC's share of its Colstrip generating facility. Parties to the sale indicated that the above-book proceeds may be used to cover an estimated $160 million in transition expenses and to reduce an approximate $156 million in regulatory assets. Any remaining above-booked proceeds could be utilized to offset long-term contract costs. Under the terms of the agreement, MPC has a power buy-back provision for three years. In other words, Montana Power will purchase power from PP&L for customers that have not selected an alternative energy supplier. The sale must be approved by Montana PSC and other regulatory bodies including FERC.

4. Ballot Initiative No. 75

In November 1998's general election, Montana voters approved Constitutional Initiative No. 75, which provides that no new tax or tax increase can be enacted without approval by a majority of voters in the geographic area subject to the charge. The Initiative also gives citizens the right to sue government agencies and officials if aggrieved persons feel they have been subject to an unfairly leveled tax. While the constitutionality of the Initiative is currently under review by the Montana Supreme Court, it has raised the question of whether the universal systems benefits program (mentioned above), which were to be assessed beginning January 1, 1999, violate the Initiative.[108] Under Montana's restructuring law, customers were to be assessed fees for the universal benefits program at an annual level of 2.4% of 1995 retail sales revenues. Various parties have questioned whether the Initiative is applicable to the universal benefits fees.

B. The California Experience

1. Legislation

In 1996, the California Legislature enacted Assembly Bill 1890 (A.B. 1890), restructuring the California electric industry. In 1997, the legislature enacted Senate Bill 477, extending and enhancing the consumer protection provisions of A.B. 1890 that were to expire on January 1, 2002. See Appendix. The goal of these two bills was to introduce retail competition in California so that all customers will have retail choice by 2002. The California Legislature believes that competition would lead to lower prices, promote energy efficiency, and spur economic growth. Generation, transmission and distribution are to be divested from the vertically integrated investor-owned utilities.

A.B. 1890 also created two new entities: 1) the Independent System Operator (ISO), and 2) the Power Exchange (PX). The ISO controls transmission capability and maintains a balance between energy demanded and energy supplied. California's three large IOUs

(Pacific Gas & Electric, Southern California Edison, and San Diego Gas & Electric) may retain ownership of their transmission facilities but must turn over operation of the facilities over to the ISO. The ISO is regulated by FERC. The PX is an auction mechanism where all power generators sell their power through the exchange to distribution suppliers. The PX is a competitive trading location for competitors to sell and distribution companies to buy power at "market-based" rates. During the four-year transition period, all distribution companies are required to obtain their power from the PX. The ISO and PX begin operating on March 31, 1998.

Other features of the Bills included:

a. Stranded costs—investor-owned utilities are allowed to fully recover their above-market investments made before December 1995 during the four-year transition period to conclude March 31, 2002. Stranded (above-market) costs of PURPA and other purchased power contract entered into before December 1995 are to be recovered over the life of the obligation. Other transition costs recovered as part of the customer transition charge (CTC) include employee transition costs and implementation costs of restructuring. Total stranded costs are estimated to be approximately $27 billion including $13 billion for PURPA and contract generators and $9.3 billion for prior nuclear investments.

b. Rate reduction—beginning January 1, 1998, residential and small business customers received a mandatory 10% rate reduction.

c. Trust Transfer Account—to achieve the 10% rate reduction, A.B. 1890 allows the three IOUs to issue bonds sold by a state banking entity (California Infrastructure & Development Bank). The Bank issued approximately $6 billion in bonds to be recovered from customers through the year 2008. Although the rate freeze will be eliminated by year 2002 while the TTA charge continues until 2008, it is assumed that the TTA will be offset by lower rates for electricity. In addition, the TTA will also be decreased as the principal is paid back.

d. Public purpose programs—all customers will continue to pay public purpose fees to support renewables, energy efficiency, low-income program, and research and development. For 1998, the total revenues collected for these programs will be approximately $505 million.

e. PUC jurisdiction—the PUC continues to regulate transmission and distribution rates through the transition period. In addition, the PUC is responsible for licensing energy service providers (ESPs), enforcing anti-slamming provisions, and setting billing and pricing practices such as labeling standards for "green" power.

f. Consumer education program—consumers will be furnished with information so that they may compare and select among the various electric products and services. Utilities and the PUC are required to implement a customer education program informing customers of the changes to the electric industry. This program is estimated to cost approximately $90 million.

For example, the average monthly residential customer's bill for 1997 and 1998 would compare as follows:

1997 Bill			1998 Bill Unbundled billing detail	
Baseline	32 kWh @11.6¢	$38.52	PX Cost (energy) @ 2.4¢	$14.14
Energy	268 kWh @ 13.3¢	$35.64	(est)	2.40
Above-Baseline		$74.16	ISO (transmission) @ 0.4	21.66
			Distribution Chgs @ 3.61	2.40
			Public purpose prg @ 0.4	3.00
Total 1997 Bill reduction		(7.42)	Nuclear Decomm @ 0.5	9.66
Minus 10%		$66.74	TTA Bonds @ 1.61	13.22
			CTC @ 3.4	$66.74
			Total 1998 Bill	

2. Current Status

The California market has been in transition for seven months. During that time, the average price for power through the California PX was approximately $20 mWh. The hottest August in California history and some outages caused that price to swing widely to as much as $100 mWh. On August 31, high temperatures prompted the ISO to declare a stage II emergency where the state's three largest distribution suppliers reduced their energy to interruptible customers.

Despite large expenditures for customer education, only 1% of the nearly 10 million electric customers in California switched electric suppliers. See Appendix. This figure can be broken down to less than 1% of residential customers selecting alternative suppliers to 14% of large industrial customers switching suppliers. The total percentage of electric load switched to direct access was less than 9% for the entire state.

3. Ballot Proposition 9

Finally, consumer advocates in California managed to place an initiative on the November ballot that would have repealed the state's Electric Reform measures. California's Proposition No. 9 was defeated when 70% of the electorate decided not to repeal the instituted reforms. It was reported that the three large utilities contributed approximately $50 million in opposition to Proposition 9.[109]

VIII.

CURRENT CONSIDERATIONS

Currently, there exists no federal mandate that compels states to implement retail electric competition. Based upon the legislative activity in Congress over the last two years, it is likely that federal legislation will be sponsored by members of Congress, as well as the Administration, in the 106th Congress.[110] Several groups are now recommending that Congress not implement federal restructuring. Other recent developments merit discussion.

A. Low-cost States' Initiative

In a December 10, 1998 letter to Congress, 23 regulatory commissions representing low-cost energy states argued that the decision to introduce retail competition should be left solely to state legislators, utility regulators, and their constituents. Congress should not dictate if, when, and how states must restructure the retail electric industry. The average retail electric rate in the low-cost states is 5.52¢ per kWh, more than 24% lower than the national average of 6.87¢ per kWh in 1996. Two-thirds of the country pays electric rates below the national average and 20 states pay below 6¢ per kWh for electricity. Only ten states pay over 9¢ per kWh for retail electric service. The average retail price of electricity in the 15 states that have restructured to date is 8.62¢ per kWh, or more than 25% higher than the national average. Exhibit Nos. 11, 7.

Although some studies have suggested that electricity prices will fall for all users in a competitive environment, the letter states that traditional logic may suggest otherwise. Higher cost states may find it attractive to purchase electricity of low-cost states, effectively raising prices for any native low-cost electricity. The letter goes on to say:

> In fact, a research paper that supports restructuring says that "regions of lowest price...may experience slightly higher prices."[111] The Energy Administration agreed in a 1997 paper on prices in a restructured market that it predicted competitive prices in the Northwest and parts of the Midwest would be higher than higher (or regulated) prices.[112] Finally, a paper from the Oakridge National Laboratory suggests that retail competition will cause electricity prices in the Northwest to rise as producers of electricity sell their inexpensive power into nearby high-cost electricity markets.[113]

Exhibit No. 11 at 6. The low-cost states also expressed concern that retail competition may disadvantage rural customers over urban customers in markets with greater densities of customers. In addition, these states voiced concerns about the areas of economic development and stranded costs. Simply put, the states are best qualified to determine the appropriate level of stranded costs and how "negative" stranded costs should be distributed.

B. NAAG

The concerns expressed by the low-cost states are similar to measures advocated by Attorney General Lance in January 1998 and adopted by the National Association of Attorneys General (NAAG) in March 1998. Exhibit No. 12. More specifically, the Attorney General advocated the following principles:

a. States' rights. Any decision to permit electric retail competition is best left to the states, not the federal government. Federal legislation mandating a specific form of restructuring or a time-schedule for deregulation will not benefit Idaho ratepayers. Idaho is in the best position to take into account our local needs, circumstances, and interests in this complex subject. We must resist any federal "one-size-fits all" approach.

b. Water rights. The sovereignty of Idaho's water rights must be maintained. Water rights, issued by the states, fuel the hydropower facilities supplying electricity to our homes and industries. The current system of state regulation guarantees that the citizens of Idaho receive the benefits of these facilities. Deregulation should not require that these benefits exit the state leaving Idahoans with only the burdens associated with hydroelectric facilities. Idaho's water should not leave our state over transmission lines.

c. Competition. Deregulation must benefit all electric users, including residential and small business customers. In Idaho, industrial, residential, small business and irrigation customers enjoy some of the lowest power costs in the nation. While some suggest that deregulation will bring lower prices, several recent studies predict higher prices in the Northwest if restructuring occurs.

d. Consumer protection. If deregulation is to occur, it must include measures to protect customers from deceptive and fraudulent practices such as "slamming," unlawfully switching a customer from one supplier to another without the customer's consent.

Customers must be able to understand and compare electric service alternatives.

e. Stranded costs. Each state must consider the appropriate recovery of stranded costs or assets consistent with equitable principles and past regulatory decisions specific to each state. Stranded costs represent a significant issue in the transition from a regulated to a competitive market.

NAAG's resolution adopting these and other principles is contained in Exhibit No. 13.

C. Interim Committee's Recommendations

The Idaho Legislative Council's Committee on Electric Utilities Restructuring[114] studied the issue of deregulation from the Idaho perspective. In December 1998, the Committee issued its Final Report. See Exhibit 14. The Committee's Final Report, recognizing the complexity and importance of the issue to Idaho, made the following seven recommendations:

1. Our Congressional delegation vigorously oppose further deregulation at the federal level;
2. No state legislative actions be taken at this time that would encourage retail electric power restructuring;
3. State statutes dealing with the production and delivery of electric power be reviewed and clarified, where appropriate;
4. Water resource questions be given more study and scrutiny to determine any risks to water rights, to changes in river operations, and to the management of the state's water resources;
5. Legislation be considered to allow inspection of books and records by the Public Utilities Commission of subsidiaries and affiliates of energy-producing utilities so that activities of these otherwise non-regulated entities do not deleteriously affect ratepayers;
6. There be follow-up on the issues of the BPA Residential Exchange Credits; and
7. The Committee be authorized to continue for the next Legislative Term.

Exhibit No. 14 at 5-6.

None of the Committee's recommendations are contradicted by this Report. The complexity of the issues presented demands a well-focused legislative policy for Idaho. There are, however, a number of issues that must be addressed regardless of the status quo recommendations of the Committee.

IX.

CONCLUDING COMMENTS

It is clear that the complexity of the deregulation debate and its importance for Idaho cannot be overstated. The hallmark of Idaho's power system has always been universal, reliable service at reasonable rates. This has been thanks, in no small part, to Idaho's hydroelectric generating resources and its responsible, well-run utility, cooperative, and municipal systems. The regulated power system in Idaho and the United States has served us well. The pivotal question then is: What benefits, if any, can Idaho expect from deregulation of the industry? Direct access to the retail power markets may well be to the advantage of some customers, notably the large business and industrial customers. However, such access may be less advantageous to the smaller business, irrigation, and residential customers than provided by the current regulatory scheme.

Proponents of deregulating the industry cite lower costs resulting from competition as the primary advantage to be gained. Since Idaho already has some of the lowest retail power rates in the country, how will "competition" in a deregulated industry benefit Idaho? The answer to this question involves economic and other factors that are beyond the scope of this Report. In theory, deregulation could reduce power costs in high cost states. But, such reductions could well result in higher rates for low cost states such as Idaho. Any expectation that retail power competition will flourish in Idaho upon deregulation is questionable because of the sparse and diverse population of this state. The Treasure Valley or other metropolitan areas may be attractive to entrepreneurs, but the more sparsely populated areas would not need to brace for a rush of competition. It is precisely the sparsely populated rural nature of most of Idaho that has been the basic driving force behind the traditional customer classes and rate averaging that lie at the heart of the current successful regulatory scheme. Availability of power to all customers at reasonable prices regardless of the load demanded (universal service) is a fundamental expectation of Idaho customers that has developed over decades of regulated service. Deregulation must not defeat this expectation.

Unlike the telecommunications industry, there remain few "technological breakthroughs" which can be expected from deregulation of the power industry. In telecommunications, the consumer benefited from technological advances in the fields of satellite transmission, cellular telephone (wireless) availability, and increased capacity and speed of data transmission, along with a large number of customer convenience options such as caller I.D., three-way calling, call rejection, and call waiting. In the power industry, barring highly unlikely developments, power will always be transmitted and delivered on hard wire. Other than the combined-cycle gas turbine and "real time" information availability (computerization of the industry), there have been no significant technological developments in generation, transmission or distribution in decades, and none are on the horizon. Deregulation may spur competition in generation by virtue of the opportunity for private entrepreneurs to design, site, and construct small generating facilities. However, this opportunity currently exits under PURPA and utilities have always had this generating option available.

Because of its low-cost status, Idaho should theoretically ignore the trend toward deregulation. However, the power system functions well primarily because of its "interconnectedness"—Idaho's power supply system is irretrievably linked to those of the region, as well as Canada. The power system in the Pacific Northwest pivots around the BPA, which owes its existence and function to federal, not Idaho, law. BPA's role in the regulated power system is controlled by Congress and can be modified, expanded or eliminated by Congress. The response of the BPA to deregulatory pressures will impact the power supply for Idaho, particularly for the cooperatives and municipally owned systems. Idaho should monitor what BPA intends to do, or what BPA may be required to do by Congress. Idaho must either have the knowledge to accurately anticipate the BPA's moves or Idaho must wait until the BPA acts. This same approach applies to the actions of adjacent states and to the actions of Congress and the FERC. Therefore, at least to a substantial extent, Idaho's choices on deregulation issues may be narrowed or, in some instances, even eliminated by decisions made by the legislatures of surrounding states and

Congress. Idaho, at worst, may be inexorably driven to deregulate the industry. At best, Idaho may be able to carefully craft and structure a strategy and accompanying legislation to avoid broad deregulation to, at least in part, insulate Idaho ratepayers from anticipated increases in cost of power and to prevent the exportation of Idaho's inexpensive hydroelectric power (water resources) to its high cost neighbors.

The letter to Congress from 23 regulatory commissions representing low cost energy states, Exhibit 11, urged Congress to reject any federally mandated deregulation of the industry. Fortunately, such opposition to federally mandated deregulation, when taken together with the decidedly mixed results flowing from states that have adopted deregulation, has abated the ardor of some advocates for deregulation in Congress.

Even the use of the term "deregulation," to describe the debate over access to the retail power market, may be misleading. It is virtually inconceivable that such an all-pervasive industry charged with the generation and delivery of a fundamental and necessary commodity consumed by every person and business in the United States will ever be truly "deregulated." Rather, deregulation will likely bring a change in the nature and source of the regulation of the industry and shift regulatory authority from the states to the federal government. The industry is too important, too interconnected, and too necessary to the health and safety of the citizens and economy of the country to be left to oversee itself. Additionally, the history, both in Idaho and at the federal level, of the deregulation of the telecommunications industry, is that the burden of regulatory oversight by state and federal regulators increases rather than decreases. The same phenomena could reasonably be expected if the power industry is deregulated (and it has actually occurred in California).

Another lesson to be learned from telecommunications deregulation is that once an industry is deregulated, it is nearly, if not totally, impossible to reinstate regulation. There are a number of reasons for this, most notably the Fifth Amendment to the United States Constitution and its Idaho Constitution corollary, Article I § 13, requiring due process of law and the payment of "just compensation" for a governmental taking of a private property rights for a public purpose. If the industry is deregulated, attempts at re-regulation would not only put the issue of "just compensation" in play, but could also turn on the persuasive power of the industry giants and their substantial financial capabilities. The California deregulation experience with Proposition No. 9 discussed above speaks volumes on the resources of the industry in this regard. Therefore, any fundamental changes in Idaho's policy for deregulating the industry must be right the first time. There is little room for error.

A deregulated power industry will likely be a segmented industry. Unlike the industry as we know it, the generation, transmission, distribution, maintenance, repair, construction, billing, metering, and other functions necessary to the operation of the system will be "unbundled" and may be performed by several different companies for a single customer. It may be difficult for government regulators to oversee this "unbundled" industry, and it certainly cannot be done without statutorily mandated regulatory authority. Deregulation may benefit certain sectors of our economy. The power marketers/brokers, the aggregators, and new companies providing billing services, collection services, and maintenance and repair services in such a segmented industry will, for the most part, be new to the economy and can expect to benefit financially from deregulation. Can power customers purchase power and power services from these new entrepreneurial enterprises for less than they now pay for the combined services? Perhaps not. In such a segmented industry, the guarantees of technical and supply reliability will come at a cost to the regulators and the customers. Consumer fraud and lack of financial stability are threats in a deregulated industry that have not been significantly present under the current regulatory scheme.

The deregulation debate involves one of the most complex and far reaching set of issues with which the Idaho Legislature will ever be required to deal. For instance, one of the most popular deregulation options is the ability of residential and small business customers to "opt out" for direct access to a competitive retail power market in exchange for foregoing the traditional protections of the regulated environment. Even this seemingly simple and fair concept has pitfalls as demonstrated by the following scenario. A homeowner at 100 Main Street opts to buy service from a "competitor" of the regulated utility serving the area in which the home is located. Subsequently, the homeowner sells the home to a new owner. May the new homeowner rejoin the regulated community or is service at 100 Main Street forever deregulated?

