EXH. SEF-1CT
DOCKET UE-191037
COLSTRIP UNIT 4 SALE
WITNESS: SUSAN E. FREE

BEFORE THE
WASHINGTON UTILITIES AND TRANSPORTATION COMMISSION

In the Matter of the Application of **PUGET SOUND ENERGY** **For an Order Authorizing the Sale of All of Puget Sound Energy's Interests in Colstrip Unit 4 and Certain of Puget Sound Energy's Interests in the Colstrip Transmission System**	**Docket UE-191037**

PREFILED DIRECT TESTIMONY (CONFIDENTIAL) OF

SUSAN E. FREE

ON BEHALF OF PUGET SOUND ENERGY

REDACTED VERSION

FEBRUARY 19, 2020

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PREFILED DIRECT TESTIMONY (CONFIDENTIAL) OF

SUSAN E. FREE

ON BEHALF OF PUGET SOUND ENERGY

I. INTRODUCTION

Q. Please state your name, business address, and position with Puget Sound Energy.

A. My name is Susan E. Free. My business address is 355 110th Ave. NE, Bellevue, WA 98004. I am the Director of Revenue Requirement and Regulatory Compliance for Puget Sound Energy ("PSE").

Q. Have you prepared an exhibit describing your education, relevant employment experience, and other professional qualifications?

A. Yes. Please see the First Exhibit to the Prefiled Direct Testimony of Susan E. Free, Exh. SEF-2.

Q. Please summarize your prefiled direct testimony.

A. This prefiled direct testimony addresses the accounting being requested in PSE's Application for authorization of the following transactions, which are explained in more detail in the Prefiled Direct Testimony of Ronald J. Roberts, Exh. RJR-1CT, (collectively, the "Proposed Transactions"):

(i) the Colstrip Unit 4 Purchase and Sale Agreement, which is provided as the Fifth Exhibit to the Prefiled Direct Testimony of Ronald J. Roberts, Exh. RJR-6;

(ii) the Colstrip Transmission System Purchase and Sale Agreement, which is provided as the Sixth Exhibit to the Prefiled Direct Testimony of Ronald J. Roberts, Exh. RJR-7; and

(iii) the NorthWestern Energy PPA, dated as of December 9, 2019, which is provided as the Seventh Exhibit to the Prefiled Direct Testimony of Ronald J. Roberts, Exh. RJR-8C.

Specifically, this prefiled direct testimony addresses the following accounting and regulatory issues in support of the Application.

(i) An overview of the 2017 GRC Settlement Agreement[1] as it relates to the unrecovered costs associated with the Colstrip Generating Station and how the 2017 GRC Settlement Agreement impacts the accounting for the Proposed Transactions (Section II);

(ii) The impact on the accounting requested in this Application for the fact that rates from PSE's 2019 general rate case reflect Colstrip Unit 4 as an owned facility (discussed throughout my testimony);

(iii) Accounting for the unrecovered plant balance for the generation assets associated with Colstrip Unit 4 (Section III);

(iv) Accounting for the decommissioning and remediation costs[2] for the generating assets associated with Colstrip Unit 4 (Section IV);

(v) Accounting for the gain or loss on the sale of the transmission assets (Section V); and

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[1] *See Wash. Utils. & Transp. Comm'n v. Puget Sound Energy*, Dockets UE-170033 & UG-170034 (consolidated), Order 08, Appx. B (Dec. 5. 2017) (the "2017 GRC Settlement Agreement").

[2] Remediation represents the costs to remediate the facilities and is generally comprised of legal obligations. Decommissioning represents the costs to close down the facilities and generally do not include legal obligations.

(vi) Impacts on PSE's power cost adjustment ("PCA") mechanism (Section VI).

