

EXHIBIT NO. \_\_\_\_\_ (WAG-10)  
DOCKET NO. \_\_\_\_\_  
2003 POWER COST ONLY RATE CASE  
WITNESS: WILLIAM A. GAINES

BEFORE THE  
WASHINGTON UTILITIES AND TRANSPORTATION COMMISSION

WASHINGTON UTILITIES AND  
TRANSPORTATION COMMISSION,

Complainant,

Docket No. \_\_\_\_\_

v.

PUGET SOUND ENERGY, INC.,

Respondent.

DIRECT TESTIMONY OF  
WILLIAM A. GAINES  
ON BEHALF OF PUGET SOUND ENERGY, INC.

### PSE'S POWER SUPPLY PORTFOLIO

On December 31, 2002, PSE's peak electric power resources were approximately 4,577,135 KW. PSE's historical peak load of approximately 4,847,000 KW occurred on December 21, 1998. In order to meet an extreme winter peak load, PSE supplements its electric power resources with call options and other instruments that may include, but are not limited to, weather related hedges and exchange agreements.

During 2002, PSE's total electric energy production was supplied 26.2% by its own resources, 22.5% through long-term contracts with several of the Washington Public Utility Districts ("PUDs") that own hydro-electric projects on the Columbia River, 22.9% from other firm purchases and 28.4% from non-firm purchases.

The following table shows PSE's electric energy supply resources at December 31, 2002, and energy production during the year:

	Peak Power Resources at December 31, 2002		2002 Energy Production	
	Kilowatts	%	Kilowatt-Hours (Thousands)	%
Purchased resources:				
Columbia River				
PUD Contracts (Hydro)	1,391,000	30.4%	5,988,118	22.5%
Other hydro	175,660	3.8%	717,215	2.7%
Other producers	1,209,675	26.4%	5,380,396	20.2%
Non-firm energy purchases	N/A	N/A	7,584,398	28.4%
<b>Total purchased</b>	<b>2,776,335</b>	<b>60.6%</b>	<b>19,670,127</b>	<b>73.8%</b>
Company-owned resources:				
Hydro	300,000	6.6%	1,351,540	5.1%
Coal	700,000	15.3%	4,627,901	17.3%
Natural gas/oil	800,800	17.5%	1,016,835	3.8%
<b>Total Company-owned</b>	<b>1,800,800</b>	<b>39.4%</b>	<b>6,996,276</b>	<b>26.2%</b>
<b>Total</b>	<b>4,577,135</b>	<b>100.0%</b>	<b>26,666,403</b>	<b>100.0%</b>

## **COMPANY-OWNED ELECTRIC GENERATION RESOURCES**

PSE and other utilities are joint owners of four mine-mouth, coal-fired, steam-electric generating units at Colstrip, Montana, approximately 100 miles east of Billings, Montana. PSE owns a 50% interest (307,000 KW) in Units 1 and 2 and a 25% interest (370,000 KW) in Units 3 and 4. The owners of the Colstrip Units purchase coal for the Units from Western Energy Company ("Western Energy"), under the terms of long-term coal supply agreements.

PSE owns a (170,000 KW) natural-gas fired cogeneration facility located near Bellingham, Washington, which was purchased from Encogen Northwest L.P. ("Encogen") on November 1, 1999. PSE also has the following plants with an aggregate net generating capability of 909,000 KW: Upper Baker River hydro project (104,900 KW) constructed in 1959; Lower Baker River hydro project (79,000 KW) reconstructed in 1960; White River hydro plant (58,500 KW) constructed in 1911; Snoqualmie Falls hydro plant (46,150 KW), half the capability of which was installed during the period 1898 to 1910 and half in 1957; and one smaller hydro plant, Electron (22,000 KW), constructed during the period 1904 to 1929; a standby internal combustion unit (2,750 KW) installed in 1969; four dual-fuel combustion turbine units (275,400 KW total) installed during 1981; and two dual-fuel combustion turbine units (202,100 KW total) installed during 1984. During 2001, PSE installed two additional dual-fuel combustion turbines (118,200 KW total). All of these generating facilities, except the Colstrip, Montana plants, are located in PSE's service territory.

## **COLUMBIA RIVER ELECTRIC ENERGY SUPPLY CONTRACTS**

During 2002, approximately 22.5% of PSE's energy output was obtained at an average cost of approximately 13.96 mills per KWH through long-term contracts with several of the Washington PUDs owning hydro-electric projects on the Columbia River.

PSE's purchases of power from the Columbia River projects is generally on a "cost of service" basis under which PSE pays a proportionate share of the annual debt service and operating and maintenance costs of each project in proportion to the amount of power annually

purchased by PSE from such project. Such payments are not contingent upon the projects being operable. These projects are financed through substantially level debt service payments, and their annual costs may vary over the term of the contracts as additional financing is required to meet the costs of major maintenance, repairs or replacements or license requirements.

PSE has contracted to purchase from Chelan County PUD ("Chelan") a share of the output of the original units of the Rock Island Project which equaled 50% as of July 1, 1999 and remains unchanged thereafter for the duration of the contract which expires in 2012. PSE has also contracted to purchase the entire output of the additional Rock Island units for the duration of the contract, except that PSE's share of output of the additional units may be reduced up to 10% per year beginning July 1, 2000, subject to a maximum aggregate reduction of 50%, upon the exercise of rights of withdrawal by Chelan for use in its local service area. Chelan began withdrawing 5% of the additional units on July 1, 2000. As of December 31, 2002, PSE's aggregate annual capacity from all units of the Rock Island Project was 455,340 KW. PSE has contracted to purchase from Chelan 38.9% (505,000 KW as of December 31, 2002) of the annual output of the Rocky Reach Project, which percentage remains unchanged for the remainder of the contract which expires in 2011. PSE has contracted to purchase from Douglas County PUD 31.3% (261,000 KW as of December 31, 2002) of the annual output of the Wells Project, the percentage of which remains unchanged for the remainder of the contract which expires in 2018.