Decisions made by the legislature will impact Idaho's natural resources, consumers, economy, and lifestyle for the foreseeable future. Because of the extremely complex nature of the issues and the fundamental impacts that can be expected whether Idaho maintains the status quo or moves toward deregulation, two overriding guidelines seem appropriate: 1) Idaho should move cautiously, if at all, toward deregulation; and 2) econometric and other studies must be conducted, and those already completed must be closely examined, to fully understand the economic and other results which will flow from any decision to move toward deregulation. The legislature is blessed and burdened with the constitutional authority and duty to set Idaho's policy on the complex issues involved in the deregulation debate. The legislature is fortunate to have, at its disposal, the Public Utilities Commission, which clearly has the technical expertise to advise the legislature on the major issues involved. The legislature may wish to vest the PUC with additional authority regarding deregulation. In any event, the legislature can benefit from the expertise of the PUC, and the PUC deserves clear statutory guidance and parameters for its work and authority from the legislature. Such legislation could ratify, prohibit or expand the PUC's authority to allow some experimentation with direct retail market access or market based rates for customers; to examine unbundled costs; and other functions.

The large number of variables that are in play at any given time and the interconnected nature of our regional and national power systems create the complexity of the deregulation debate. It is as if the legislature is being forced to play a multi-dimensional chess game without rules. As in chess, many times it is not prudent to make the first move. Often, it is better to wait and see the first move made by your opponent. That appears to be the case here. The dynamic nature of the deregulation movement, when taken with the extreme complexity of the issues would seem to favor such an approach.

Both the Montana and California deregulation experiences dictate that since our current regulatory scheme works, Idaho should not rush into changing it simply for the sake of change. Idaho should watch, listen, and learn from the experiences of other states as they deregulate their industries. The clear trend, both at the state and federal levels, is to "go slow" on deregulation, a trend that Idaho should follow. Idaho's greatest future danger is that of congressionally mandated deregulation. Even that danger seems to have diminished over the last year. Nevertheless, Idaho must be involved in any policy-making activity at the federal level to assure that Congress and/or FERC do not override the interests of Idaho and its consumers.

By virtually all accounts, Idaho, as a low-cost state, does not need nor want across-the-board deregulation of the power industry now. There is sparse support for deregulation in Idaho except possibly from eastern Idaho irrigators, who want power price equity with irrigators served by Idaho Power Company and believe deregulation may be the only way to attain such equity. However, forces beyond Idaho's borders may deny Idaho the opportunity to continue regulation of the industry as we know it today. Choosing, for the time being, the status quo, as recommended by the Interim Committee, or even choosing a "go slow" approach to deregulation, will not eliminate the need to obtain information necessary to stay abreast of regional or national developments. Market pressures or activity in Congress and the FERC can impose defacto deregulation on Idaho, if they are not anticipated and dealt with by the legislature in an informed and orderly manner.

Because of the potential for action by Congress, the FERC, major utilities, and the legislatures of other states relative to deregulation, it would be prudent for the legislature and PUC to continue monitoring the following issues, factors, components, and concerns, which are beyond the scope of this Report:

- Montana deregulation experience;
- California deregulation experience;
- Impact on retail rates for all existing Idaho customer classes;
- Adjustments to, additions to, or elimination of retail customer classes;
- Cross subsidization of rates among customer classes;
- Cost of service for existing consumer classes;
- Elimination or retention of certificated service territories—effect on universal service and "provider of last resort" issues;
- Whether new authority over utilities should be granted to the PUC;
- Whether new restrictions should be placed on the authority of the PUC;
- Impact on and protection of Idaho's water resources;

- Tax legislation that may be necessary;
- Statutory guidelines for utility asset valuation;
- Identification and quantification of "stranded costs" and "stranded benefits" for Idaho utilities;
- Universal approach to quantify "stranded costs" and stranded benefits;"
- Apportionment of the benefits and liabilities associated with stranded costs and stranded benefits (ratepayers vs. stockholders);
- Impact of "ripple effect" of deregulation in adjacent states on Idaho;
- Impact of foreseeable changes at the BPA;
- Protection of Idaho ratepayers and water resources from mandated federal deregulation;
- Strategy to forestall federally mandated deregulation;
- Statutory defenses ("Poison Pills") to defeat or minimize impacts of federally mandated deregulation;
- Impact of costs of hydro-electric relicensing on cost of generation;
- Appropriateness and amount of "exit fees;"
- Impacts on cooperatives;
- Impacts on utilities;
- Impacts on municipally-owned supply systems (including municipal bonding issues);
- Impacts of divestiture of generating assets by utilities;
- Future and funding of social programs, such as low income assistance, conservation, and weatherization;
- Consumer protection issues;
- Licensing, financial, reliability, safety, supply, repair, maintenance, consumer protection, reporting, and pricing requirements;
- Entry requirements and regulation for power brokers/ marketers;
- Entry requirements and regulation for aggregators;
- Entry requirements and regulation for providers of "unbundled" or segmented services;
- Requirements for, and enforcement of requirements related to, responsibility for maintenance, repair, line construction, reliability, and safety;

- Regulatory access to records of industry participants;
- Generation facility siting requirements;
- Y2K readiness of utilities and other industry participants;
- Impact of deregulation on PUC staffing and funding needs;
- Universal approach to determine "unbundled costs;"
- Definition of "transmission;"
- Definition of "distribution;"
- Definition of "intra-state wholesale competition;"
- Equitable power costs for similarly situated consumers statewide—rural and urban power cost equity;
- Likelihood of and suspected magnitude of retail competition in Idaho;
- Desirability of instituting or continuing pilot programs fostering retail competition;
- Strategy to foster retail competition in Idaho; and
- Impact of anadromous fisheries mitigation costs on power costs.

The Office of the Attorney General stands ready to assist the legislature and the PUC on any legal issues that may arise related to the choices available to Idaho in this extremely complex process.

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1 The Working Group invited or received presentations from the following stakeholders: Idaho Power; Washington Water Power; Utah Power & Light (PacifiCorp); Idaho Retailers Association; Idaho Water Users Association; Idaho Association of Commerce and Industry; Idaho Association of Counties; Association of Idaho Cities; Potlatch Corporation; Association of Idaho Irrigators; Micron Technology; Industrial Customers of Idaho Power (e.g., Boise Cascade Corporation and Simplot); Idaho School Administrators Association; Idaho Consumer-Owned Utilities Association; Kootenai Electric Co-op; Northern Lights Co-op; and Idaho Energy Coalition (American Association of Retired Persons, Idaho Citizens Coalition, Idaho Consumer Affairs, Idaho Rivers United, Idaho Rural Council, State AFL-CIO, State Council of Senior Citizens, International Brotherhood of Electrical Workers (Local 291), and the Idaho Migrant Council).

2 In the preparation of this report, the Office of the Attorney General has amassed many documents. Pertinent and substantive materials have been included in this Report as exhibits; other documents have been compiled in an Appendix. The Appendix's Table of Contents is the last Exhibit in the Report.

3 Webster's New International Dictionary (2d Ed.) (1953), at 1269: "[Induction] 6. Elec & Magnetism. An act or process by which: . . . (3) an electromotive force is produced in a circuit by varying the magnetic field linked with the circuit (electromagnetic induction) . . . ."

4 Pacific Gas & Electric Company, "Resource: An Encyclopedia of Utility Industry Terms," at 130-31 (1985) (hereinafter, "PG&E").

5 This use of solar energy for generation is distinct from photovoltaic processes, in which sunlight is converted directly into electricity via a solid state semi-conductor devise, commonly made from silicon. See PG&E, supra, at 252-54.

6 PG&E, supra. See also, Leonard Hyman, "America's Electric Utilities: Past, Present and Future," Public Utilities Reports, Inc. at 21-23 (5th Ed.) (1994) (hereinafter, "Hyman").

7 Another measure of price is sometimes calculated in mills per kilowatt. A mill is equal to 1/10 cent.

8 PG&E, 62, 311-12.

9 In telecommunications, wireless technology (cellular, PCS, LMDS, DBS, etc.) can bypass wireline connections to the consumer by radio wave.

10 Alaska and Hawaii are not physically interconnected with the lower-48 network. Texas maintains a "normally open interconnection" interface with the rest of the lower-48 network. Some intertie exists with Canadian and Mexican systems. See Energy Information Administration (DOE), "The Changing Structure of the Electric Power Industry: An Update," at 15-18 (Washington, D.C. 1996) (hereinafter, "EIA").

11 Voltage is the measure of electrical pressure in a circuit. PG&E at 340.

12 Peter Fox-Penner, "Electric Utility Restructuring: A Guide to the Competitive Era," Public Utilities Reports, Inc. at 23 (Vienna, Virginia 1997) (hereinafter "Fox-Penner").

13 For a general discussion of these considerations, see Hyman at 33-34; Fox-Penner at 26.

14 Ron Binz, et al. "Navigating a Course to Competition: A Consumer Perspective on Electric Restructuring," Competition Policy Institute at 27-29 (Washington, D.C., 1997); PG&E at 138, 141-144. Idaho is in the Western Systems Coordinating Council. The WSCC recently moved to implement a reliability management system covering operating reserves, disturbance controls, performance standards, etc.

15 16 U.S.C. § 824(d).

16 EIA at 28-29.

17 16 U.S.C. § 824(b)(1).

18 Charles Phillips, "The Regulation of Public Utilities" at 583-85 (2d ed. 1988).

19 Alan Richardson (American Public Power Assn.), Remarks to the American Bar Association (Dec. 3, 1998).

20 "Promoting Wholesale Competition Through Open Access Non-Discriminatory Transmission Services by Public Utilities; Recovery of Stranded Costs by Public Utilities and Transmitting Utilities," FERC Docket Nos. RM95-8-000 and RM94-701, Order No. 888 (April 24, 1996) (hereinafter "Order No. 888"). Idaho and nine other states have appealed portions of FERC's Order No. 888 to the Second Circuit Court of Appeals.

21 FERC Order No. 888, Appendix G, "Legal Analysis of Commission Jurisdiction Over the Rates, Terms and Conditions of Unbundled retail Transmission in Interstate Commerce," at 40-41.

22 FERC Order No. 888 at 198.

23 FERC Order No. 888 at 200-201.

24 D. Fessler, "Social, Economic, and Political Perspectives on California's Role in the Changing Dynamics of the electric Industry," National Regulatory Research Institute, Quarterly Bulletin (Vol. 17, No. 3 1996) at 338-39.

25 J. Dierdorff, "How Edison's Lamp Helped Light the West" (Pacific Power & Light 1971) at 7 (hereinafter, "Dierdorff").

26 Susan Stacy, "Legacy of Light—A History of Idaho Power Company" at 3-4 (1991).

27 *Id.*

28 EIA at 5.

29 EIA, citing Encyclopedia Americana, International Edition, Vol. 23 (New York, N.Y.; Americana Corporation 1977), p. 769.

30 Dierdorff at 177.

31 Fox-Penner at 12.

32 *Id.*

33 See Hyman at 119, 127.

34 Fox-Penner at 14.

35 For further discussion of these events, see Hyman , 141-148; Fox-Penner, 12-17.

36 On January 1, 1999, Washington Water Power officially became known as Avista Corporation.

37 On December 7, 1998, PacifiCorp agreed to "merge" with ScottishPower. ScottishPower currently serves 7,000,000 customers in the United Kingdom while PacifiCorp serves about 2,000,000 customers in the western United States and Australia. Under the terms of the merger agreement, each PacifiCorp share will be exchanged for 2.32 ordinary shares of ScottishPower. After the merger, ScottishPower shareholders and PacifiCorp shareholders will own approximately 64% and 36% of the combined company, respectively. According to the companies' press release, the price paid for each PacifiCorp share is $25.13. PacifiCorp's share price closed on the date of the press release at $20.56.

If approved, the merger would be the first time a foreign utility acquired a U.S.-based vertically integrated utility. The merger is subject to the approval of the shareholders of both companies, the FERC, and the regulatory commissions in the states served by PacifiCorp. The transaction is also subject to review by the S.E.C. and U.S. Department of Justice. The companies expected the transaction will close in the fall of 1999.

38 Idaho Code §§ 61-119 and 61-129.

39 Idaho's Electric Cooperatives include: Clearwater Power Company, East End Mutual Electric, Fall River Rural Electric Co-op, Idaho County Light & Power Co-op, Kootenai Electric Co-op, Lost River Electric Co-op, Northern Lights, Raft River Rural Electric Co-op, Riverside Electric Company, Salmon River Co-op, South Side Electric Lines, and United Electric. PUC Annual Report (1998).

40 Charles Phillips, "The Regulation of Public Utilities" at 599 (2d ed. 1988).

41 The Idaho municipal supplier serve the communities of: Albion, Bonners Ferry, Burley, Declo, Heyburn, Idaho Falls, Minidoka, Plummer, Rupert, Soda Springs, and Weiser. PUC Annual Report (1998). Rupert is considering selling its distribution system, prompted by potential adverse impacts of deregulation. Reported suitors include Idaho Power, the City of Burley, and United Electric (a cooperative). Clearing Up, No. 858 at ¶ 12 (Dec. 21, 1998).

42 Idaho Code § 61-104.

43 Under the Public Utilities Regulatory Policy Act (PURPA) an investor-owned utility is required to purchase power from qualifying PURPA facilities at the utility's "avoided costs." See pages 21-22.

44 In early December 1998, WWP announced plans that its affiliate Avista Power will build a gas-fired generating plant of about 270 mW in Rathdrum, Idaho. Another affiliate, Avista Energy, will deliver the natural gas to the plant and purchase the output.

45 Idaho Falls does have its own hydroelectric facilities.

46 C. Phillips at p. 600.

47 Presentation of Idaho Attorney General Alan G. Lance to Special Legislative Committee on Utility Restructuring at p. 2 (September 1996).

48 PUR Utility Weekly at p. 1 (November 6, 1998).

49 PUR Utility Weekly (November 6, 1998) at p. 1 quoting DOE's Energy Information Administration's "Electric Sales and Revenue 1997." (EIA Website at "ftp://ftp.eia.doe.gov/pub/ electricity").

50 Forrester, Khaneja, Haeri & Carter, "Which Utility Ranks the Highest," Public Utility Fortnightly at 24 (Sept. 1, 1998).

51 EPRI Report TR-104858, "Water Resource Management and Hydropower: Guidebook for Collaboration and Public Involvement," Prepared by Kearns & West, Inc., San Francisco and Richard Hunt Associates, Annapolis (Dec. 1995).

52 The avoided cost resource assumption is now a gas-fired turbine generator.

53 Gregory Basheda, et al., "The FERC, Standard Cost Recover and Municipalization," 19 Energy Law Journal 351 (1998).

54 Idaho Code § 61-501.

55 In re Idaho Light & Company, 2 P.U.C.I. 53 (1915A).

56 Kootenai Electric Cooperative v. Washington Water Power, 127 Idaho 432, 901 P.2d 1333 (1995).

57 "Escheat," as used in Idaho Code § 61-328, means that ownership of the property reverts to the state as a consequence of violating this statute. See Idaho Code § 61-329 (after paying liens and claims against the property, the balance of the sales proceeds "shall be paid into the state treasury for the credit of the school fund").

58See historical text on page 11.

59 Susan Stacy, "Legacy of Light – A History of Idaho Power" at 190-203 (1991).

60 The flow is measured at the Murphy Gage.

61 See discussion of special contract customers on page 18.

62 For a good overview of electric restructuring issues, see "The Wall Street Journal Reports: Energy," The Wall street Journal, Section R (Sept. 14, 1998).

63 See discussion on page 11.

64 Fox-Penner at 89.

65 EIA at 38.

66 "Open Access Same-time Information System (formerly Real-time Information Networks) and Standards of Conduct," FERC Docket No. RM95-9-000, Order No. 889 (April 24, 1996) at 9, 88 (hereinafter, "FERC Order 889").

67 In the years 1990 through 1994, non-utility net additions to generation capacity exceeded utility additions. EIA at 14-15.

68 FERC Order No. 888 at 24, n.42: ". . . Power marketers take title to electric energy. Power brokers, on the other hand, do not take title and are limited to a matchmaking role."

69 Examples of aggregators include: school districts, retailers, grocery chains, even residential customers in Montana.

70 Fox-Penner at 89.

71 Telecommunications Act of 1996, amending the Communications Act of 1934, 47 U.S.C. 151, et. seq.

72 FERC Order No. 888 at 26.

73 House Concurrent Resolution No. 34, Alaska State Legislature, Twentieth Legislature (2nd Sess.) (May 1998).

74 Alan Lance, "Federal One-size-fits-all Electric Energy Proposal may not be Best for Idaho," Idaho Statesman (Nov. 4, 1997).

75 Such as General Accounting Principles (GAP).

76 Bluefield Water Works Improvement Co. v. P.S.C. of West Virginia, 262 U.S. 679 (1923); Federal Power Commission v. Hope Natural Gas Co., 320 U.S. 591 (1944).

77 FERC Order No. 888 at 443-44.

78 FERC stranded costs are defined in terms of "wholesale stranded costs." See FERC Order No. 888 at 618-29.

79 Fox-Penner at 397.

80 See, e.g., Public Utilities Code, State of California, Chapter 2.3 "Electric Restructuring" Section 330(s): ". . . In determining the costs to be recovered, it is appropriate to net the negative value of above market assets against the positive value of below market assets" (hereinafter, "CPUC Code").

81 Bangor Daily News (Sept. 29, 1998).

82 Hayden Pines Water Co. v. Idaho PUC, 122 Idaho 356, 834 P.2d 873 (1992); Utah Power & Light Co. v. Idaho PUC, 102 Idaho 282, 629 P.2d 678 (1981); Intermountain Gas Co. v. Idaho PUC, 97 Idaho 113, 540 P.2d 775 (1975); In re Mtn. States Tel. & Tel. Co., 76 Idaho 474, 284 P.2d 681 (1955).