II. OVERVIEW OF 2017 GENERAL RATE CASE SETTLEMENT AS IT RELATES TO COLSTRIP UNIT 4

Q. Please describe the elements of the 2017 GRC Settlement Agreement that relate to Colstrip Unit 4 assets.

A. The depreciation rates set for Colstrip Units 3 & 4 in the 2017 GRC Settlement Agreement contained three components intended to be recovered through December 31, 2027:

1. the original book cost for Colstrip Units 3 & 4 based on information as of September 30, 2016,
2. estimated decommissioning costs for Colstrip Units 3 & 4, and
3. estimated remediation costs for Colstrip Units 3 & 4 based on early reports from Geosyntec Consultants.[3]

The 2017 GRC Settlement Agreement assumed that PSE would fund the recovery of the original book cost, decommissioning, and remediation costs through depreciation rates. Due to the imperfect nature of ratemaking, however, the parties to 2017 GRC Settlement Agreement understood that the depreciation rates would

[3] Cost estimates for compliance with the Coal Combustion Residuals Rule ("CCR") were provided in a report from Geosyntec Consultants ("Master Plan"). The Colstrip owners had not yet entered into the investigation phase of remediation which is the phase when more detailed cost estimates are established. However, before the investigation phase, it was important to understand the potential impacts of the CCR and the Montana Administrative Order on Consent. Therefore, Geosyntec Consultants compiled the Master Plan to provide an order of magnitude for what compliance with the new regulations might entail. At the time Geosyntec Consultants developed the Master Plan, the Colstrip owners were early in the process in determining the manner in which the Colstrip Generating Station would comply with the CCR.

likely be insufficient to fully recover each of the three components (i.e., original book cost, decommissioning, and remediation costs). Therefore, the 2017 GRC Settlement Agreement provided PSE with the ability to use the regulatory liability associated with Production Tax Credits ("PTCs") to fund unrecovered plant (i.e., original book cost) and decommissioning and remediation costs.

Q. Please explain how the 2017 GRC Settlement Agreement provided for the Regulatory Liability for PTCs to be used related to Colstrip Units 3 & 4.

A. Section I of the 2017 GRC Settlement Agreement permitted PSE to use its outstanding regulatory liability for PTCs, once monetized and in the following order of priority, to address future costs associated with the Colstrip Generating Station:

(i) to fund $5 million for the Montana Community Transition payment, as identified in paragraph 118 in the 2017 GRC Settlement Agreement;

(ii) to recover unrecovered plant balances for Colstrip Units 1 through 4; and

(iii) to fund and recover prudently incurred decommissioning and remediation costs for Colstrip Units 1 through 4.[4]

The 2017 GRC Settlement Agreement recognized that the timing of monetization of PTCs may not align with the timing of the closure of Colstrip Units 1 & 2. Accordingly, the 2017 GRC Settlement Agreement permitted PSE to hold the remaining unrecovered plant balances in a regulatory asset in rate base until the

[4] *See* 2017 GRC Settlement Agreement at ¶ 117.

earlier to occur of either (i) the recovery of all plant balances for Colstrip Units 1 & 2 through offsets of monetized PTCs or (ii) December 31, 2029.[5] At the time of the 2017 GRC Settlement Agreement, it was generally understood that monetization of PTCs occurs when PSE filed its annual tax return and used the PTCs on the filed tax return.

Q. What is the total amount of regulatory liability associated with PTCs that will be available to address the future costs outlined in the 2017 GRC Settlement Agreement?

A. The total amount of the regulatory liability associated with PTCs is $240 million. As of December 31, 2019, PSE had monetized $87.2 million of PTCs.

Q. What is the balance of the regulatory liability associated with PTCs after addressing the Community Transition payment and the unrecovered plant associated with Colstrip Units 1 & 2?

A. As noted above, the total amount of the regulatory liability associated with PTCs is $240 million as of December 31, 2019. Consistent with the terms and conditions of the 2017 GRC Settlement Agreement, PSE will use approximately $[redacted] million of this $240 million to (i) fund $5 million for the Montana Community Transition payment and (ii) recover the unrecovered plant balance

[5] *See id.* at ¶ 25.

associated with Colstrip Units 1 & 2. Therefore, approximately $[redacted] million of this $240 million remains.