PSE has contracted to purchase from Grant County PUD 8.0% (72,000 KW as of December 31, 2002) of the annual output of the Priest Rapids Project and 10.8% (98,000 KW as of December 31, 2002) of the annual output of the Wanapum Project. The current contract for purchase of the Priest Rapids output ends on October 31, 2005 and the contract for purchase of the Wanapum Contract expires on October 31, 2009. In December 2001 PSE signed new contracts continuing its power purchases upon termination of the current contracts. The new arrangement includes three contracts under which PSE's portion of the Projects output will diminish over time as Grant PUD's loads increase.

## **ELECTRIC ENERGY SUPPLY CONTRACTS AND AGREEMENTS WITH OTHER UTILITIES**

PSE has entered into long-term firm purchased power contracts with other utilities in the West region. PSE is generally not obligated to make payments under these contracts unless power is delivered.

Under a 1985 settlement agreement relating to Washington Public Power Supply System ("WPPSS") Nuclear Project No. 3, in which PSE had a 5% interest, PSE is entitled to receive from BPA beginning January 1, 1987, electric power during the months of November through April. Under the contract, PSE is guaranteed to receive not less than 191,667 MWH in each contract year until PSE has received total deliveries of 5,833,333 MWH. PSE expects the contract to be in effect until at least June 2008. Also pursuant to the 1985 settlement agreement, BPA has an option to request that PSE deliver up to 67 MW of exchange energy to BPA in all months except May, July and August through the remaining term of the agreement which is no earlier than June 2008.

On December 31, 2002, a 15 year power contract between Avista Corporation and PSE expired under the terms of the agreement. During 2002 the contract provided for the delivery of 33 MW of capacity and 24.75 average MW of energy.

On October 27, 1988, PSE executed a 15-year contract for the purchase of firm power and energy from PacifiCorp. Under the terms of the agreement, PSE receives 120 average MW of energy and 200 MW of peak capacity. This contract expires on October 31, 2003.

On October 1, 1989, PSE signed a contract with The Montana Power Company, which subsequently sold its assets to Northwestern Energy in 2002, under which Northwestern Energy provides PSE, from its share of Colstrip Unit 4, 71 average MW of energy (97 MW of peak capacity) over a 21-year period. This contract expires December 2010.

PSE executed an exchange agreement with Pacific Gas & Electric Company ("PG&E") which became effective on January 1, 1992. Under the agreement, 300 MW of capacity together with 413,000 MWH of energy are exchanged seasonally every year on a unit for unit basis. No

payments are made under this agreement. PG&E is a summer peaking utility and will provide power during the months of November through February. PSE is a winter peaking utility and will provide power during the months of June through September. Each party may terminate the contract for various reasons.

In October 1997, a 10-year power exchange agreement between PSE and Powerex (a subsidiary of a British Columbia utility) became effective. Under this agreement Powerex pays PSE for the right to deliver power to PSE at the Canadian border in exchange for PSE delivering power to Powerex at various locations in the United States.

### **ELECTRIC ENERGY SUPPLY CONTRACTS AND AGREEMENTS WITH NON-UTILITIES**

As required by the federal Public Utility Regulatory Policies Act ("PURPA"), PSE entered into long-term firm purchased power contracts with non-utility generators. The most significant of these are the contracts described below which PSE entered into in 1989, 1990 and 1991 with operators of natural gas-fired cogeneration projects. PSE purchases the net electrical output of these three projects at fixed and annually escalating prices which were intended to approximate PSE's avoided cost of new generation projected at the time these agreements were made. On June 29, 1989, PSE executed a 20-year contract to purchase 70 average MW of energy and 80 MW of capacity, beginning October 11, 1991, from the March Point Cogeneration Company ("March Point"), which owns and operates a natural gas-fired cogeneration facility known as March Point Phase I, located at the Equilon refinery in Anacortes, Washington. On December 27, 1990, PSE executed a second contract (having a term coextensive with the first contract) to purchase an additional 53 average MW of energy and 60 MW of capacity, beginning in January 1993, from another natural gas-fired cogeneration facility owned and operated by March Point, which facility is known as March Point Phase II and is located at the Equilon refinery in Anacortes, Washington.

On February 24, 1989, PSE executed a 20-year contract to purchase 108 average MW of energy and 123 MW of capacity, beginning in April 1993, from Sumas Cogeneration Company, L.P., which owns and operates a natural gas-fired cogeneration project located in Sumas, Washington.

On March 20, 1991, PSE executed a 20-year contract to purchase 216 average MW of energy and 245 MW of capacity, beginning in April 1994, from Tenaska Washington Partners, L.P., which owns and operates a natural gas-fired cogeneration project located near Ferndale, Washington. In December 1997 and January 1998, PSE and Tenaska Washington Partners entered into revised agreements in which PSE became the principal natural gas supplier to the project and power purchase prices under the Tenaska contract were revised to reflect market-based prices for the natural gas supply. PSE obtained an order from the Washington Commission creating a regulatory asset related to the \$215 million restructuring payment. Under terms of the order, PSE is allowed to accrue as an additional regulatory asset one-half the carrying costs of the deferred balance over the first five years, which ended December 2002.

In December 1999, PSE bought out the remaining 8.5 years of one of the natural gas supply contracts serving Encogen from Cabot Oil & Gas Corporation (Cabot) which provided approximately 60% of the plant's natural gas requirements. PSE became the replacement gas supplier to the project for 60% of the supply under the terms of the Cabot Agreement.