83 Idaho's Constitution provides that "the police powers of the state shall never be abridged or construed as to permit corporations to conduct their business in such a manner as to infringe the equal rights of individuals, or the general well being of the state. Art. XI, § 8.

84 Fox-Penner at 385-86.

85 For example, the recent sale of Montana Power Company's assets was 155% of book value. See related text on page .

86 See, e.g., Central Maine Power Company Divestiture of Generation Assets, Maine Public Utilities Commission Docket No. 97-523, Order (Part II) (January 14, 1998) at 1 (hereinafter, "CMP Order"): "The Restructuring Act requires the divestiture [of CMP's generation assets and all generation-related business activities] to be accomplished according to a plan submitted to the commission for review. The divestiture of generation assets is important both as a means to ensure effective competition and as a means to value generation assets for purposes of measuring stranded costs."

87 Another form of ISO is the TransCo—a term usually referring to a separate, private corporation controlling the transmission assets. Some believe that a private-for profit would be more inclined to safeguard and maintain the transmission assets.

88 Otter Tail Power Co. v. United States, 410 U.S. 366 (1973).

89 In a Notice issued December 1, 1998, FERC requested input from state PUCs regarding transmission policy. In particular, FERC invited states to comment on the need for designating boundaries for regional transmission operators (ISO, TransCo, RGO) and the governance of the RTOs. FERC Order No. 888 encourages the formation of RTOs. 63 Fed. Reg. 66, 158 (Dec. 1, 1998).

90 Similar to imputed access charges for telecommunication companies, Idaho Code § 62-609.

91 FERC Order No. 889 at 9.

92 BPA's Business Transmission unit is anticipating a rate case for transmission issues to follow BPA's power rate case. The agency would like to have new transmission rates in place by October 2001.

93 In some Western rural areas (e.g., Washington, Oregon) where investor-owned utilities were slow to expand, public power entities may own a more noticeable share of the local distribution (and some transmission) facilities. See EIA at 7, 12-15.

94 Assuming, of course, that there are sellers willing to enter a particular market. Rural states with low population density may not find sellers willing to enter rural markets.

95 See CPUC Code Section 331(a), (b), (c).

96 See, e.g., Montana [code cite] 69-8-404 concerning licensing of "electric suppliers" and 69-8-103 (9) defining "electric suppliers" to include aggregators, marketers, and brokers offering to sell electricity to retail customers.

97 Competitive Policy Institute, "Addressing Market Power: The Next Step in Electric Restructuring," at 1 (Washington, D.C. 1997).

98 See CMP Order, supra footnote 86.

99 See Idaho Code § 62-612 regarding telecommunications providers of last resort.

100 For example, California committed $90 million to consumer education.

101 The Clinton Administration restructuring plan ("Comprehensive Electricity Competition Plan") proposed to create a $3 billion public benefit fund (PBF) to provide matching funds to states for projects such as energy efficiency, renewables, and consumer education.

102 Fessler 355. During the three-year period 1998-2000, California has budgeted about $1.16 billion in public purpose programs, including renewables, energy efficiency, low-income support, and research and development.

103 Caution must be exercised in categorizing the activities of particular states as (a) having taken "final action" with respect to electric restructuring matters or (b) having restructured or determined not to restructure. Each state's activities reflect the unique characteristics of that state, including constitutional, statutory, regulatory, economic, political, and other factors. A summary of the status of state activities is included in the Appendix. See also Edison Electric Institute, "Current Status Summary," Washington, D.C. (Aug. 1998).

104 Montana Dakota Utilities Company may postpone offering its customers access to retail competition until 2006.

105 In October 1998, Montana Power sued the PSC alleging that the standards of conduct and affiliate rules were unreasonable.

106 At least one large industrial customer (arguing it was cut out of the sharing formula), has asked the PSC to reconsider its decision. "Parties Ask MPSC to Modify Profit Allocation in PacifiCorp Sale", Clearing Up, No. 854 at ¶19 (Nov. 23, 1998). In December 1998, the PSC granted motions to reconsider the fund allocation and will hold hearings in 1999. Clearing Up, No. 858 at ¶ 9.5 (Dec. 21, 1998).

107 An affiliate, PP&L Inc., serves 1.2 million customers in Pennsylvania.

108 "Public purpose law on hold as [Montana] restructuring hits another snag," Clearing Up, at ¶¶ 1-17, No. 858 (December 21, 1998).

109 Electric Power Alert at 17 (November 18, 1998).

110 For a review of past federal restructuring bills, see "Report of the Electric Utility Regulation Committee (Federal Energy Bar Ass'n)," 19 Energy Law Journal 465 (1998); Appendix.

111 Maloney, McCormick & Sauer, "Customer Choice, Consumer Value: an Analysis of Retail Competition in America's Electric Industry," Citizens for a Sound Economy Foundation at 33 (July 1996).

112 Energy Information Administration, "Electricity Prices in a Competitive Environment: Marginal Cost Pricing of Generation Services and Financial Status of Electric Utilities", DOE/EIA-0614 at 51, 57 (August 1997).

113 Hirst and Hadley, "Will Electricity Competition Benefit Customers in Low-Cost Regions?," Energy Division, Oakridge National Laboratory, reprinted in NRRI Quarterly Bulletin, Vol. 19 No. 1, Spring 1998.

114 Created by House Concurrent Resolution No. 2, by the First Regular Session of the Fifty-fourth Idaho Legislature 1997 S.L. page 32 (1997).

OFFICIAL OPINIONS
OF
THE ATTORNEY GENERAL
FOR 1999

ALAN G. LANCE
ATTORNEY GENERAL
STATE OF IDAHO

ATTORNEY GENERAL OPINION 99-1

The Honorable John H. Tippets
Idaho House of Representatives
Idaho State Legislature
STATEHOUSE MAIL

Per Request for Attorney General's Opinion

QUESTION PRESENTED

Does the ballot access restriction contained in Idaho Code § 34-907(1)(c) apply to members of the judiciary?

CONCLUSION

The phrase "state elected official" is not defined in the Idaho Code. However, this office believes that a reviewing court probably will conclude that the judiciary is not included in the ballot access restriction created by Idaho Code § 34-907(1)(c).

ANALYSIS

Idaho Code § 34-907 was enacted by voter initiative, along with Idaho Code §§ 50-478 and 33-443, during the 1994 general election. Collectively, these provisions appeared on the ballot as "Proposition 2." The statutes enacted through Proposition 2 established ballot access restrictions for a variety of incumbent federal state and local officials. While ballot access restrictions for federal elected officials were ruled unconstitutional by the United States Supreme Court in United States Term Limits, Inc. v. Thornton, 514 U.S. 779 (1995), Proposition 2's ballot access restrictions for state and some local officials remain in place.

As an initial matter, art. 3, sec. 1 of the Idaho Constitution states that the voters of Idaho may exercise the power to enact legislation without the legislature:

> This power is known as the initiative, and legal voters may, under such conditions and in such manner as may be provided by acts of the legislature, initiate any desired legislation and cause the same to be submitted to the vote of the people at a general election for their approval or rejection.

Idaho Const., art. 3, §1.

The Idaho Supreme Court has determined that the initiative is "on equal footing" with acts of the legislature. Luker v. Curtis, 64 Idaho 703, 706, 136 P.2d 978, 979 (1943). Therefore, in attempting to interpret the phrase "state elected official," a reviewing court is likely to use whatever information was prepared in connection with Proposition 2 to determine the meaning of language within the proposition in the same way that a court would use legislative history to determine the meaning of statutory language adopted by the legislature.

Idaho Code § 34-907(1)(c) prohibits a person's name from appearing on an election ballot if that person has served as "a state elected official, during eight (8) or more of the previous fifteen (15) years." The phrase "state elected official" is not defined in the Idaho Code. Therefore, it is possible to argue that since members of the judiciary are subject to retention elections every four or six years, they should then be considered state elected officials for purposes of Idaho Code § 34-907(1)(c). However, there are two factors that serve to undercut this conclusion.

First, the ballot title for the initiative enacting term limits in 1994 stated that Idaho Code § 34-907(1)(c) is limited to "state executive offices":

proposition two
an initiative establishing term limits for elected federal, state, county, municipal and school district officials

> Initiative relating to the number of years an elected official may serve: providing a new section to the Idaho Code, § 34-907, limiting the number of years a person may serve in the following elected offices by restricting eligibility to appear on the ballot after serving a prescribed number of years: United States House of Representatives, United

> States Senate, state executive offices, state legislature, county elected offices; providing a new section to the Idaho Code, § 50-478, restricting municipal officers' eligibility to appear on the ballot after serving eight years in one position; providing a new section to the Idaho Code, § 33-443, restricting school district trustees' eligibility to appear on the ballot after serving six years in one district; providing that any person may stand for election as a write-in candidate; providing an effective date of January 1, 1995; providing that service prior to that date shall not be counted for purposes of ballot eligibility and providing a severability clause.

(Emphasis added.)

Naturally, members of the judiciary do not hold "state executive offices." Put another way, judges and justices are not officers of the executive branch of government. They are officers of the judicial branch governed by art. 5 of the Idaho Constitution.

Idaho Code § 34-1809 sets out a formal process for the development of ballot titles. They are intended to be a "true and impartial statement of the purpose of" the initiative. Idaho Code § 34-1809. In preparing these titles, the office of the attorney general is performing "a quasi judicial function." In re Idaho State Fed'n of Labor, 75 Idaho 367, 374, 272 P.2d 707, 711 (1954). As a result, a reviewing court is likely to place great importance on how a ballot title describes the application of a voter initiative. If a reviewing court follows the ballot title that was developed for Idaho Code § 34-907(1)(c), then the court is likely to rule that ballot access restrictions apply only to executive branch officers, not to members of the judiciary.

Second, the event that triggers Idaho Code § 34-907(1)(c)'s ballot access restriction is the holding of a "state elected office" for eight or more years after January 1, 1995. For every official covered by section 34-907(1)(c), the statutory limit coincides with the end of the second term of office. If the provision applied to members of the Idaho Supreme Court, for example, the eight-year limit would occur at the midpoint of each justice's second term because art. 5, sec. 6 of the Idaho Constitution establishes six-year terms for members of the Idaho Supreme Court. A reviewing court is likely to conclude that section 34-907(1)(c) does not apply to members of the judiciary because it does not reflect the actual term of office for some members of the judiciary.

AUTHORITIES CONSIDERED

1. **Idaho Constitution:**

   Art. 3, § 1.
   Art. 5.
   Art. 5, § 6.

2. **Idaho Code:**

   § 33-443.
   § 34-907.
   § 34-907(1)(c).
   § 34-1809.
   § 50-478.

3. **Federal Cases:**

   United States Term Limits, Inc. v. Thornton, 514 U.S. 779 (1995).

4. **Idaho Cases:**

   In re Idaho State Fed'n of Labor, 75 Idaho 367, 374, 272 P.2d 707, 711 (1954).

   Luker v. Curtis, 64 Idaho 703, 136 P.2d 978 (1943).

Dated this 17th day of March, 1999.

Sincerely,

ALAN G. LANCE
Idaho Attorney General

Analysis by:

Matthew J. McKeown
Deputy Attorney General

ATTORNEY GENERAL OPINION 99-2

Honorable Shawn Keough
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Honorable Dolores J. Crow, Chair
House Revenue and Taxation Committee
Idaho House of Representatives
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Honorable Jerry Thorne
Idaho State Senate
331 Winther Boulevard
Nampa, ID 83651

Dear Senators Keough, Dunklin and Thorne and Representative Crow:

Each of you requested an Attorney General's Opinion on closely related issues about the proper application of the Idaho Constitution's requirement that "bills for raising revenue shall originate in the house of representatives." This opinion responds to all three requests.

QUESTIONS PRESENTED

1. Must a bill to amend a property tax exemption for certain agricultural property by removing apparently limiting language, thereby presumptively expanding the exemption, originate in the House of Representatives? (Senator Keough)

2. Whether a bill to exempt a non-profit, charitable organization from sales tax was properly printed and considered in the Senate Local Government and Taxation Committee. (Senator Dunklin)

3. "The Revenue and Taxation Committee respectfully requests an Attorney General's opinion regarding the constitutionality of starting all tax bills, both adding and taking from the revenue base, in the house of representatives." (Representative Crow)

CONCLUSIONS

Prudence requires that bills potentially affecting general revenues be introduced in the house of representatives. The existing authority interpreting article 3, section 14 of the Idaho Constitution ("the Origination Clause") is both sparse and ambiguous. This lack of definite guidance strongly counsels a cautious approach that favors introducing doubtful bills in the house or adding senate amendments to revenue bills originating in the house if that can be done consistently with the Idaho Constitution's provision limiting bills to one subject.

A strong, but not certain, case can be made (contrary to prior guideline letters issued by this office) that the Idaho Supreme Court would follow the general rule that revenue bills are those that levy taxes, in the strict sense of the word, and not bills for other purposes which may incidentally create new revenue. However, existing Idaho authority suggests the Idaho Supreme Court may find bills to be revenue bills that would not be so classed by other courts.

The only Idaho case addressing the subject seems to favor the rule that a bill having the effect of raising less revenue in the future than was raised in the past is still a bill raising revenue and therefore must originate in the house.

An additional complication relates to property tax bills, such as S.B.1219 (about which Senator Keough inquires), because article 7, section 6 of the Idaho Constitution prohibits the legislature from raising property tax revenues for local governments. This might mean that bills relating to property taxation could not be revenue bills. The Idaho Supreme Court, however, has not ruled on this possibility so it cannot be clearly said to be the law of the State of Idaho.

ANALYSIS

A. Considerations Guiding the Analysis

This opinion reflects a particularly cautious approach by recommending a more expansive understanding of what is a revenue bill. Because it is also possible to justify a more limited understanding (which would allow additional types of bills to be introduced in the senate), it is important to express the reasons for this caution.

First. This opinion keeps in mind Justice Harlan's comment about the Origination Clause of the U.S. Constitution in Twin City Nat'l Bank v. Nebaler, 167 U.S. 196, 202 (1897), "What bills belong to that class [of bills raising revenue] is a question of such magnitude and importance that it is the part of wisdom not to attempt, by any general statement, to cover every possible phase of the subject."

Second. Most of the knowledge about Idaho's Origination Clause must be drawn from Dumas v. Bryan, 35 Idaho 557, 207 P. 720 (1922). In addition to being over 75 years old, that case is subject to differing understandings.

Third. Legislative reliance on a less cautious opinion may result in the enactment of invalid laws if, as several guideline letters from this office suggest, the Idaho Supreme Court ultimately rejects the more limited interpretation that "revenue bills" are only those that levy taxes.

Fourth. Any controversy finding its way into court will involve a law requiring payment of money to the government. To justify litigating the issue, the amounts are likely to be significant. If the law resulted from a senate bill that is found to be a revenue bill that should have originated in the house, the law will be void. *See* Dumas, 35 Idaho at 564, 207 P. at 722. Those who paid the money will be due refunds. *See, e.g.*, Idaho Code § 63-3067 (1998). If the case is a class action, the resulting depletion of the state treasury by refunds could be large. *See, e.g.*, Ware v. Idaho State Tax Commission, 98 Idaho 477, 483, 567 P.2d 423, 429 (1977).

Fifth. Mistakes are easily avoided. Resolving questions of doubt in favor of originating bills in the house removes any taint of unconstitutionality under the Origination Clause.

B. Introduction

Article 3, section 14 of the Idaho Constitution provides:

Bills may originate in either house, but may be amended or rejected in the other, except that bills for raising revenue shall originate in the house of representatives.

(Emphasis added.) The Idaho Constitutional Convention in 1889 adopted this section without debate or amendment. Proceedings, Constitutional Convention, Vol. II, p. 1227.

The federal Constitution, and the constitutions of many states, contain similar origination provisions. *See* Dumas, 35 Idaho at 564, 207 P. at 722. "The requirement that revenue bills must originate in the House of Representatives is historically derived from Parliament's long struggle with the Crown for control of the purse-strings of the English Empire." Worthen v. State, 96 Idaho 175, 178, 525 P.2d 957, 960 (1974). The Origination Clause of the federal Constitution (Art. I, § 7) accomplished two purposes. First, it was one of several important "counterpoises" to the additional authorities conferred upon the Senate, such as the trying of impeachments, confirmation of executive appointments, and ratification of treaties. The Federalist No. 66 (Alexander Hamilton); Millard v. Roberts, Treasurer of the United States, 202 U.S. 429 (1906). Second, it ensured that the branch of the national legislature most representative of the people, the House of Representatives, would have to take the political initiative of taking more money from the people through taxation. *See* Dumas, 35 Idaho at 563, 207 P. at 723. *See also*, T. Jipping, TEFRA and the Origination Clause: Taking the Oath Seriously, 35 Buff. L. Rev. 633, 649 (1986).

C. Decisions of the Idaho Supreme Court

The Idaho Supreme Court has decided only a few cases involving challenges under the Origination Clause. Consequently, there is sparse guidance from which to draw concrete conclusions. Any definite answers to the questions presented must be drawn from only three significant cases in which the Idaho Court has ruled on the Origination Clause. These cases need some examination and explanation and can be briefly summarized.

1. Worthen v. State, 96 Idaho 175, 525 P.2d 957 (1974)

The plaintiffs challenged, under the Origination Clause, the 1972 enactment of House Bill 789. *See* Worthen v. State, 96 Idaho 175, 176, 525 P.2d 957, 958 (1974), *citing* 1972 Idaho Sess. Laws 1149. The bill made significant changes to Idaho's Income Tax Act. Although the bill originated in the house of representatives, the senate added two significant amendments. *See* Worthen, 96 Idaho at 177, 525 P.2d at 952. The first repealed the individual deduction for federal income taxes (thereby increasing the amount of Idaho tax due from individuals). *Id.* The second increased the corporate income tax rate from 6% to 6.5%. *Id.* The challenge to the senate's right to amend a revenue bill originating in the house arose because of the difference between the federal and state versions of the Origination Clause. As the Idaho Supreme Court explained:

> The United States Constitution has a similar provision in art. I, § 7,
>
> "All Bills for raising Revenue shall originate in the House of Representatives; but the Senate may propose or concur with Amendments as on other bills."
>
> The United States Constitution's provision for revenue bills differs from the Idaho provision in that it specifically provides that the Senate may amend revenue bills that originate in the House.