Q. Is the remaining regulatory liability associated with PTCs discussed above sufficient to recover the undepreciated value of Colstrip Unit 4?

A. Yes. If the Proposed Transactions were to close as of September 30, 2020,[6] and PSE stops depreciating Colstrip Unit 4 as of such date, the projected undepreciated value of Colstrip Unit 4 is $[redacted] million.[7]

Although the $[redacted] million balance of the remaining regulatory liability associated with PTCs, once monetized, may be sufficient to cover the projected undepreciated plant value of $[redacted] million for Colstrip Unit 4 as of September 30, 2020, the differential of approximately $[redacted] million (i.e., the difference between the $[redacted] million balance of the remaining regulatory liability associated with PTCs and the projected undepreciated plant value of $[redacted] million for Colstrip Unit 4) would provide limited ability for PSE to cover any undepreciated plant on Colstrip Unit 3. As previously discussed, the 2017 GRC Settlement Agreement prioritizes the use of the regulatory liability associated with PTCs to recover undepreciated plant values over the recovery of decommissioning and

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6 As discussed in the Application, PSE is requesting approval by August 31, 2020 in order to close the transaction in September or October of 2020.

7 This balance (i) is based on actuals as of December 31, 2019, projected forward to September 30, 2020, (ii) assumes no additions or retirements to Colstrip Unit 4 after December 31, 2019; (iii) assumes depreciation rates authorized by the Commission in Dockets UE-170033 & UG-170034 (consolidated) through May 19, 2020 and (iv) assumes depreciation rates requested by PSE in Dockets UE-190529, *et al.*, beginning May 20, 2020.

remediation costs. Therefore, it is possible that not enough regulatory liability associated with PTCs will be available for PSE to recover any decommissioning and remediation costs for Colstrip Units 3 & 4 that exceed PSE's existing depreciation reserves associated with those units.

Therefore, in order to preserve the balances of regulatory liability associated with PTCs, PSE respectfully requests that the Commission permit PSE to (i) continue to include the depreciation for Colstrip Unit 4 approved by the Commission in Dockets UE-190529, *et al.*, in rates and (ii) apply such amounts to the requested unrecovered plant regulatory assets for Colstrip Unit 4 in the manner that is defined in more detail below.

III. ACCOUNTING FOR THE SALE OF COLSTRIP UNIT 4 ASSETS

Q. Please describe the proposed accounting associated with the sale of the Colstrip Unit 4 assets.

A. Assuming a closing date of September 30, 2020, for the Proposed Transactions, PSE proposes the following accounting treatment:

(i) PSE retires the net book value of the assets associated with Colstrip Unit 4 on September 30, 2020, and transfers the unrecovered balance (along with any applicable transaction costs) to a regulatory asset (the "Colstrip Unit 4 Unrecovered Plant Regulatory Asset") that PSE will amortize through December 31, 2025;

(ii) The Commission permits PSE to continue to include in rates the depreciation expense associated with the Colstrip Unit 4 assets that will be approved in rates in Dockets UE-

190529, *et al*., through December 31, 2025, which would be built into rates at the time the transaction is closed; and

(iii) PSE be allowed to offset the Colstrip Unit 4 Unrecovered Plant Regulatory Asset with the depreciation expense associated with the Colstrip Unit 4 assets included in rates in Dockets UE-190529, *et al*.

This treatment is similar to the treatment afforded Colstrip Units 1 & 2, and is also consistent with the priorities established in the 2017 GRC Settlement Agreement.

Q. Can you quantify and describe the depreciation that PSE proposed in its Dockets UE-190529, *et al*., for Colstrip Units 3 & 4?

A. Yes. Table 1, below, shows the depreciation expense for Colstrip Unit 4 that PSE proposed in Dockets UE-190529, *et al*.