96 Idaho at 178, 525 P.2d at 961.

Despite the absence from Idaho's Origination Clause of language expressly authorizing senate amendment of revenue bills, the court concluded that the senate could do so, holding:

> Article 3, § 14 does not prohibit the Senate from denying passage of a revenue bill, and it does not specifically prohibit the

> Senate from amending a revenue bill. House Bill 789 began in the House as a revenue bill. Under a strict reading of art. 3, § 14 as argued by the appellants, the Senate could only veto House Bill 789 and could not have suggested the changes that the House subsequently concurred in. To prohibit the Senate from amending House originated revenue bills, would be an obstruction of the legislative process. Art. 3, § 14 must be read to require that revenue bills originate in the House, and that the Senate is permitted to amend such bills. House Bill 789 was not enacted in violation of art. 3, § 14. *Id.* at 179, 961. [1]

2. State ex rel. Parsons v. Workmen's Compensation Exchange, 59 Idaho 256, 81 P.2d 1101 (1938)

At issue in Parsons were worker's compensation benefits payable as the result of the work-related death of an employee. The relevant statute, originally enacted as a Senate bill, provided that if a deceased worker was without dependents (as was the case in *Parsons*), the death benefit was payable to the state treasury. *See* Parsons, 59 Idaho at 260, 81 P.2d at 1102. The surety liable to pay the benefits contended that this provision rendered the bill enacting that law a revenue bill that should have originated in the House. *Id.*

The Idaho Supreme Court rejected this position, holding that "we do not consider this provision of the act, either in part or as a whole, as a revenue act or as an act levying a tax." *Id.* The court reasoned:

> Now, as we understand this statute, it was the intention of the legislature that *compensation* should be paid by the employer or his surety *for every employee killed by accident* while engaged in the course of his employment. . . . When no one appears within a year who can qualify as a dependent, within the definition of the statute, then it is made the duty of the proper official to file a claim for the sum of $1,000 in behalf of the state. In other words, the state, as the *sovereign or parens patriae*, asserts its right to recover for the death of an employee, in the event no person qualifies as an

> actual dependent within the meaning of the statute. It certainly can not be gainsaid that the state has an interest in these employees, its subjects to whom it owes police and general welfare protection, which is equal to, if not superior to, the interests of some of the persons who are named as dependents. We know of no reason why the state may not be made a beneficiary under such a law as well as the persons designated as dependents. Had the decedent died a natural death and left an estate, and left no heir or person surviving him entitled under the succession statute to take his estate, the same would go to the state under the law of escheat (subd. 9, sec. 14-103, I.C.A.), which is as old as the common law; and no one would seriously question the right of the state to take such property. For like reasons we can see no constitutional objection to the state, in its corporate capacity as the sovereign or head of the governmental family, asserting its right to compensation from industry, in the case of the death of one of its subjects while engaged in the course of his employment, where no actual dependent exists.

59 Idaho at 261, 81 P.2d at 1102.

3. Dumas v. Bryan, 35 Idaho 557, 207 P. 720 (1922)

This is the most important and the most perplexing of the three Idaho cases decided under the Origination Clause. The facts were that in 1921 the legislature enacted a bill, which originated in the senate, providing for the transfer of the Albion Normal School from Albion to Burley. *See* Dumas, 35 Idaho at 562, 207 P. at 721 (referencing 1921 Idaho Sess. Laws 256). The first four sections of the bill provided the authorization and procedures of the change. *Id.* The fifth section levied a statewide property tax of one-eighth mill for two years to fund the move. *Id.* Opponents of the move challenged the entire statute on Origination Clause grounds. *Id.*

The court reviewed the then existing case law from other states applying similar state constitutional provisions. The court acknowledged:

> [M]any cases holding that where the revenue part of an act is merely an incident and not the principal purpose for which it was enacted, the fact that it contains a provision for raising revenue as an incident to such purpose does not make it a revenue law within the meaning of this constitutional provision.

35 Idaho at 564, 207 P. at 722.

The court's survey of then-existing case law included two cases analogous to the facts before it in the Dumas case. The court summarized these cases as follows:

> Thus in *Chicago, B. & Q. R. Co. v. School District No. 1*, 63 Colo. 159, 165 P. 260 (1917), an act amending a former law which established a system of public schools, and, as an incident to such amendment, provided for the raising of revenue to meet the requirements of the law as amended, was properly held not to be an act for the raising of revenue, which under the Constitution must originate in the House of Representatives.
>
> So in *Evers v. Hudson*, 36 Mont. 135, 92 P. 462 (1923), it is held that an act authorizing the establishment of county free high schools, and providing for a tax to supply funds for the current expenses of such schools and for bond issues to raise money for building or purchase of school property, authorizing the commissioners to make a tax levy upon all of the property for the support thereof, and limiting the funds so raised exclusively to this purpose, does not fall within the purview of this constitutional provision.

Id.

After reviewing this and other case law from other jurisdictions establishing the general rule that when the revenue raising part of a bill is merely incidental to the bill's main purpose the bill is not a revenue bill that must originate in the house, the Idaho Supreme Court ruled as follows:

> Section 5 of this act is a measure for raising revenue; that is, it is a revenue bill, or money bill, as those terms are usually used. It provides for levying a direct tax against all property in the state, for governmental purposes. It requires no argument to prove that the state maintains the Albion normal school in its governmental capacity. <u>It will not do to say that this tax represents a mere incident to the main purpose of the bill, for this would be a mere evasion. Most revenue bills could in the same manner be made incidental.</u> The amount of the tax levied is immaterial, for the Constitution requires that all bills for raising revenue shall originate in the House. This is as truly a tax levied for governmental purposes, as it would be if levied for the construction of a capitol building, an insane asylum, or for the support of any department of the state government, and therefore falls within the inhibition of article 3, § 14, of the Constitution.

35 Idaho at 566, 207 P. at 723 (emphasis added).

The <u>Dumas</u> court then concluded that the bill at issue was a revenue bill that, because it originated in the senate, was unconstitutional. *Id.* Because, without the revenue needed, moving the Albion Normal School was impossible; the invalid portion of the statute was inseparable from the remainder. Therefore, the court held, the entire statute was void. *Id.*

D. Discussion

These cases establish definite rules upon which the legislature can rely.

The <u>Dumas</u> case establishes that originating a revenue bill in the senate is a fatal flaw that can result in the enacted statute's being declared void if it is challenged. This is the majority rule in other states. *See* <u>Morgan v. Murray</u>, 328 P.2d 644, 654 (Mont. 1958). It is also the federal rule. *See* <u>U.S. v. Munoz-Flores</u>, 495 U.S. 385, 387 (1990). The exception appears to be Pennsylvania, which has held that because both branches of its state legislature are equally representative of the electorate, the constitutional commandment is procedural, not substantive, and therefore is left to the duty and conscience of the members of the legislature. *See* Mikell v. Philadelphia School District, 58 A.2d 339, 341 (Pa. 1948).

The Worthen case definitely establishes the right of the Idaho Senate to amend a revenue bill to add revenue-raising returns, but does not directly address the issues to which this opinion is directed.

The Parsons case establishes that not every statute that results in the addition of moneys to the state treasury is a revenue bill within the meaning of Idaho's Origination Clause. Although that case held that the worker's compensation provisions at issue in that case were not the result of a revenue bill, the case provides no analysis or discussion of what constitutes a revenue bill. However, the ruling is consistent with the general rule applied by federal courts and in other states. That general rule is "that revenue bills are those that levy taxes, in the strict sense of the word, and not bills for other purposes which may incidentally create new revenue." Twin Cities Nat'l Bank, 167 U.S. at 201 (*citing* Story, Commentaries on the Constitution § 880); U.S. v. Munoz-Flores, 167 U.S. at 495, U.S. at 397. The Idaho court recognized that this rule is the general rule in Dumas. *See* 35 Idaho at 566, 207 P. at 723.

The confusion over Dumas arises because the court voided a statute primarily aimed at moving the Albion Normal School, but which also imposed a statewide property tax levy to fund the move. Attorney general guideline letters issued by this office have understood Dumas to reject the general rule:

> The general rule . . . is that if the revenue raising provisions are "incidental" to the main provisions of the act, it may originate in the Senate. This argument however specifically was rejected in *Dumas v. Byron*, ...

Guideline letters to Senator Fairchild dated Feb. 24, 1983, and to Senators Beitelspacher and Anderson dated Feb. 25, 1986.

This conclusion flows from the fact that the Dumas court, in explaining the general rule, summarized cases from other states (including the Montana and Colorado decisions discussed above) involving statutes that were similar to the statute in Dumas but were held valid. That the Idaho court in Dumas then struck down the Idaho statute strongly implies that the court was indeed rejecting the rule that incidental revenue provisions do not make a bill a revenue bill.

If this is correct, then Idaho legislators may not reliably look to interpretations of origination clauses of either the U.S. Constitution or those of other states for guidance to help determine what kind of bills are revenue bills under the Idaho Constitution. Given the dearth of Idaho cases, there is virtually no reliable guidance available to legislators (or attorneys general and their deputies) for resolving close questions about where a bill must originate. Nevertheless, Dumas makes it clear that originating a bill in the wrong body can be fatal if it is successfully challenged.

There is another way to read the Dumas decision. That is that the court in Dumas did not reject the general rule. Instead, Dumas accepted the general rule, but concluded that the tax at issue in that case (a statewide property tax levy of one-eighth mill) was not "incidental." That is because the tax was a tax of general statewide application that was not limited to persons directly receiving benefit from facilities or services offered by the Albion Normal School. Several cases predating Dumas hold that the feature that characterizes bills for raising revenue is that such bills raise revenue for the general purpose of government and give no specific benefit in return. *See, e.g.*, Commissioner v. Bailey, 3 Ky. L.R. 110 (1881); U.S. v. Norton, 91 U.S. 566, 568 (1875) (*quoting* Story, J. in U.S. v. Mayo, 26 F. Cas. 1230 (C.C.D. Mass. 1813) (No. 15,755)) (law providing for postal money orders and imposing a fee was not a revenue bill); Northern Counties Invest. Trust v. Sears, 41 P. 931, 935 (Oreg. 1895) (law requiring fees from parties to legal proceeding not a revenue bill). *See also,* Lang v. Commonwealth, 226 S.W. 379, 381 (Ky. 1920) (law requiring county to pay fee for admissions to reformatory not a revenue bill); Kervick v. Bontempo, 150 A.2d 34, 36 (N.J. 1959) (law providing tax to retire state water bond not a revenue bill); Leveridge v. Oklahoma Tax Comm., 294 P.2d 809 (Okla. 1956) (law imposing excise tax on registration of used cars by a dealer was incidental to purpose of registration act and therefore not a revenue bill). This view explains the court's emphasis that:

> [t]his is as truly a tax levied for governmental purposes, as it would be if levied for the construction of a capitol building,

> an insane asylum, or for the support of any department of the state government, ...

Dumas, 35 Idaho at 566, 207 P. at 723.

In practice, the Idaho Legislature follows the rule that a bill that raises revenue only incidentally to its main purpose may originate in the senate. Examples from the 1999 session of the Idaho Legislature include: 1999 Idaho Sess. Laws 431 (S.B. 1029) (increasing the charge for a petition filed against a juvenile found to be within the purview of the Juvenile Corrections Act); 1999 Idaho Sess. Laws 423 (S.B. 1018) (relating to licensure to practice optometry to authorize an increase in the fee for licensure); 1999 Idaho Sess. Laws 427 (S.B. 1020) (increasing the maximum fee for renewal of licensure as a podiatrist).

This practical approach is consistent with Justice Swain's *ipsi dixit* statement in U.S. v. Norton, 91 U.S. at 568, "It is a matter of common knowledge, that the appellative revenue laws is never applied to the statutes involved in these classes of cases." It is also consistent with the Idaho Supreme Court's determination that the worker's compensation death benefit at issue in the Parsons case did not result from a revenue bill. 59 Idaho at 260, 81 P.2d at 1102.

These conflicting ways of understanding Dumas counsel the Idaho Legislature to caution. While it is unlikely that the Idaho court will utterly reject the proposition that bills with only incidental revenue effects (like the senate bills described above) may originate in the senate, Dumas does suggest that the Idaho court may find bills to be revenue bills that would not be so classed by federal courts or courts of other states. Recently, the court has given a similarly strict construction to art. 20, § 2 of the Idaho Constitution prohibiting joining two constitutional amendments in a single ballot question. *See* Idaho Watersheds Project v. State Board of Land Commissioners, 1999 WL 179591 (Idaho April 2, 1999).

E. A Bill Having the Effect of Raising Less Revenue

The only Idaho case addressing the subject seems to favor the minority rule that a bill having the effect of raising less revenue in the future than was raised in the past is still a bill raising revenue and therefore must originate in the house.

In Dumas, the court cited Perry County v. Railroad Co., 58 Ala. 546, 547 (1877), holding that a bill for raising revenue is a bill providing for the levy of taxes as a means of collecting revenue. 35 Idaho at 563, 207 P. at 723. Hence, a bill for reducing taxes, if it provides for collecting revenue, is still a bill for raising revenue. The Alabama court has ruled consistently on this issue in several cases, most recently in Opinion of the Justices, 379 So. 2d 1267 (Ala. 1980).

Since the time of Dumas, only two other states, New Jersey and Oklahoma, have ruled on the issue. They have established rules contrary to the Alabama rule. *See* In Re Paton's Estate, 168 A. 422, 424 (N.J. Eq. 1933) (statute granting an exemption from an inheritance transfer tax for a gift to Princeton University was not a revenue bill); Thompson v. Huston, 39 P.2d 524, 526 (Okla. 1935) (bill reducing penalty on delinquent taxes was not a revenue bill).

Rulings by courts of three states over the course of a century and a quarter are a small basis for determining a majority and minority rule. Several factors recommend following the Alabama rule that bills diminishing revenue must originate in the house. First is the recognition in Dumas that the Alabama rule was a part of the jurisprudential landscape at the time. Another is the deliberate inclination in this analysis to favor introduction of doubtful bills in the house to avoid Origination Clause challenges. Also important is the fact that whether a bill increases or diminishes revenue is itself sometimes a questionable matter.

Advocates of tax benefit proposals (tax exemptions, deductions, credits or refunds) sometimes support the proposal because the benefit will increase, not decrease, revenue. The assumption is that the benefit will act as an economic incentive, stimulating sufficient economic growth to generate enough new tax revenue to more than off-set the direct cost of the benefit. *See, e.g.*, statement of purpose and fiscal note to 1996 Idaho Sess. Laws 1446 (H.B. 873) (relating to expanding eligibility for the income tax credit payable to another state). There is no authority, judicial or otherwise, holding or suggesting that such an effect, if true, does or does not transform a tax benefit proposal into a revenue-raising bill.

F. Property Tax Bills

S.B. 1219 is an example of another problem that adds doubt to the proper resolution of this issue. The bill would expand a property tax exemption. Property tax exemptions do not necessarily result in either an increase or decrease of property tax revenues. The amount of property tax revenue raised by a local taxing district (such as a county or city) is most directly determined by its budget, not by its assessed valuation. *See generally* Idaho Code, ch. 8, title 63. If an exemption decreases the size of the base, then, mathematically, the amount of the levy goes up, generating the same amount of revenue for the district by increasing the tax bill for owners of non-exempt property in the district. The Idaho court observed in both Dumas and Worthen:

> The purpose of incorporating [art. 3, § 14] into the fundamental law is that laws for raising revenue are an exercise of one of the highest prerogatives of government, and confer upon taxing officers authority to take from the subject his property by way of taxation for the public good, a burden to which he assents only because of it being necessary in order to maintain the government, and the people have accordingly reserved the right to determine this necessity by that body of the Legislature which comes most directly from the people, the house of representatives.

Dumas, 35 Idaho at 563, 207 P. at 721; Worthen, 96 Idaho at 178, 525 P.2d at 960.

Since the creation or expansion of a property tax exemption will increase taxes for most property owners, such a bill can be viewed as being within the intent of the Origination Clause.

A property tax exemption may reduce revenue for those districts for which the increased levy exceeds a statutory levy limit. However, such an event is usually unforeseeable at the time a proposed property tax exemption is under consideration by the legislature.

There is an additional complication for property tax related bills. Courts in other states hold that an authorization to levy taxes is not itself a bill to raise revenue. Courts uniformly hold that acts creating incorporated towns or other political subdivisions of the state and granting the right to levy taxes are not acts for raising revenue. *See* Houston County v. Covington, 172 So. 882 (Ala. 1937); Chicago, B. & Q. R. Co. v. School Dist., 165 P. 260 (Colo. 1917); Harper v. Elberton, 23 Ga. 566 (1857); Rankin v. Henderson, 7 S.W. 174 (Ky. 1888); Livingston County v. Dunn, 51 S.W.2d 450 (Ky. 1932); Excelsior Planting & Mfg. Co. v. Green, 1 So. 873 (La. 1887); Evers v. Hudson, 92 P. 462 (Mont. 1907); Dickey v. State, 217 P. 145 (Okla. 1923); Ryan Co. v. State, 228 P. 521 (Okla. 1924); Protest of Chicago, R. I. & P. R. Co., 279 P. 319 (Okla. 1929); Mikell v. Philadelphia School Dist., 58 A.2d 339 (Pa. 1948); Day Land & Cattle Co. v. State, 4 S.W. 865 (Tex. 1887); Gieb v. State, 21 S.W. 190 (Tex. Crim. App. 1893).