Table 1. Components of 2019 General Rate Case Depreciation Expense for Colstrip Unit 4 as Requested by PSE

Component	Colstrip Unit 4
Life	$16,159,996
+ Decommissioning	$647,640
+ Remediation	$2,685,254
Total	$19,492,890

As shown in Table 1, above, PSE has broken down the depreciation into three components: a life component, a decommissioning component, and a remediation component. This breakdown assumes that (i) PSE amortizes the unrecovered balance as of September 30, 2020, to zero by December 31, 2025, and (ii) the remaining amount of depreciation is attributable to decommissioning and remediation costs. PSE proposes to offset the Colstrip Unit 4 Unrecovered Plant Regulatory Asset with the projected depreciation expense of $16,159,996 associated with the life component for Colstrip Unit 4. This amount will change depending on the balance of the regulatory asset at the close of the Proposed Transactions.

PSE proposes that the amortization of the Unit 4 regulatory asset continue until December 31, 2025, the proposed depreciation life in Dockets UE-190529, *et al*. This treatment is intended to recover as much of the original book cost as possible from the customers who receive the benefit of power from Colstrip Unit 4.

Q. Why does PSE propose to continue to include Colstrip Unit 4 depreciation in rates?

A. PSE proposes to continue to include Colstrip Unit 4 depreciation in rates for several reasons. First, customers will continue to receive generation associated with Colstrip Unit 4 for the duration of the NorthWestern Energy PPA, which expires on May 15, 2025. Continuing to include amortization of unrecovered plant costs in rates is appropriate because these customers will continue to receive the benefit of the generation from the unit in the form of the NorthWestern PPA.

Second, the approach proposed by PSE is similar to the treatment for other regulatory assets related to transferred production plant, including both the White River and Electron Hydroelectric Projects, wherein PSE continued to apply depreciation expense included in rates against the regulatory asset balance after the sale.[8]

Finally, under PSE's proposal, there is no need to change or defer PSE's rates related to depreciation expense for Colstrip Unit 4 that are approved in Dockets UE-190529, *et al*. Instead, PSE would continue to expense the amounts established in rates. This treatment is supported by the 2017 GRC Settlement Agreement wherein depreciation rates were the first source of funding for unrecovered plant balances as well as decommissioning and remediation, and PTCs were only included as an option if depreciation rates were not sufficient.

Q. Please summarize the proposed entries for which PSE is requesting Commission Approval for the sale of the Colstrip Unit 4 assets.

A. PSE proposes to record the entries reflected in Table 2 below to recognize the pre-tax loss on the sale of the assets and the establishment of a regulatory asset for the unrecovered plant balance. The amounts in Table 2 provide an estimate of the unrecovered plant balance as of September 30, 2020 as discussed in footnote 7 above.

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[8] *See* Docket UE-040640 Order 06 at ⁋⁋ 251-253 and Docket UE-141141 Order 10 at ⁋ 30.

Table 2. Requested Entries for Sale of Colstrip Unit 4 Assets

	FERC Account	Description	Debit	Credit
Cr.	101	Electric Plant in Service		$272 million
Dr.	108	Accum Prov for Dep	$187 million	
Dr.	182.2	Unrecovered Plant	$85 million	
To record the unrecovered plant as a regulatory asset				
Dr.	131	Cash	$1 dollar	
Cr.	182.2	Unrecovered Plant		$1 dollar
To record the sales proceeds against the unrecovered plant regulatory asset				
Dr.	407	Amort of Prop Loss	$16.2 million	
Cr.	182.2	Unrecovered Plant		$16.2 million
To record ongoing annual amortization of regulatory asset through 2025 at $16.2 million reflected in Table 1, which is an estimated annual amount that is subject to change.				

Q. Please explain how accumulated deferred income taxes and excess deferred income taxes would be treated.

A. Deferred taxes would follow the book transactions at the statutory rate of 21 percent. They would be reversed on the plant in service when sold and established on the regulatory asset when created. Additionally, as Mr. Marcelia testified in Dockets UE-190529, *et al.*, excess deferred income taxes ("EDIT") must continue to reverse as if the sale had not occurred.[9] The tax regulations

[9] Dockets UE-190529, *et al.*, Marcelia, Exh. MRM-11T at 7:15 – 8:7.

prescribe the treatment of EDIT when an asset becomes “deregulated” (“whether by disposition, deregulation, or otherwise”) as follows:

> the reduction in the taxpayer's excess tax reserve [...] is equal to the amount by which the reserve could be reduced under that provision if all such property had remained public utility property of the taxpayer and the taxpayer had continued use of its normalization method of accounting with respect to such property.[10]

In other words, a taxpayer must continue to reverse its EDIT as if the retirement had not occurred (i.e. as “if all such property had remained public utility property of the taxpayer”). In the case of Colstrip Unit 4, EDIT will continue to reverse over its remaining life (approximately 5.5 years) as if no retirement had occurred.

Q. How will PSE address the property taxes associated with the sale of its interests in Colstrip Unit 4?

A. PSE includes property taxes associated with the Colstrip Unit 4 assets, like all of PSE’s property taxes, in the property tax tracker (Schedule 141). The Colstrip Unit 4 Purchase and Sale Agreement requires each of PSE and NorthWestern Energy to pay its pro-rata share of the property taxes based on the closing date.[11] Consistent with all other property taxes, PSE will include in the Schedule 141 filing, the amount of property taxes actually paid by PSE related to the Colstrip Unit 4 assets. Any differences, including refunds or surcharges, due to the timing of the closing, will be trued-up in the following year’s Schedule 141 filing.

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[10] 26 CFR § 1.168(i)-3(b).

[11] Roberts, Exh. RJR-6, at 17-18.

IV. ACCOUNTING FOR THE DECOMMISSIONING AND REMEDIATION COSTS FOR THE GENERATING ASSETS ASSOCIATED WITH COLSTRIP UNIT 4

Q. How does PSE currently recover decommissioning and remediation costs for Colstrip Units 3 & 4?

A. Currently, PSE recovers decommissioning and remediation costs for Colstrip Units 3 & 4 through depreciation rates. Based on the best estimates available at the time of setting depreciation rates, PSE (i) included approximately $48 million in cumulative decommissioning and remediation costs associated with Colstrip Units 3 & 4 (*i.e.*, $24 million for Colstrip Unit 4) in the depreciation rates in Dockets UE-170033 & UG-170034 (consolidated) and (ii) proposed to increase this to approximately $73 million in cumulative decommissioning and remediation costs associated with Colstrip Units 3 & 4 (*i.e.*, $36.5 million for Colstrip Unit 4) in Dockets UE-190529, *et al*.

If the Commission were to approve PSE's updated depreciation rates in Dockets UE-190529, *et al*., PSE projects that, as of September 30, 2020, PSE will have collected approximately $10.7 million for decommissioning and remediation costs for Colstrip Units 3 & 4 (*i.e.*, $5.2 million for Colstrip Unit 4).

A. <u>PSE's Proposed Accounting Treatment for Remediation Costs for Colstrip Unit 4</u>

Q. What accounting treatment is PSE requesting for remediation costs for Colstrip Unit 4?

A. Utility plant associated with legal remediation costs are accounted for based on Accounting Standards Codification ("ASC") 410-20 Asset Retirement Obligations which are recorded in FERC account 230 Asset Retirement Obligations. As the underlying asset (Colstrip Unit 4) will no longer be property held by PSE, PSE proposes to account for the associated legal remediation liability, (i.e., the portion that remains with PSE per the Colstrip Unit 4 Purchase and Sale Agreement), under ASC 410-30 (Environmental Remediation) and recorded in FERC account 228.4 Accumulated miscellaneous operating provisions.