Consistent with this idea is that the Idaho Constitution prohibits the legislature from raising revenue for local governments. *See* art. 7, § 6, Idaho Constitution; Leonardson v. Moon, 92 Idaho 796, 800, 451 P.2d 542, 546 (1969). This authority suggests—but does not hold—that bills affecting property tax matters can not be bills raising revenue since the legislature is prohibited from raising property tax revenues for local governments.

Conclusion

For these reasons, we counsel the legislature to adopt practices that remove or at least minimize the possibility that a bill, if enacted, could be successfully challenged on Origination Clause grounds. These practices would give to the term "bills for raising revenue" a broader rather than narrower understanding. They would prefer the introduction of doubtful bills, including bills granting tax benefits, in the house and limit the senate to initiating revenue measures in the form of amendments to revenue bills originating in the house. If bills with incidental revenue raising effects or bills changing the property tax system are introduced in the Senate, it should be with full knowledge of the possible, but not certain, implications under the Origination Clause in the event the enacted statute is judicially challenged.

AUTHORITIES CONSIDERED

1. United States Constitution:

Art. 1, § 7.

2. Idaho Constitution:

Art. 3, § 14.
Art. 7, § 6.
Art. 20, § 2.

3. Idaho Code:

Title 63, chapter 8.
§ 63-3067.

4. Idaho Session Laws:

1921 Idaho Sess. Laws 256 (S.B. 298).
1972 Idaho Sess. Laws 1149 (H.B. 789).
1996 Idaho Sess. Laws 1446 (H.B. 873).
1999 Idaho Sess. Laws 423 (S.B. 1018).
1999 Idaho Sess. Laws 427 (S.B. 1020).
1999 Idaho Sess. Laws 431 (S.B. 1029).

5. Idaho Cases:

Dumas v. Bryan, 35 Idaho 557, 207 P. 720 (1922).

Idaho Watersheds Project v. State Board of Land Commissioners, 1999 WL 179591 (Idaho April 2, 1999).

Leonardson v. Moon, 92 Idaho 796, 451 P.2d 542 (1969).

State ex rel. Parsons v. Workmen's Compensation Exchange, 59 Idaho 256, 81 P.2d 1101 (1938).

Ware v. Idaho State Tax Commission, 98 Idaho 477, 567 P.2d 423 (1977).

Worthen v. State, 96 Idaho 175, 525 P.2d 957 (1974).

6. **Federal Cases:**

Hubbard v. Lowe, 226 F. 135 (1915).

Millard v. Roberts, Treasurer of the United States, 202 U.S. 429 (1906).

Twin City Nat'l Bank v. Nebaler, 167 U.S. 196 (1897).

U.S. v. Mayo, 26 F. Cas. 1230 (C.C.D. Mass. 1813) (No. 15,755).

U.S. v. Munoz-Flores, 495 U.S. 385 (1990).

U.S. v. Norton, 91 U.S. 566 (1875).

7. **Other Cases:**

Chicago, B. & Q. R. Co. v. School Dist., 165 P. 260 (Colo. 1917).

Commissioner v. Bailey, 3 Ky. L.R. 110 (1881).

Day Land & Cattle Co. v. State, 4 S.W. 865 (Tex. 1887).

Dickey v. State, 217 P. 145 (Okla. 1923).

Excelsior Planting & Mfg. Co. v. Green, 1 So. 873 (La. 1887).

Evers v. Hudson, 92 P. 462 (Mont. 1907).

Gieb v. State, 21 S.W. 190 (Tex. Crim. App. 1893).

Harper v. Elberton, 23 Ga. 566 (1857).

Houston County v. Covington, 172 So. 882 (Ala. 1937).

In Re Paton's Estate, 168 A. 422 (N.J. Eq. 1933).

Kervick v. Bontempo, 150 A.2d 34 (N.J. 1959).

Lang v. Commonwealth, 226 S.W. 379 Ky. 1920).

Leveridge v. Oklahoma Tax Comm., 294 P.2d 809 (Okla. 1956).

Livingston County v. Dunn, 51 S.W.2d 450 (Ky. 1932).

Mikell v. Philadelphia School Dist., 58 A.2d 339 (Pa. 1948).

Morgan v. Murray, 328 P.2d 644 (Mont. 1958).

Northern Counties Invest. Trust v. Sears, 41 P. 931 (Oreg. 1895).

Opinion of the Justices, 379 So. 2d 1267 (Ala. 1980).

Perry County v. Railroad Co., 58 Ala. 546 (1877).

Protest of Chicago, R. I. & P. R. Co., 279 P. 319 (Okla. 1929).

Rankin v. Henderson, 7 S.W. 174 (Ky. 1888).

Ryan Co. v. State, 228 P. 521 (Okla. 1924).

Thompson v. Huston, 39 P.2d 524, 526 (Okla. 1935).

8. **Other Authorities:**

The Federalist No. 66 (Alexander Hamilton).

Proceedings, Constitutional Convention, Vol. II, p. 1227.

Story, Commentaries on the Constitution § 880.

T. Jipping, TEFRA and the Origination Clause: Taking the Oath Seriously, 35 Buff. L. Rev. 633 (1986).

Dated this 19th day of July, 1999.

Sincerely,

ALAN G. LANCE
Idaho Attorney General

Analysis by:

Theodore V. Spangler, Jr.
Deputy Attorney General

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1 It is worth noting a case presenting the converse situation. In Hubbard v. Lowe, 226 F. 135 (1915), the court invalidated a federal law because it originated in the senate, contrary to the constitutional provision, even though the revenue feature was added by amendment in the house of representatives.

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ATTORNEY GENERAL'S SELECTED INFORMAL GUIDELINES FOR THE YEAR 1999

ALAN G. LANCE
ATTORNEY GENERAL
STATE OF IDAHO

February 10, 1999

Mr. Paul S. Laggis
Power County Prosecuting Attorney
20 Hillcrest Avenue
P.O. Box 419
American Falls, ID 83211-0419

THIS CORRESPONDENCE IS A LEGAL GUIDELINE OF THE ATTORNEY GENERAL SUBMITTED FOR YOUR GUIDANCE

Re: Zoning Authority Within Fort Hall Reservation

Dear Mr. Laggis:

Your letter requested this office to address the following questions:

(1) Whether Power County has authority to require non-Indians residing on non-Indian fee lands within the Fort Hall Reservation to comply with Power County land use and zoning requirements.

(2) Whether Power County has authority to require non-Indians residing on non-Indian fee lands within the Fort Hall Reservation to obtain county building permits.

ANALYSIS

Unfortunately, it is impossible to answer such questions as a matter of law. Accurate analysis requires an involved investigation and analysis of numerous and complex factual issues, including, among others, the location and extent of the non-Indian lands relative to tribal lands, the history and manner in which such lands entered non-Indian ownership, the history of tribal efforts to control land use within the Fort Hall Reservation, and the impact that application of the zoning ordinances of Power County would have upon application of the zoning ordinances of the Shoshone-Bannock Tribes ("Tribes"). We do, however, offer the following analysis as a framework which may guide you in determining your course of action.

1. Tribal Zoning Ordinances

Your questions require a two-pronged analysis. First, it must be decided whether the Tribes have zoning jurisdiction over non-Indian lands within the Fort Hall Reservation. If they do not, then the county would clearly have jurisdiction. The Supreme Court has "recognized the rights of States, absent a congressional prohibition, to exercise criminal (and, implicitly, civil) jurisdiction over non-Indians located on reservation lands." Yakima County v. Yakima Indian Nation, 112 S. Ct. 683, 688 (1992). If the Tribes are determined to have jurisdiction, however, then the second prong of the analysis is to determine whether the county's jurisdiction is preempted.

The only Supreme Court decision to directly address tribal authority to impose planning and zoning requirements on non-Indian lands is Brendale v. Confederated Tribes and Bands of the Yakima Indian Nation, 492 U.S. 408 (1989). Brendale involved two different sections of the Yakima Reservation; the "open" section, where the majority of lands belonged to non-Indians, and the "closed" section, where the vast majority of lands belonged to the Tribe, who strictly restricted access to the area in order to maintain its pristine character.

A sharply divided opinion upheld tribal zoning authority on the closed section of the reservation, and denied such authority on the open section of the reservation. Four members of the Court would have denied tribal zoning authority on both sections, three members would have upheld such authority on both sections, and the two swing votes held that the authority rested on the relative abundance of Indian and non-Indian lands. The two swing votes opined that when non-Indian parcels comprise only a small percentage of the lands in a particular section of a reservation, the tribe has not lost the ability to "define the character of that area," 492 U.S. at 434, and therefore can impose land-use regulations on non-Indian lands. *Id.* In contrast, where a majority of lands are held in fee by non-Indians, the swing votes concluded that the Tribe "lacks the power to define the essential character of the territory," *id.* at 445, and therefore lacks zoning authority over non-Indian lands.

Because the votes of the Court members in Brendale were so badly split, the case provides little in the way of reliable guidance. At most, it establishes that the relative abundance of Indian and non-Indian lands is a critical factor in determining whether a tribe has zoning authority over non-Indian lands. What level of non-Indian ownership is necessary to relieve tribes of such zoning authority is difficult to say. The "closed" portion of the reservation at issue in Brendale only contained 3.4% non-Indian lands (by comparison, the Fort Hall Reservation contains 4% non-Indian lands). At first glance, the similarity in percentages suggests that the Brendale holding would apply to the Fort Hall Reservation.

It would be a mistake, however, to place too much reliance on raw percentages of Indian and non-Indian lands. The closed portion of the reservation at issue in Brendale was an area retained in a natural state as a forest and hunting preserve, and was also an area where no county services were provided. All roads into the area were maintained by the Bureau of Indian Affairs and, at the time of the suit, closed to the general public. *Id.* at 415. Non-Indians could not even enter the area without a tribal permit. *Id.* In other words, there was a long history of the Tribe's exercising jurisdiction over the "closed" area with the goal of preserving it in its natural state. As the swing votes noted in Brendale, the Tribe had established an "historic and consistent interest in preserving the pristine character of this vast, uninhabited portion of its reservation." *id.*. at 440. Under those unique circumstances, tribal authority over non-Indian lands was essential to the Tribe's ability to retain the unique characteristics of the area.

Whether the Shoshone-Bannock Tribes would be able to prove a similar need for tribal regulation of land uses on the Fort Hall Reservation is a factual question beyond the scope of this analysis. Because the resolution of any zoning dispute would depend heavily on factual issues, we do not suggest that you necessarily accept the holding in Brendale as determinative in future cases.

The future application of the holding in Brendale is uncertain for several reasons. First, since the decision was so badly splintered, with no rationale mustering a majority opinion, it is of questionable precedential value and subject to future reexamination by the Supreme Court. *See* Seminole Tribe of Florida v. Florida, 517 U.S. 44, 63 (1996). Second, Justice Stevens' swing opinion relied, in part, on rationale subsequently rejected by the majority of the Court. Justice Stevens viewed tribal zoning authority as falling within the ambit of tribal jurisdiction over non-Indians as defined in Montana v. United

States, 450 U.S. 544 (1981). Montana held that tribes have been divested of sovereignty over non-Indians, but defined two exceptions to that rule, the first being when non-Indians enter into consensual relations with a tribe, and the second being where non-Indian conduct "threatens or has some direct effect on the political integrity, the economic security, or the health or welfare of the tribe." 450 U.S. at 566.

In Brendale, Stevens invoked the second Montana exception by adopting the finding of the trial court that development in the closed area of the Yakima Reservation "would undoubtedly negatively affect the general health and welfare of the Yakima Nation and its members." 492 U.S. at 443. Subsequent Supreme Court opinions, however, have clarified that effects on the general health and welfare of tribal members are not enough to sustain tribal jurisdiction over non-Indians. In fact, they have warned against the danger that the second Montana exception "can be misperceived," and applied so broadly that "the exception would severely shrink the rule." Strate v. A-1 Contractors, 117 S. Ct. 1404, 1415, 16 (1997).[1] Instead, Strate admonishes that the Montana exceptions must be applied in the context of "what is necessary to protect tribal self-government or to control internal relations." *Id.* at 1416. The kinds of self-governing regulations the Court had in mind are outlined in the preface to the Montana exceptions: "Indian tribes retain their inherent power [to punish tribal offenders,] to determine tribal membership, to regulate domestic relations among members, and to prescribe rules of inheritance for members." *Id.* at 1416, quoting Montana, 450 U.S. at 564.

With the narrowing of the Montana exceptions, future decisions regarding tribal zoning are likely to turn on whether zoning authority over non-Indians is necessary to protect the tribe's sovereign authority to zone and regulate lands owned by the tribe and its members.

2. Preemption of County Zoning Regulations

Generally, state laws may be applied to non-Indians residing within Indian reservations, "unless such application would interfere with reservation self-government or would impair a right granted or reserved by federal law." Mescalero Apache Tribe v. Jones, 411 U.S. 145, 148 (1973). Whether state authority is preempted requires a "particularized inquiry into the nature of the state, federal, and tribal interests at stake." White Mountain Apache Tribe v.

Bracker, 448 U.S. 136, 145 (1980). State jurisdiction is preempted if it "interferes or is incompatible with federal and tribal interests reflected in federal law, unless the state interests at stake are sufficient to justify the assertion of state authority." New Mexico v. Mescalero Apache Tribe, 462 U.S. 324, 334 (1983). In assessing federal and tribal interests, "traditional notions of Indian sovereignty provide a crucial 'backdrop,'" as do federal objectives of promoting tribal self-government. *Id.* The preemption analysis, however, is "informed by historical notions of tribal sovereignty, rather than determined by them." Rice v. Rehner, 463 U.S. 713, 718 (1983).

Unfortunately, the Supreme Court in Brendale did not have the opportunity to apply this preemption analysis to determine whether the county would possess concurrent zoning authority over lands subject to tribal zoning ordinances, since the involved county did not appeal. This leaves only the Ninth Circuit's decision in the same case as guidance. *See generally* Confederated Tribes and Bands of the Yakima Indian Nation v. Whiteside, 828 F.2d 529 (9th Cir. 1987). The Whiteside decision held that county zoning ordinances would be preempted in the face of competing tribal ordinances, especially where the county ordinances allowed uses inconsistent with those allowed by the Tribe's land use plan. *Id.* at 535. The court noted that "[c]omprehensive planning enables a centralized regulatory authority to balance the competing needs of landowners and to distribute land uses in a desirable pattern." 828 F.2d at 534. The court's comments appeared to focus on the concern that competing land use ordinances would defeat the very purpose of zoning, i.e., centralized and comprehensive planning.

This is not to say that a tribal zoning ordinance automatically preempts a county zoning ordinance. In Whiteside, the county ordinance would have allowed the construction of homes, restaurants, bars, and commercial campgrounds in an area zoned by the Tribe as quasi-wilderness. Such obvious conflict led to the conclusion of preemption. In cases where conflict is non-existent or at least less substantial, the possibility exists for concurrent state and tribal regulation. As Justice Stevens noted in Brendale, "overlapping land-use regulations are not inherently suspect," citing as an example federal environmental protections superimposed on county zoning ordinances. 492 U.S. at 440.

Thus, it appears that the question of preemption in the area of zoning law may well depend on existence of an actual conflict between tribal and local zoning regulations. Strate, Rice, and other cases demonstrate that the central question in any future zoning case is whether application of county zoning regulations to non-Indian lands impacts the tribe's right to regulate uses of tribally-owned lands. Where there is no conflict between county and tribal zoning laws, the possibility exists that both sets of zoning ordinances could be applied to non-Indian lands. Where conflict exists, the outcome will likely depend on the impact that land uses allowed by the county ordinance have on the tribe's ability to regulate uses of Indian lands in the same area, especially in areas where tribal lands are predominant.

3. Building Permits

Much of the above analysis applies equally to building permits. Where a tribe lacks zoning authority over non-Indian lands, there is no barrier to requiring county building permits for construction on non-Indian lands within an Indian reservation. In those instances where tribal zoning laws apply to non-Indian lands, a county building permit may be preempted if the permitted use is inconsistent with the tribal ordinance. The circumstances of preemption would be nearly identical to those discussed above. If the use allowed by a county building permit is consistent with the tribal zoning ordinance, there should be no barrier to requiring a county building permit. In such instances, there may be an increased burden on the landowner, but no threat to tribal self-government.

CONCLUSION

Power County possesses the general authority to require non-Indians residing on non-Indian fee lands within the Fort Hall Reservation to obtain county building permits and comply with county land use requirements. Whether such authority is preempted in specific circumstances is a factual question, largely dependent on (1) the relative abundance of non-Indian property in that portion of the reservation that lies within Power County, (2) the nature of the lands and the history of tribal control over the "character" of that portion of the reservation and (3) whether the uses permitted by the county would substantially conflict with uses permitted by the Tribes on surrounding tribal lands, or otherwise negatively affect the Tribes' ability to control the use of tribally-owned lands.

Sincerely,

Steven W. Strack
Deputy Attorney General

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1 The Ninth Circuit Court of Appeals has also warned against broad application of the second Montana exception, noting that "the exception would swallow the rule because virtually every act that occurs on the reservation could be argued to have some political, economic, health or welfare ramification to the tribe." County of Lewis v. Allen, 163 F.3d 509, 515 (9th Cir. 1998).

May 5, 1999

Mr. Don Fortney
Sheriff of Lewis County
P.O. Box 206
Nezperce, ID 83543

THIS CORRESPONDENCE IS A LEGAL GUIDELINE OF THE ATTORNEY GENERAL SUBMITTED FOR YOUR GUIDANCE

Dear Sheriff Fortney:

You have asked the Attorney General's Office to provide legal guidance regarding the effect of the recent action of the Nez Perce Tribal Executive Committee in rescinding NP 65-126, the tribe's assent to jurisdiction of the State of Idaho over the crimes enumerated therein. Specifically, you asked:

> Does the Nez Perce Tribal Government's unilateral rescission of their prior consent to concurrent jurisdiction affect the state's jurisdiction over the civil and criminal matters set forth in Idaho Code § 67-5101 . . .?
>
> Does the Nez Perce Tribal Government's unilateral rescission of their prior consent to concurrent jurisdiction affect the state's jurisdiction over matters set forth in Idaho Code § 67-5102 and enumerated in NP 65-126 . . .?