Accordingly, the net unrecovered legal remediation that is recognized as an Asset Retirement Cost in FERC accounts 101 and 108 under Asset Retirement Obligation accounting must be transitioned to an unrecovered environmental remediation asset. PSE estimates the amount associated with Colstrip Unit 4 as of September 30, 2020, will be $15 million. PSE respectfully requests this amount be included in a separate regulatory asset and amortized in the same manner as the unrecovered plant noted in Table 2 above. The proposed entries associated with this requested accounting are below and are based on the estimated unrecovered legal remediation as of September 30, 2020. Similar to the entries in Table 2, the accumulated deferred taxes would follow the book transactions.

Table 3. Requested Entries for Colstrip Unit 4 Remediation Costs

	FERC Account	Description	Debit	Credit
Cr.	101	Electric Plant in Service		$22 million
Dr.	108	Accum Prov for Dep	$7 million	
Dr.	182.2	Unrecovered Remediation	$15 million	

To record the unrecovered remediation as a regulatory asset.

Per generally accepted accounting principles ("GAAP"), the basis for valuing the legal obligation for the Asset Retirement Obligation in FERC account 230 is different than the basis for the valuation of the liability under environmental remediation accounting. Essentially, the Asset Retirement Obligation is recorded at a discounted value of the future legal obligation and an environmental remediation liability is recorded in nominal dollars. Therefore, upon transitioning the Asset Retirement Obligation to an environmental liability, there is a valuation adjustment that is recorded, as shown in Table 4 on the following page, based on the estimated Asset Retirement Obligation and environmental liability as of September 30, 2020:

Table 4. Requested Entries for Transitioning to an Environmental Remediation Liability

	FERC Account	Description	Debit	Credit
Dr.	230	Asset Rtrmt Oblig	$17.5 million	
Dr.	182.2	Unrecovered Remediation	$5.0 million	
Cr.	228.4	Accum Misc. Op. Prov. (Env. Rem.)		$22.5 million[12]

To transition legal remediation liability from Asset Retirement Obligation to Environmental Remediation Liability.

After establishing the unrecovered remediation regulatory asset and recording the associated valuation adjustment, PSE will amortize the net unrecovered remediation regulatory asset based on the amounts included in Table 1, as shown in Table 5 below.

Table 5. Requested Entries for Amortization of the Unrecovered Remediation Concurrent with Amounts Set in Rates

	FERC Account	Description	Debit	Credit
Dr.	407	Amort of Prop Loss	$2.7 million	
Dr.	182.2	Environmental Remediation		$2.7 million

To record ongoing annual amortization of regulatory asset through 2025 at $2.7 million annual amount reflected in Table 1.

[12] The actual amount will be equal to the nominal value of the legal remediation costs currently estimated by PSE after reduction for actual remediation spending. As noted further below, PSE just received conditional approval from the Montana Department of Environmental Quality for Alternative #4 of the remedy evaluation report filed for Colstrip Units 3 & 4. Therefore, the amount of the actual entry will change based on PSE's final assessment of the conditional approval.

B. <u>PSE's Proposed Accounting Treatment for Decommissioning Costs for Colstrip Unit 4</u>

Q. What accounting treatment is PSE requesting for decommissioning costs for Colstrip Unit 4?

A. Although PSE recovers decommissioning costs in a similar manner through depreciation rates, PSE would not include decommissioning costs in the regulatory asset because it would continue to be included in FERC account 108 Accumulated Provision for Depreciation. PSE respectfully requests that it be allowed to continue to accumulate decommissioning costs in FERC account 108 by recognizing the annual amount of $0.7 million of depreciation expense for decommissioning costs included in rates through 2025, the entries for which are shown in Table 6 below.

Table 6. Requested Entries for Colstrip Unit 4 Decommissioning Costs

	FERC Account	Description	Debit	Credit
Dr.	407	Amort of Prop Loss	$0.6 million	
Cr.	108	Accum Prov for dep (311 sub account)		$0.6 million

To record ongoing annual accumulation of decommissioning costs included in depreciation rates through 2025 at the $0.6 million annual amount reflected in Table 1.