Our conclusion is that, by rescinding NP 65-126, the tribe has effectively revoked its consent to state jurisdiction over the enumerated offenses and has, thus, deprived the state of jurisdiction over those offenses. Our further conclusion, however, is that the state retains jurisdiction over the matters listed in I.C. § 67-5101.

ANALYSIS

A. Jurisdiction in Indian Country

Indian country is defined in 18 U.S.C. § 1151 as, among other things, "all land within the limits of any Indian reservation under the jurisdiction of the United States Government notwithstanding the issuance of any patent, and, including rights-of-way running through the reservation."[1] "When addressing the question of state jurisdiction in Indian country, we are guided by the canon of construction that federal and state 'statutes passed for the benefit of Indians are to be construed in the Indians' favor.'" State v. Major, 111 Idaho 410, 415, 725 P.2d 115, 120 (1986) (citations omitted).

The states have no jurisdiction over Indians in Indian country without congressional consent. McClanahan v. State Tax Commission of Arizona, 411 U.S. 164, 170-71, 93 S. Ct. 1257, 1261, 36 L. Ed. 2d 129 (1973).

Generally, jurisdiction in Indian country is determined by both the status of the parties involved and the nature of the crime. For instance, intra-Indian crimes were exempted from the federal jurisdiction of the General Crimes Act of 18 U.S.C. § 1152, but that section was limited by the subsequent enactment of the Major Crimes Act, 18 U.S.C. § 1153, which provided for federal jurisdiction over 14 enumerated crimes. Thus, jurisdiction over crimes by Indians against Indians is in tribal court unless the crime is one enumerated in the Major Crimes Act. Proper jurisdiction for crimes committed between non-Indians in Indian country is in state court. U.S. v. McBratney, 104 U.S. 621 (1881) (the "McBratney Rule"). Jurisdiction for crimes committed by non-Indians against Indians on Indian land is federal court. *See* Duro v. Reina, 495 U.S. 676, 110 S. Ct. 2053, 109 L. Ed. 2d 693 (1990); State v. Verdugo, 901 P.2d 1165 (Ariz. Ct. App. 1995); see generally 18 U.S.C. §§ 1152, 1153; Cohen's Handbook of Federal Indian Law (1982 ed.). The Idaho Supreme Court has held that the Idaho state courts have jurisdiction over "victimless" crimes, such as DUI, committed by non-Indians on the reservation. State v. Snyder, 119 Idaho 376, 807 P.2d 55 (1991); *see also* State v. Warden, 127 Idaho 763, 906 P.2d 133 (1995).

Public Law 280 is an exception to the general jurisdictional framework in Indian country. *See, generally*, Clinton, *Criminal Jurisdiction Over*

Indian Lands: A Journey Through a Jurisdictional Maze, 18 Ariz. L. Rev. 503, 504 (1976). In Public Law 280, Congress gave Idaho and other states the "consent of the United States" to assume jurisdiction over criminal and civil matters "at such time and in such manner as the people of the State shall, by affirmative legislative action, obligate and bind the State to assumption thereof." Public Law No. 280, § 7, 67 Stat. 588, 590 (1953). When Public Law 280 was enacted, the states were not required to obtain consent of the tribes before asserting state jurisdiction.

In 1963, pursuant to Public Law 280, Idaho enacted I.C. § 67-5101, assuming jurisdiction over the following matters:

A. Compulsory school attendance
B. Juvenile delinquency
C. Dependent, neglected and abused children
D. Public Assistance
F. Domestic Relations
G. Operations and management of motor vehicles upon highways and roads maintained by the county or state, or political subdivisions thereof.

Idaho also enacted a statute allowing the individual tribes to extend to the state further concurrent jurisdiction. I.C. § 67-5102 (1963). In addressing that statute, the courts have referred to "what, in effect, is a bilateral agreement between the State of Idaho and the [tribe] to confer jurisdiction to the state courts." Boyer v. Shoshone-Bannock Indian Tribes, 92 Idaho 257, 262, 441 P.2d 167, 171(1968).

On April 13, 1965, the Nez Perce passed NP 65-126, consenting to concurrent state court jurisdiction over enumerated offenses including disturbing the peace, contributing to the delinquency of minors, simple assault, battery and receiving stolen property. Tribal Resolution 65-126, quoted in State v. Major, 111 Idaho 410, 418, 725 P.2d 115, 123 (1986); State v. Marek, 112 Idaho 860, 869, 736 P.2d 1314, 1323(1987). Thereby, the tribe and the State of Idaho entered into a compact extending state jurisdiction to the enumerated offenses.

In 1968, Congress passed the Indian Civil Rights Act, 25 U.S.C. § 1321(a) (1983), which amended Public law 280 to require formal tribal consent to the further assumption of jurisdiction by the states. The Act repealed § 7 of Public Law 280, but specifically did not "affect any cession of jurisdiction made pursuant to such section prior to repeal." In State v. McCormack, 117 Idaho 1009, 1012, 793 P.2d 682, 685 (1990), the court noted that the limiting language of § 1321 "does not require further tribal consent . . . because that jurisdiction [in I.C. § 67-5101] had been granted and assumed prior to enactment of § 1321." See also State v. Michael, 111 Idaho 930, 932, 729 P.2d 405, 406 (1986) (". . . those areas over which the state had assumed jurisdiction in 1963 remain under state jurisdiction").

Thus, until recently, it was clear that the state courts of Idaho had jurisdiction over both the matters set forth in I.C. § 67-5101 and the offenses listed in NP 65-126.

B. Recent Action by the Nez Perce Tribe

On March 9, 1999, the Nez Perce Tribal Executive Committee (NPTEC) rescinded NP 65-126. In a subsequent letter to local law enforcement, the Tribal Chairman indicated two bases for the tribe's action. First, the tribe felt that the need for state jurisdiction over crimes committed on the reservation had been nullified by the establishment and training of the tribal police force. Second, the tribe considered it "essential to the sovereignty of the Nez Perce Tribe that the law enforcement jurisdiction transferred by NP 65-126 be returned to the exclusive control of the Tribe." The letter apparently referred to the decision of the Ninth Circuit Court of Appeals in County of Lewis v. Allen, 163 F.3d 509 (9th Cir. 1998). In that case, the court held that the tribe's compact with the state to extend state jurisdiction to the offenses enumerated in NP 65-126 "was tantamount to alienation of the land to non-Indians for this limited purpose." *Id.*, at 514. The tribe provided notice of its action to local law enforcement.

C. The Current Status of Idaho State Court Jurisdiction in Indian Country

1. I.C. § 67-5101

The validity of I.C. § 67-5101 was not affected by the enactment of the Indian Civil Rights Act and is not subject to assent by the tribes. Therefore, the areas over which the state assumed jurisdiction in I.C. § 67-5101 remain under state jurisdiction.

2. The Minor Offenses Enumerated in NP 65-126

I.C. § 67-5102 provides that "[a]dditional state jurisdiction . . . may be extended to particular reservations or Indian country with the consent of the governing body of the tribe . . .." It is clear that the Nez Perce Tribe has now revoked its consent to state jurisdiction over the minor offenses enumerated in NP 65-126. When the compact between the tribe and the state was originally entered into pursuant to I.C. § 67-5102, the additional jurisdiction became effective when the tribe forwarded the resolution to the Office of the Attorney General. When NPTEC revoked jurisdiction over crimes set forth in NP 65-126, however, it did so in a unilateral manner. It later provided notice to local law enforcement agencies, which notice was forwarded to the Office of the Attorney General. The issue arises whether this unilateral action on the part of the tribe was an effective revocation of consent to additional state jurisdiction. We conclude that it was.

The statute provides that additional jurisdiction may be effected by "negotiation with the tribe or by unilateral action by the tribe." Thus, although the tribe must eventually provide notice, the tribe is free to extend additional jurisdiction as it sees fit. There does not appear to be any authority for the proposition that the tribe was required to follow this same procedure in order to effectively revoke its consent to the additional state jurisdiction. Rather, it appears that the key is tribal consent, without which the state may not exercise additional jurisdiction.

CONCLUSION

It is the conclusion of this office that NPTEC's action in rescinding NP 65-126 effectively deprived the state courts of Idaho of jurisdiction over the offenses set forth in that ordinance, but did not have any effect on the jurisdiction of the Idaho courts over the matters listed in I.C. § 67-5101. Further, the state courts retain jurisdiction over matters unrelated to Public Law 280, such as crimes between non-Indians that may occur on the reservation and victimless crimes, such as DUI, committed in Indian country by non-Indians.

Sincerely,

Alison A. Stieglitz
Deputy Attorney General
Criminal Appellate Unit

1 There currently is a dispute about whether the Nez Perce Reservation includes lands ceded pursuant to the Agreement of May 1, 1893, 28 Stat. 326. The state has taken the position that the reservation does not include such lands, while the tribe has taken the position that it does. Obviously, the outcome of the dispute will determine what lands constitute "Indian country" as defined in 18 U.S.C. § 1151.

May 20, 1999

Senator Grant R. Ipsen
Idaho State Senate
1010 Houston Road
Boise, ID 83706

THIS CORRESPONDENCE IS A LEGAL GUIDELINE OF THE ATTORNEY GENERAL SUBMITTED FOR YOUR GUIDANCE

Dear Senator Ipsen:

You have asked the Attorney General's Office to provide legal guidance regarding the workers' compensation law in the state as it specifically pertains to non-profits and, more specifically, to faith groups. The more specific questions are listed below.

QUESTIONS PRESENTED

1. Is workers' compensation insurance required for "small" non-profits, more specifically, faith groups?

2. If so, is the communication of such clearly stipulated under the law?

3. Is the minimum premium and penalty assessed these small organizations reasonable in light of the fact that the minimum premium charged is often a large percentage of the compensation paid?

CONCLUSION

1. Yes. Pursuant to Idaho Code § 72-203, the workers' compensation law applies to all public employment and private employment not expressly exempted by the provisions of Idaho Code § 72-212.

2. Yes, the requirement for workers' compensation insurance is set forth in Idaho Code § 72-301 with exemptions to that requirement set forth in Idaho Code § 72-212. There is Idaho case law interpreting the exemptions provided in Idaho Code § 72-212.

3. The penalty for failure to secure compensation is statutorily set by Idaho Code § 72-319. The minimum premium is confined to a range by Idaho Code § 41-1612(2), which states that "no filing shall contain a minimum premium that is less than one hundred fifty dollars ($150) or greater than three hundred dollars ($300)."

ANALYSIS

Question Number 1:

Idaho Code § 72-203 provides that all public and private employment is covered by the workers' compensation law, and coverage is required unless expressly exempt by the provisions of Idaho Code § 72-212. The exemptions from coverage, under Idaho Code § 72-212, that may be applicable to "small" non-profits, more specifically, faith groups, are set forth as follows:

> **72-212. Exemptions from coverage.**—None of the provisions of this law shall apply to the following employments unless coverage thereof is elected as provided in section 72-213, Idaho Code.
>
> . . . .
>
> (2) Casual employment.
>
> . . . .
>
> (6) Employment which is not carried on by the employer for the sake of pecuniary gain.

As is set forth in this analysis, Idaho case law does not support the application of the above quoted exemptions in the case of faith groups.

The Supreme Court of Idaho has defined "casual employment" as found in Idaho Code § 72-212(2) as follows:

> This Court has defined "casual employment" as employment that is only occasional, or comes at uncertain times, or at irregular intervals, and whose happening cannot be reasonably anticipated as certain or likely to occur or to

> become necessary. It is employment that arises only occasionally or incidentally and is not part of the usual trade or business of the employer. *Tuma v. Kosterman*, 106 Idaho 728, 682 P.2d 1275 (1984); *Wachtler v. Calnon*, 90 Idaho 468, 413 P.2d 449 (1966); *Flynn v. Carson*, 42 Idaho 141, 243 P. 818 (1926).

Larson v. Bonneville Pacific Services Co., 117 Idaho 988, 989-90, 723 P.2d 220, 221-22 (1990).

It does not appear that typical employees of a small faith group would meet the casual employment exception as interpreted by Idaho case law. My understanding is that the employees of a small faith group, that is the focus of this analysis, would consist of a pastor and secretaries conducting the usual business of the faith group.

The "pecuniary gain" exemption provided under Idaho Code § 72-212(5) was recently interpreted by the Supreme Court of Idaho in Burrow v. Caldwell Treasure Valley Rodeo, 129 Idaho 675, 931 P.2d 1193 (1997). Don Burrow was employed by the Caldwell Treasure Valley Rodeo to do various maintenance jobs. When Mr. Burrow was injured in the course of installing a scoreboard, he sought workers' compensation benefits. Caldwell Treasure Valley Rodeo asserted that it was an exempt employer under Idaho Code § 72-212(5). Caldwell Treasure Valley Rodeo, the employer, was described in the decision as follows:

> For federal tax purposes, the employer is a non-profit, tax-exempt organization under 26 U.S.C. § 501(c)(4). The employer does not fall within the definition of non-profit organization for purposes of the collection of state sales tax. The employer reinvests its proceeds back into the rodeo grounds it operates, and the members of its board of directors are volunteers.

Id. at 676.

The supreme court held that the employer was not exempt under Idaho Code § 72-212(5). It reasoned as follows:

The Commission determined that the employer is not exempt under the I.C. § 72-212(5) exemption because it receives remuneration for its services in the form of admissions to the rodeos it conducts. The Commission based its decision on *Modlin*, 49 Idaho 199, 286P. 612. In *Modlin*, the employer was a for-profit employer, and attempted to avoid workers' compensation liability on the basis that it did not generate any profit in the particular instance in which the employee was injured. *Id.* In *Modlin*, the employer argued that it was not acting for pecuniary gain. *Id.* at 206, 286 P. at 614. The Court rejected this contention, stating, "[w]hether it made a profit or not is beside the issue. It was supplying service and receiving remuneration for it." *Id.*

The Court has cited *Modlin* for the proposition that "an employer cannot escape liability for compensation on the ground that he is not engaged in a business for pecuniary gain because on some transactions he loses money." *Dillard v. Jones*, 58 Idaho 273, 279, 72 P.2d 705, 708 (1937); see also *Dameron v. Yellowstone Trail Garage, Inc.*, 54 Idaho 646, 652, 34 P.2d 417, 419 (1934) ("Whether or not the employer was making a profit at the time the employee was injured is immaterial.") Therefore, the employer's non-profit tax status is irrelevant to the determination of whether the employment was carried on by the employer for the sake of pecuniary gain.

More recently, this Court addressed the I.C. § 72-212(5) exemption in *Dewey v. Merrill*, 124 Idaho 201, 858 P.2d 740 (1993), stating that "[i]n addressing the issue of pecuniary gain, the Court considers whether a party is supplying a service and receiving remuneration for it." *Id.* at 205, 858 P.2d at 744. The Court also stated in *Dewey* that the "Worker's Compensation Act was intended for commercial and governmental employers who can spread the costs of compensation through the price of goods and services. The pecuniary gain exemption was created to protect individuals . . . who may be deemed to be statutory employers but do not regularly employ others for business purposes." *Id.*

The employer in the present case received remuneration for its services. Therefore, the employer is not exempt under I.C. § 72-212(5).

Id. at 676-77 (citations omitted).

Applying the Burrow holding, a small faith group is not exempt under the Idaho Code § 72-212(5) exemption because it receives remuneration for its services in the form of donations for the religious services it conducts. "[T]he employer's non-profit tax status is irrelevant to the determination of whether the employment was carried on by the employer for the sake of pecuniary gain." Burrow, 125 Idaho at 676.

Question Number 2:

Please see analysis for Question Number 1.

Question Number 3:

The penalty for failure to secure compensation is set forth in Idaho Code § 72-319, which provides in pertinent part, as follows:

> 72-319. Penalty for failure to secure compensation.— . . . .
>
> (4) Any employer required to secure the payment of compensation under this law, who fails to do so, may be liable for a penalty of either two dollars ($2.00) for each employee for each day or twenty-five dollars ($25.00) for each day during which such failure continues, whichever is greater. . . . In determining whether penalties should be assessed or collected for the employer's failure to secure the payment of compensation, the commission may consider the following factors:
>
> (a) When the employer was notified that such employer's worker's compensation insurance coverage had been cancelled or that such insurance was required;

> (b) The length of time that elapsed between when the employer was notified that worker's compensation insurance coverage was required or that such employer's coverage had been cancelled, and the date that such coverage was put into effect;
>
> (c) Whether the employer is able to document attempts to secure worker's compensation insurance coverage during the period of time that such employer was without such coverage;
>
> (d) Whether there were prior instances in which the employer failed to keep worker's compensation insurance in effect or such coverage was cancelled, and the reasons for such failure or cancellation;
>
> (e) The reasons that the employer is unable to obtain or keep in effect worker's compensation insurance coverage;
>
> The above factors are not exclusive and the commission may consider any other relevant factor.

The Idaho Industrial Commission is given discretion on assessing penalties.

Workers' compensation rates are regulated pursuant to title 41, chapter 16, Idaho Code. Idaho Code § 41-1612 provides in pertinent part as follows:

> 41-1612. Adherence to filings.
>
> . . . .
>
> (2) No filing shall contain a minimum premium that is less than one hundred fifty dollars ($150) or greater than three hundred dollars ($300).

Every insurer writing workers' compensation coverage in Idaho files its rates with the Director of the Idaho Department of Insurance. Idaho Code § 41-

1606. Every insurer, including the Idaho State Insurance Fund, writing workers' compensation insurance in Idaho shall be a member of a workers' compensation rating organization. Idaho Code § 41-1615. The workers' compensation rating organization currently operating in Idaho is NCCI.

CONCLUSION

All public and private employers are required to carry workers' compensation insurance unless they are expressly exempt pursuant to Idaho Code § 72-212. Absent some unique situation that places the employer within one of the exemptions provided by Idaho Code § 72-212, a small faith group would be required to carry workers' compensation insurance. The penalty for failure to secure compensation is provided by Idaho Code § 72-319, which gives the Industrial Commission discretion in assessing penalties. Idaho Code § 41-1612 provides that a minimum premium must be within the range of one hundred fifty dollars to three hundred dollars. The filing and approval of workers' compensation rates is under the authority of the Department of Insurance pursuant to title 41, chapter 16, Idaho Code.

Sincerely,

Scott B. Muir
Deputy Attorney General

July 1, 1999

Representative Roger W. Chase
District 33, Bannock County
4985 Clearview Avenue
Pocatello, ID 83201

THIS CORRESPONDENCE IS A LEGAL GUIDELINE OF THE ATTORNEY GENERAL SUBMITTED FOR YOUR GUIDANCE

Dear Representative Chase:

You have asked the Attorney General's Office to provide legal guidance regarding the propriety of a real property transaction between the Bannock County School District and the Katsilometes family. Specifically, you have asked us to examine the provisions of the School Property Act ("Act"), Idaho Code §§ 33-601 to 33-603, and examine what the Act requires when a school district wishes to purchase or convey real property. You asked (1) whether a school district must give public notice of the real property it wished to purchase, and once it gave such notice whether the district was obligated to purchase that parcel of land without any alteration of land boundaries; and (2) whether a school district, once it has an ownership interest in real property, can convey real property without receiving consideration or other value for the land and without public notice or an appraisal?

Concerning the other questions that you submitted to our office for review, they appear to be factual in nature, and do not involve legal issues relating to the School Property Act. For that reason, our office respectfully declines to answer those factual issues, and limits its response to the legal issues outlined above.

ANALYSIS

1. Once a school district gives public notice of real property it wishes to purchase, is it statutorily obligated to purchase the parcel of land without alteration to the parcel's boundaries?

Idaho Code § 33-601 regulates the acquisition, use or disposal of real and personal property by a school district. The statute empowers the board of trustees of each school district to "contract for the construction, repair, or improvement of any real property, or the acquisition, purchase or repair of any equipment, or other personal property necessary for the operation of the school district." Idaho Code § 33-601(2). However, the board of trustees shall not enter into any contract "which entails the expenditure of Fifteen Thousand Dollars ($15,000) or more without notice first being given by publishing twice in the manner required by subsections (g) and (h) of Section 33-402, Idaho Code. . . . The board of trustees may let the contract to the lowest responsible bidder, or reject any bid, or reject all bids and publish notice for bids as before." Idaho Code § 33-601(2).

Thus, it appears clear from the statute that the board of trustees may enter into contracts for the construction, repair or improvement of real property,i or the acquisition of equipment or other personal property necessary for the school district's operation. However, it is important to note that the public notice requirements of Idaho Code § 33-601(2) appear to apply only when the board of trustees is contracting for the construction, repair, or improvement of real property, not the purchase or conveyance of real property. Accordingly, it does not appear that the board of trustees is required to give public notice of any land purchase, even if the purchase price is greater than $15,000.

It appears that the section of the statute applicable to the purchase of real property is subsection (3) of Idaho Code § 33-601. The statute provides that the board of trustees may:

> designate and purchase any real property necessary for school purposes or in the operation of the district, <u>the provisions of subsection (2) of this section notwithstanding</u>, or remove any building, or dispose of any real property. The board of trustees shall determine the size of the site necessary for school purposes. The site shall be located within the incorporated limits of any city within the district; provided, however, that if the board finds that it is not in the best interest of the electors and the students of the district to locate the site within the incorporated limits of a city, the board, by duly adopted resolution setting forth the reasons for its findings, may designate a site located elsewhere within the district. In

> elementary school districts, except upon removal for highway purposes, a site may be designated or changed only after approval of two-thirds (2/3) or more of the electors voting at the annual meeting.

Idaho Code § 33-601(3) (emphasis added).

It appears from subsection (3) that the board of trustees may designate and purchase any parcel of land necessary for school purposes, notwithstanding the notice requirements of subsection (2) discussed above. Accordingly, when determining whether to purchase land, the statute appears to exempt the board of trustees from the public notice and election provisions of subsection (2). It follows, therefore, that the board of trustees, even if they gave the public notice of the boundaries of the designated parcel of land, could change the designated parcel to any parcel of its choosing, because the public notice provisions are not applicable in the first instance.

2. Once a school district has an ownership interest in land, can it convey the land without receiving consideration, without public notice of the conveyance, and without an appraisal?

Your second question did not concern the purchase of real property, but, rather, a conveyance or transfer of real property. It would thus appear that Idaho Code § 33-601(4) governs such a transaction. That code section provides that the board of trustees may:

> convey, except as provided by (b) of this subsection, by deed, bill of sale, or other appropriate instrument, all of the estate and interest of the district in any property, real or personal. . . . Prior to such sale or conveyance, the board shall have the property appraised by three (3) disinterested residents of the district, which appraisal shall be entered in the records of the board of trustees. The property may be sold at public auction or by sealed bids, as the board of trustees shall determine, to the highest bidder. Such property may be sold for cash or for such terms and conditions as the board of trustees shall determine for a period not exceeding ten (10) years with the annual rate of interest on all deferred payments not less than seven

> percent (7%) per annum. . . . Notice of the time and the commissions of such sale shall be published twice, and proof thereof made, in accordance with subsections (g) and (h) of Section 33-402, Idaho Code, except that when the appraised value of the property is less than Five Hundred Dollars ($500), one (1) single notice by publication shall be sufficient and the property shall be sold by sealed bids.
>
> The board of trustees may accept the highest bid, may reject any bid, or reject all bids. If the property was donated to the school district the board may, within a period of one (1) year from the time of the appraisal, sell the property without additional advertising or bidding. Otherwise, the board of trustees may have new appraisals made and again publish notice for bids, as before. If, thereafter, no satisfactory bid is made and received, the board may proceed under its own direction to sell and convey the property. In no case shall any real property of the school district be sold for less than its appraisal.

Idaho Code § 33-601(4)(a).

It appears that the board of trustees may only sell land in which it has an ownership interest pursuant to the provisions of Idaho Code § 33-601(4)(a). The statute requires that the board of trustees must, prior to a sale or transfer of property, have the property appraised by three disinterested residents, and then determine whether to sell the property to the highest bidder. The board of trustees would also have to give public notice of the sale and the terms of the sale. If the real property was donated to the school district, the board has a period of one year from the time the appraisals were done to sell the property without any additional advertising or bidding. The board may not in any event sell the real property for less than its appraised value.

However, the statute does not appear to require the board of trustees to actually conduct a sale of the property. Arguably, the board could convey or exchange the property in another manner pursuant to Idaho Code § 33-601(4)(b). That subsection authorizes the board of trustees to exchange real property:

> for other property if the consideration received by said school district shall be deemed adequate by the board of trustees, provided, however, that aside from the provisions of this paragraph hereof, any school district may by a vote of one-half (1/2) plus one (1) of the members of the full board of trustees, by resolution duly adopted, authorize the transfer or conveyance of any real or personal property owned by such school district to the government of the United States, any city, county, the state of Idaho, any hospital district organized under chapter 13, title 39, Idaho Code, any other school district, any library district, any community college district, or any recreation district, with or without any consideration accruing to the school district, when in the judgment of the board of trustees it is for the interest of such school district that said transfer or conveyance be made.

Idaho Code § 33-601(4)(b).

According to subsection (4)(b) of Idaho Code § 33-601, the school district may exchange land for other property or consideration, and does not have to sell property it owns. An exchange may be undertaken as long as the board of trustees deems the consideration received to be adequate. It would appear from this statute that the board of trustees may only exchange land without receiving any consideration or value in return when it is conveying real property to any of the listed governmental entities in Idaho Code § 33-601(4)(b).

CONCLUSION

It is the conclusion of this office that the only way a school district may convey or transfer real property in which it holds an ownership interest is by following the provisions of Idaho Code § 33-601(4). If the board of trustees wished to sell the property, Idaho Code § 33-601(4)(a) would require the board to (1) have the property appraised by three disinterested residents; (2) determine whether to sell the land at public auction or via sealed bids; (3) and determine whether to sell to the highest bidder. The date of any such sale and the terms of a sale must be published. The board is prohibited from selling real property it owns for less than its appraised value. If the board of trustees wanted to exchange property in a transaction with a private citizen as opposed to a statutorily designated governmental entity, pursuant to Idaho Code § 33-601(4)(b) the board must receive value for the land exchanged and make a determination that the value received was adequate.

If the district desired to purchase land, it appears that the board of trustees is exempt from the public notice provisions of Idaho Code § 33-601(2) and could purchase any parcel of land it designated as necessary for school purposes. Idaho Code § 33-601(3). It does not appear that there are any sanctions or other remedies provided for a violation of Idaho Code § 33-601.

Sincerely,

Kirsten L. Wallace
Deputy Attorney General

1 Real property refers to real estate or land, whereas personal property can refer to anything other than land.

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and

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ATTORNEY GENERAL'S CERTIFICATES OF REVIEW FOR THE YEAR 1999

ALAN G. LANCE
ATTORNEY GENERAL
STATE OF IDAHO

February 25, 1999

The Honorable Pete T. Cenarrusa
Secretary of State
HAND DELIVERED

Re: Certificate of Review
Initiative Regarding Amendment to Title 44, Chapter 10, Idaho Code

Dear Mr. Cenarrusa:

An initiative petition was filed with your office on February 19, 1999. Pursuant to Idaho Code § 34-1809, this office has reviewed the petition and has prepared the following advisory comments. It must be stressed that, given the strict statutory time frame in which this office must respond and the complexity of the legal issues raised in this petition, this office's review can only isolate areas of concern and cannot provide in-depth analysis of each issue that may present problems. Further, under the review statute, the Attorney General's recommendations are "advisory only," and the petitioners are free to "accept or reject them in whole or in part."

BALLOT TITLE

Following the filing of the proposed initiative, our office will prepare short and long ballot titles. The ballot titles should impartially and succinctly state the purpose of the measure without being argumentative and without creating prejudice for or against the measure. While our office prepares the titles, if petitioners would like to propose language with these standards in mind, we would recommend that they do so and their proposed language will be considered.

MATTERS OF SUBSTANTIVE IMPORT

The proposed initiative would create a new code section, Idaho Code § 44-1006, that states:

44-1006. Determining prevailing wages as paid in county seat of county in which work is being performed.—The advertised specifications for every contract let by the State of Idaho and/or any county, city, school district, or other political subdivision of the state for construction, repair and maintenance work on public buildings or public works projects, which involves the employment of mechanics and/or laborers, shall contain a provision stating the minimum wage rates and fringe benefits to be paid various classes of laborers and mechanics in the performance of the contract. It shall be the responsibility of the director of the department of labor and industrial services to determine the prevailing wage rates and fringe benefits in accordance with rates compiled by and on file with the Davis-Bacon Section of the United States Department of Labor by the following procedure:

(a) In all counties in which wage rates and fringe benefits have been compiled by the United States Department of Labor in accordance with the Davis-Bacon Act, such rates and fringe benefits shall be deemed to be the prevailing rates in the county seat of the county in which the work is to be performed.

(b) In all other instances the director of the department shall make a determination after an actual survey of wages and fringe benefits being paid at or near the site of the work. Such determination shall be deemed to be the prevailing rates in the county seat of the county in which the work is to be performed.

The identical language that is proposed by the initiative was enacted by the Idaho legislature in 1955, 1965 and 1974 as Idaho Code § 44-1006.

See 1955 Idaho Session Laws 77-78; 1965 Idaho Session Laws 456 (adding "fringe benefits"); 1974 Idaho Session Laws 1056 (changing "state commissioner of labor" to "director of the department of labor and industrial services"). In 1985, the legislature repealed Idaho Code § 44-1006. 1985 Idaho Session Laws 8. Therefore, the proposed initiative is simply an attempt to resurrect previously repealed statutory language.

One statutory change that has occurred since 1985 affects the language in the proposed initiative. Idaho Code § 67-2402 has changed the name of the "Idaho Department of Labor and Industrial Services" to the "Idaho Department of Labor." The petitioners should probably change the designation of the agency in the proposed language to reflect its current name.

I HEREBY CERTIFY that the enclosed measure has been reviewed for form, style and matters of substantive import and that the recommendations set forth above have been communicated to petitioner Daniel R. Obray by deposit in the U.S. Mail of a copy of this certificate of review.

Sincerely,

ALAN G. LANCE
Attorney General

Analysis by:

Matthew J. McKeown
Deputy Attorney General

March 31, 1999

The Honorable Pete T. Cenarrusa
Secretary of State
HAND DELIVERED

Re: Certificate of Review
Initiative Regarding Election of Fish and Game Commissioners

Dear Mr. Cenarrusa:

An initiative petition was filed with your office on March 19, 1999. Pursuant to Idaho Code § 34-1809, this office has reviewed the petition and has prepared the following advisory comments. It must be stressed that, given the strict statutory timeframe in which this office must respond and the complexity of the legal issues raised in this petition, our review can only isolate areas of concern and cannot provide in-depth analysis of each issue that may present problems. Further, under the review statute, the Attorney General's recommendations are "advisory only," and the petitioners are free to "accept or reject them in whole or in part."

BALLOT TITLE

Following the filing of the proposed initiative, our office will prepare short and long ballot titles. The ballot titles should impartially and succinctly state the purpose of the measure without being argumentative and without creating prejudice for or against the measure. While our office prepares the titles, if petitioners would like to propose language with these standards in mind, we would recommend that they do so and their proposed language will be considered.

MATTERS OF SUBSTANTIVE IMPORT

The proposed initiative purports to amend Idaho Code §§ 36-102(b) through (e) to change the way fish and game commissioners are selected. Currently, there are seven fish and game commissioners. Idaho Code § 36-

102(b). Each of these commissioners represents an individual district. Idaho Code § 36-102(c). Idaho Code § 36-102(c) establishes the term that each commissioner serves. If the proposed initiative were enacted into law, there would be four fish and game commissioners, two elected at large from each congressional district. The only people eligible to vote in fish and game commissioner elections would be those electors who also possess a valid hunting or fishing license.

As an initial matter, the initiative should be formatted to clearly indicate how it is supposed to amend the current language of Idaho Code § 36-102. Instead of stating that the language of Idaho Code § 36-102 should be "modified," the initiative should specifically repeal Idaho Code §§ 36-102(b) through (d) and replace the repealed language with the language in the initiative. Also, the initiative should not state that the current language contained in Idaho Code § 36-102(e) is "modified" by the initiative when the version of Idaho Code § 36-102(e) found in the initiative is identical to the existing language in section 36-102(e).

Next, the proposed initiative reduces the number of fish and game commissioners from seven (7) to four (4). While this change does not raise any legal issue, the petitioner may wish to consider retaining an odd number of commissioners to eliminate the possibility of tie votes.

Third, the initiative's limitation on those who may vote for fish and game commission positions poses a serious constitutional concern. The Twenty-Fourth Amendment to the United States Constitution states:

> The right of citizens of the United States to vote in any primary or other election for President or Vice President, for electors for President or Vice President, or for Senator or Representative in Congress, shall not be denied or abridged by the United States or any State by reason of failure to pay any poll tax or other tax.

(Emphasis added.) In essence, the proposed initiative would require otherwise qualified electors to pay the fee for a hunting or fishing license in order to vote for fish and game commissioners. While the licensure requirement for voting is not explicitly a poll tax, the initiative does have the effect of conditioning the right to vote upon the payment of a fee. Even if the licensure requirement is not deemed a poll tax, a reviewing court may rely on the line of case authority prohibiting the placement of restrictions, such as property ownership, on the right to vote. In Johnson v. Lewiston Orchard Irr. Dist., 99 Idaho 501, 584 P.2d 646 (1978), the Idaho Supreme Court ruled that restrictions on the right to vote must be "carefully and meticulously scrutinized." Johnson, 99 Idaho at 503, quoting Kramer v. Union Free School Dist., 395 U.S. 621, 626-27 (1969). Such a restriction must be "necessary to promote a compelling state interest in order to survive constitutional attack." *Id.* Since the proposed initiative contains no findings that would explain the "compelling state interest" to a reviewing court, the proposed initiative will be very vulnerable to challenge under this standard. Indeed, this office concludes that a reviewing court is likely to rule that conditioning the ability to vote for a public official on the payment of a fee is unconstitutional.

Fourth, the proposed initiative does not include any procedure to be used in conducting the election of fish and game commissioners. Title 34 contains comprehensive rules and restrictions governing elections. Taking just one example, the proposed initiative states that the "Idaho Department of Fish and Game shall designate the time and place for the election of commissioners," while Idaho Code § 34-106 establishes strict limits on the times during the year when elections can be held. If it is the intent of the proposed initiative to deviate from the general election guidelines contained in title 34, that intention should be specifically stated in the text of the initiative. Furthermore, if the elections for commissioners will follow a different process than the process established for other elections, the text of the initiative should specifically set out the desired process.

Finally, a statewide election carries a significant cost. The proposed initiative does not address the question of how the fish and game commissioner elections are to be funded. The proposed initiative should either contain a funding mechanism or designate a particular account within the Department of Fish and Game that will bear the cost of commissioner elections.

I HEREBY CERTIFY that the enclosed measure has been reviewed for form, style and matters of substantive import and that the recommendations set forth above have been communicated to petitioner Jim Pratt by deposit in the U.S. Mail of a copy of this certificate of review.

Sincerely,

ALAN G. LANCE
Attorney General

Analysis by:

Matthew J. McKeown
Deputy Attorney General

May 28, 1999

Honorable Pete T. Cenarrusa
Secretary of State
HAND DELIVERED

Re: Certificate of Review
Initiative Concerning State Term Limits

Dear Mr. Cenarrusa:

An initiative petition was filed with your office on May 19, 1999, called the "Idaho State Term Limits Act of 2000" (proposed initiative).[1] Pursuant to Idaho Code § 34-1809, this office has reviewed the proposed initiative and has prepared the following advisory comments. It must be stressed that, given the strict statutory timeframe in which this office must respond and the complexity of the legal issues raised in this proposed initiative, our review can only isolate areas of concern and cannot provide in-depth analysis of each issue that may present problems. Further, under the review statute, the Attorney General's recommendations are "advisory only," and the petitioners are free to "accept or reject them in whole or in part."

BALLOT TITLES

Following the filing of the proposed initiative, our office will prepare short and long ballot titles. The ballot titles should impartially and succinctly state the purpose of the measure without being argumentative and without creating prejudice for or against the measure. While our office prepares the titles, if petitioners would like to propose language with these standards in mind, we would recommend that they do so and their proposed language will be considered.

MATTERS OF SUBSTANTIVE IMPORT

The proposed initiative would make a number of changes to Idaho Code § 34-907. Idaho Code § 34-907 contains the ballot access restrictions for statewide elected officials, state legislators and county officials that were adopted by voter initiative in 1994. None of these changes raise any statutory or constitutional concern.

1. Addition of the term "Special"

Currently, Idaho Code § 34-907(1) states that the ballot access restrictions apply for all multi-term incumbents planning to appear on the "primary or general election ballot." The proposed initiative would include ballots prepared for "special" elections in the list of ballots covered by the ballot access restrictions in Idaho Code § 34-907(1).

2. Repeal of Ballot Access Restrictions for Congressional Candidates

Currently, Idaho Code §§ 34-907(1)(a) and (b) set out ballot access restrictions for multi-term congressional incumbents. Ballot access restrictions for congressional candidates were held to be unconstitutional in U.S. Term Limits, Inc. v. Thornton, 514 U.S. 779 (1995). The initiative would remove the unconstitutional language from Idaho Code § 34-907.

3. Restriction on Switching from House to Senate and Vice Versa in Consecutive Elections

Idaho Code § 34-907(1)(d) prohibits an individual from appearing on the ballot as a candidate for either the State Senate or House of Representatives when that individual has served as "a state legislator, representing any district within the state, including all House seats within the same district, during eight (8) or more of the previous fifteen (15) years." However, the initial language in Idaho Code § 34-907(1) limits this restriction to service in the "same office." Therefore, under the current version of Idaho Code § 34-907, a person who is prohibited from appearing on the ballot as a candidate for the State Senate, for example, could appear on the ballot as a candidate for the House of Representatives. The same would be true for a multi-term member of the House appearing on the ballot as a candidate for State Senate.

The initiative would narrow the ability of a multi-term incumbent in one house to appear on the ballot as a candidate for a position in the other house. A state legislator cannot appear on the ballot as a candidate for either the State Senate or the State House of Representatives once he or she has served as a "member of the state legislature during twelve (12) or more of the previous fifteen (15) years."

4. Repeal of Ballot Access Restrictions for County Officials

Currently, Idaho Code §§ 34-907(1)(e) and (f) contain ballot access restrictions for multi-term incumbent candidates for county commission and other county elected positions. The initiative would repeal these restrictions.

5. Change of Effective Date for Terms Counted Toward Ballot Access Restrictions

Section 5 of the 1994 initiative enacting the current version of Idaho Code § 34-907 stated that the effective date of the initiative was January 1, 1995. It also stated that "[s]ervice prior to January 1, 1995 shall not be counted for purpose of" calculating when the ballot access restrictions go into effect. Legislative terms begin on December 1 following the general election. Idaho Code § 67-404. Therefore, the term that resulted from the 1994 general election does not count toward the ballot access restriction calculations for state legislators only.

Section 3 of the proposed initiative would change the date from which terms are calculated to determine when ballot access restrictions begin. The initiative includes all "terms of office [that] began or begin at any time after December 1, 1994" in the calculation of terms leading toward ballot access restrictions. It is not clear what the drafters intend by this change. It does not cover the state legislative terms that were the subject of the 1994 general election because those terms began on December 1, 1994, not after December 1, 1994. The drafters should clarify what they hope to accomplish with the language in section 3 that differs from the existing effective date of Idaho Code § 34-907.

Sincerely,

ALAN G. LANCE
Attorney General

Analysis by:

Matthew J. McKeown
Deputy Attorney General

1 A companion petition called the "Idaho Term Limits Act of 2000" was also submitted on May 19, 1999.

May 28, 1999

Honorable Pete T. Cenarrusa
Secretary of State
HAND DELIVERED

Re: Certificate of Review
Initiative Concerning State Term Limits

Dear Mr. Cenarrusa:

An initiative petition was filed with your office on May 19, 1999 called the "Idaho Term Limits Act of 2000" (proposed initiative).[1] Pursuant to Idaho Code § 34-1809, this office has reviewed the proposed initiative and has prepared the following advisory comments. It must be stressed that, given the strict statutory timeframe in which this office must respond and the complexity of the legal issues raised in this proposed initiative, our review can only isolate areas of concern and cannot provide in-depth analysis of each issue that may present problems. Further, under the review statute, the Attorney General's recommendations are "advisory only," and the petitioners are free to "accept or reject them in whole or in part."

BALLOT TITLES

Following the filing of the proposed initiative, our office will prepare short and long ballot titles. The ballot titles should impartially and succinctly state the purpose of the measure without being argumentative and without creating prejudice for or against the measure. While our office prepares the titles, if petitioners would like to propose language with these standards in mind, we would recommend that they do so and their proposed language will be considered.

MATTERS OF SUBSTANTIVE IMPORT

The proposed initiative makes a number of changes to Idaho Code § 34-907. Idaho Code § 34-907 contains the ballot access restrictions for statewide elected officials, state legislators and county officials that were adopted by voter initiative in 1994. None of these changes raises any statutory or constitutional concern.

1. Addition of the term "Special"

Currently, Idaho Code § 34-907(1) states that the ballot access restrictions apply for all multi-term incumbents planning to appear on the "primary or general election ballot." The proposed initiative would include ballots prepared for "special" elections in the list of ballots covered by the ballot access restrictions in Idaho Code § 34-907(1).

2. Repeal of Ballot Access Restrictions for Congressional Candidates

Currently, Idaho Code §§ 34-907(1)(a) and (b) set out ballot access restrictions for multi-term congressional incumbents. Ballot access restrictions for congressional candidates were held to be unconstitutional in U.S. Term Limits, Inc. v. Thornton, 514 U.S. 779 (1995). The initiative would remove the unconstitutional language from Idaho Code § 34-907.

3. Restriction on Switching from House to Senate and Vice Versa in Consecutive Elections

Idaho Code § 34-907(1)(d) prohibits an individual from appearing on the ballot as a candidate for either the State Senate or House of Representatives when that individual has served as "a state legislator, representing any district within the state, including all House seats within the same district, during eight (8) or more of the previous fifteen (15) years." However, the initial language in Idaho Code § 34-907(1) limits this restriction to service in the "same office." Therefore, under the current version of Idaho Code § 34-907, a person who is prohibited from appearing on the ballot as a candidate for the State Senate, for example, could appear on the ballot as a candidate for the House of Representatives. The same would be true for a multi-term member of the House appearing on the ballot as a candidate for State Senate.

The initiative would narrow the ability of a multi-term incumbent in one house to appear on the ballot as a candidate for a position in the other house. A state legislator cannot appear on the ballot as a candidate for either the State Senate or the State House of Representatives once he or she has served as a "member of the state legislature during twelve (12) or more of the previous fifteen (15) years."

4. Local Option to Opt Out of Ballot Access Restrictions for County Officials

The proposed initiative would allow counties to hold local referenda to determine whether ballot access restrictions should apply to county commissioners and county row officers (sheriff, assessor, prosecuting attorney, clerk, treasurer, coroner). The proposed initiative specifies that county commissioners and county row officers be separated into two referendum questions for any local election that would be held pursuant to the new language.

The proposed initiative states that if a majority of votes is cast in favor of eliminating ballot access restrictions for multi-term incumbent candidates for county commission, then the restrictions that are set out in Idaho Code § 34-907(1) will not apply to county commissioner candidates. The drafters of the initiative have not included similar language that specifies what the effect would be of a majority vote against ballot access restrictions for county row officers. Assuming that the drafters wish to treat the election results for both county commissioners and county row officers in the same fashion, the proposed initiative should be amended to include language that would specify the effect of a majority vote against ballot access restrictions for county row offices.

5. Local Option to Opt Out of Ballot Access Restrictions for Municipal Officials

The ballot access restrictions for municipal elected officials are set out in Idaho Code § 50-478. The proposed initiative would allow municipal corporations to hold local referenda to determine whether ballot access restrictions should apply to multi-term incumbent candidates for mayor and city council. While the process for conducting the referenda is the same as it is for county officials set out above, voters would not be able to consider ballot access restrictions for mayoral candidates and city council candidates separately. Voters would either have to vote against ballot access restrictions for "all elected offices" or for ballot access restrictions for "all elected offices."

6. Local Option to Opt Out of Ballot Access Restrictions for School District Trustees

The ballot access restrictions for school district trustees are set out in Idaho Code § 33-443. The proposed initiative would allow school districts to hold local referenda to determine whether ballot access restrictions should apply to multi-term incumbent candidates for school district trustee. The process for conducting the referenda is the same as it would be for county and city referenda.

7. Change of Effective Date for Terms Counted Toward Ballot Access Restrictions

Section 5 of the 1994 initiative enacting the current version of Idaho Code § 34-907 stated that the effective date of the initiative was January 1, 1995. It also stated that "[s]ervice prior to January 1, 1995 shall not be counted for purpose of" calculating when the ballot access restrictions go into effect. Legislative terms begin on December 1 following the general election. Idaho Code § 67-404. Therefore, the term that resulted from the 1994 general election does not count toward the ballot access restriction calculations for state legislators only.

Section 5 of the proposed initiative would change the date from which terms are calculated to determine when ballot access restrictions begin. The initiative includes all "terms of office [that] began or begin at any time after December 1, 1994" in the calculation of terms leading toward ballot access restrictions. It is not clear what the drafters intend by this change. It does not cover the state legislative terms that were the subject of the 1994 general election because those terms began on December 1, 1994, not after December 1, 1994. The drafters should clarify what they hope to accomplish with the language in section 5 that differs from the existing effective date of Idaho Code § 34-907.

Sincerely,

ALAN G. LANCE
Attorney General

Analysis by:

Matthew J. McKeown
Deputy Attorney General

1 A companion petition called the "Idaho State Term Limits Act of 2000" was also submitted on May 19, 1999.

November 5, 1999

Honorable Pete T. Cenarrusa
Secretary of State
HAND DELIVERED

Re: Certificate of Review
Proposed Initiative Regarding Amendment to Idaho Code § 67-6525

Dear Mr. Cenarrusa:

An initiative petition was filed with your office on November 3, 1999, that would amend Idaho Code § 67-6525. Pursuant to Idaho Code § 34-1809, this office has reviewed the proposed initiative and has prepared the following advisory comments. It must be stressed that, given the strict statutory timeframe in which this office must respond and the complexity of the legal issues raised in this proposed initiative, our review can only isolate areas of concern and cannot provide in-depth analysis of each issue that may present problems. Further, under the review statute, the Attorney General's recommendations are "advisory only," and the petitioners are free to "accept or reject them in whole or in part."

BALLOT TITLES

Following the filing of the proposed initiative, our office will prepare short and long ballot titles. The ballot titles should impartially and succinctly state the purpose of the measure without being argumentative and without creating prejudice for or against the measure. While our office prepares the titles, if petitioners would like to propose language with these standards in mind, we would recommend that they do so and their proposed language will be considered.

MATTERS OF SUBSTANTIVE IMPORT

The proposed initiative would amend Idaho Code § 67-6525 in the following manner:

> Prior to annexation of an unincorporated area, a city council shall request and receive a recommendation from the planning and zoning commission, or the planning commission and the zoning commission, on the proposed plan and zoning ordinance changes for the unincorporated area. Each commission and the city council shall follow the notice and hearing procedures provided in section 67-6509, Idaho Code. <u>Annexation shall not take place until a favorable concurrence of the majority of affected property owners within the unincorporated area is established.</u> Concurrently or immediately following the adoption of an ordinance of annexation, the city council shall amend the plan and zoning ordinance.

(Proposed language underlined.) If enacted by the voters, the new language would appear to limit a city's ability to annex unincorporated land by conditioning annexation on approval by property owners within the area proposed for annexation. This proposal raises a number of potential legal problems.

First, annexation is currently governed by Idaho Code §§ 50-222 through 50-233. These provisions establish a detailed procedure for municipalities to follow when annexing adjacent and nonadjacent territory. In particular, Idaho Code § 50-222(1) currently authorizes "forced annexation" under certain circumstances:

> [A]ny land lying contiguous or adjacent to any city in the state of Idaho, or to any addition or extension thereof may be annexed by the city only if the land is lying in the area of city impact as determined by procedures contained in section 67-6526, Idaho Code, and the land is laid off into blocks containing not more than five (5) acres of land each, whether the same shall have been or shall be laid off, subdivided or platted in accordance with any statute of this state or otherwise, or whenever the owner or proprietor or any person by or with his authority, has sold or begun to sell off such contiguous or adjacent lands by metes and bounds in tracts not exceeding five (5) acres.

Section 50-222(1) does not condition annexation on voter approval. Therefore, section 50-222(1) and the amendment proposed by the initiative could be in direct conflict with each other. The proposed amendment should be revised to resolve the potential conflict with Idaho Code § 50-222(1).

Next, the reference in the proposed language to a "favorable concurrence of the majority of affected property owners" appears to contemplate some type of election. However, the proposed initiative does not specify how that election would occur or who would bear the cost of such an election. The proposed initiative should probably be modified to set out a procedure for holding the elections that appear to be anticipated. In addition, the initiative should specify how the election will be funded. This is particularly important since the proposed initiative appears to anticipate some type of election in an unincorporated area. Currently, such an election would be unlawful.

Finally, the "favorable concurrence" that is incorporated into the proposed initiative is limited to "affected property owners within the unincorporated area." The Idaho Constitution specifically prohibits nearly all restrictions on voting based on property ownership. Art. I, § 20 of the Idaho Constitution states:

> No property qualifications shall ever be required for any person to vote or hold office except in school elections, or elections creating indebtedness, or in irrigation district elections, as to which last-named elections the legislature may restrict the voters to land owners.[1]

Since the proposed initiative would limit voting to "property owners within the unincorporated area," a reviewing court is likely to determine that the proposed initiative is invalid because it violates Art. I, § 20 of the Idaho Constitution.

I HEREBY CERTIFY that the enclosed measure has been reviewed for form, style and matters of substantive import and that the recommendations set forth above have been communicated to petitioner William H. Thomas by deposit in the U.S. Mail of a copy of this certificate of review.

Sincerely,

ALAN G. LANCE
Attorney General

Analysis by:

Matthew J. McKeown
Deputy Attorney General

1 The Idaho Supreme Court invalidated the exception for school district elections in Muench v. Paine, 94 Idaho 12, 480 P.2d 196 (1971).

December 13, 1999

Honorable Pete T. Cenarrusa
Secretary of State
HAND DELIVERED

Re: Certificate of Review
Proposed Initiative Regarding Small Stakes Video Machine Gaming

Dear Mr. Cenarrusa:

An initiative petition was filed with your office on November 22, 1999, that would add a new section to chapter 9, title 23, Idaho Code. Pursuant to Idaho Code § 34-1809, this office has reviewed the proposed initiative and has prepared the following advisory comments. It must be stressed that, given the strict statutory timeframe in which this office must respond and the complexity of the legal issues raised in this proposed initiative, our review can only isolate areas of concern and cannot provide in-depth analysis of each issue that may present problems. Further, under the review statute, the Attorney General's recommendations are "advisory only," and the petitioners are free to "accept or reject them in whole or in part."

BALLOT TITLES

Following the filing of the proposed initiative, our office will prepare short and long ballot titles. The ballot titles should impartially and succinctly state the purpose of the measure without being argumentative and without creating prejudice for or against the measure. While our office prepares the titles, if petitioners would like to propose language with these standards in mind, we would recommend that they do so and their proposed language will be considered.

MATTERS OF SUBSTANTIVE IMPORT

The proposed initiative would create a new provision titled, "Small Stakes Video Machine Gaming," as Idaho Code § 23-929. Section one of the contemplated statute would make it lawful to "make available for public play only, up to five (5) video, bingo, keno, blackjack, draw poker, reel or other approved gaming machines" in establishments holding a liquor license. The remainder of the contemplated statute establishes limits on prizes and creates various regulatory duties for the director of the Department of Law Enforcement.

Article 3, § 20 of the Idaho Constitution prohibits all forms of gambling, except the types of gambling specifically enumerated in subsections 1(a) through 1(c). Article 3, § 20, subsection 2, specifically prohibits "any form of casino gambling including, but not limited to, blackjack, craps, roulette, poker, baccarat, keno and slot machines." This prohibition includes "any electronic or electromechanical imitation or simulation of any form of casino gambling."

The proposed initiative is an attempt to legalize a method of casino gambling that is specifically prohibited by art. 3, § 20 of the Idaho Constitution. Legislation that is passed via citizen initiative has the same force and effect as legislation passed by the legislature. *See, e.g.*, Westerberg v. Andrus, 114 Idaho 401, 757 P.2d 664 (1988). As a result, a reviewing court will invalidate legislation passed via citizen initiative that directly conflicts with a constitutional requirement. *See, e.g.*, Simpson v. Cenarrusa, 130 Idaho 609, 944 P.2d 1372 (1997) (prohibiting the secretary of state from implementing certain ballot legend requirements promulgated via citizen initiative because those requirements violated constitutional provisions). Therefore, this office concludes that a reviewing court will invalidate the proposed initiative because it directly conflicts with Art. 3, § 20 of the Idaho Constitution.

Sincerely,

ALAN G. LANCE
Attorney General

Analysis by:

Matthew J. McKeown
Deputy Attorney General

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