Q. Why should the Commission allow amortization to continue after the sale of Colstrip Unit 4 if PSE has PTCs available to address undepreciated plant and decommissioning and remediation costs?

A. The amounts included for decommissioning and remediation estimates are based on the best available information known as of the date of filing of this Application and are subject to change as circumstances change. Although PSE projects $[redacted] million in remaining PTCs (if PTCs are used to offset the unrecovered balance of Colstrip Unit 4 when sold), this amount of remaining PTCs will be minimal considering that this amount would need to recover any unrecovered balance on Colstrip Unit 3 and decommissioning and remediation costs that exceed depreciation reserves for all four units and the Treasury Grants for Colstrip Units 1 & 2.

The Second Exhibit to the Prefiled Direct Testimony of Susan E. Free, Exh. SEF-3, provides a copy of the most recently submitted Colstrip Annual Report filed under Docket UE-170033. As noted in the report, the only cost estimates that have been conditionally approved by the Montana Department of Environmental Quality is Alternative #4 of the common plant site remedy evaluation report. Additionally, the remediation on Colstrip Units 1 & 2 has been separated into two phases. PSE and its co-owner of Colstrip Units 1 & 2, Talen Montana, LLC, have yet to determine and file the estimated costs for the second phase, which means that not all potential decommissioning and remediation costs have been identified.

Shortly before the filing of this Application, the Montana Department of Environmental Quality conditionally approved Alternative #4 of the filed remedy evaluation report for Colstrip Units 3 & 4. The communication from the Montana Department of Environmental Quality indicated that the total approved estimated decommissioning and remediation costs are $107 million. At this time, the details have not been made available to allow PSE to compare PSE's ownership share of the $107 million to the estimate used in Dockets UE-190529, *et al*. Nonetheless, PSE anticipates that it is possible that including ongoing amounts in PSE's rates to recover decommissioning and remediation costs through 2025 will not be sufficient to recover all of the estimated costs due to the fact that the conditionally approved amounts remain estimates that are subject to change.

Given the uncertainty regarding these costs, PSE should continue to build the depreciation reserves for the decommissioning and remediation as it will allow for the most flexibility in the source of funds used to fund decommissioning and remediation costs.

Q. Will PSE be able to track the amounts received for decommissioning and remediation?

A. Yes. PSE will be able to track the amounts received for decommissioning and remediation in order to preserve the ability for parties to audit both the recovery of and spending on decommissioning and remediation. This will allow the Commission, PSE, and stakeholders to (i) ensure that costs incurred by PSE were prudent, (ii) track the decommissioning and remediation costs recovered through depreciation, (iii) determine the amount, if any, by which incurred decommissioning and remediation costs exceed the decommissioning and remediation costs recovered in depreciation expense, and (iv) determine the necessity, if any, to use monetized PTCs to recover decommissioning and remediation costs not recovered in depreciation expense.

Q. What balances will PSE record in electric rate base?

A. PSE proposes to record the regulatory assets associated with unrecovered plant and legal remediation in electric rate base. The reserve for decommissioning is already included in electric rate base, and PSE respectfully requests that this treatment continue. PSE also proposes to record the environmental remediation liability as an offset within electric rate base.

PSE does not generally record future cost estimates of environmental remediation assets or liabilities within rate base. PSE, however, previously included Asset Retirement Obligation liability in the electric rate base. Therefore, PSE believes it is appropriate to continue this treatment, which will offset the regulatory asset associated with the legal remediation.

V. ACCOUNTING FOR THE SALE OF COLSTRIP TRANSMISSION ASSETS

Q. Will there be a gain or loss on the sale of the transmission assets?

A. The transmission assets that PSE proposes to sell pursuant to the Colstrip Transmission System Purchase and Sale Agreement would be sold at the net book value of those assets at the time of closing.[13] Therefore, PSE anticipates little or no gain or loss associated with the sale of assets pursuant to the Colstrip Transmission System Purchase and Sale Agreement, and PSE proposes that any gain or loss would be addressed in the same manner as any other gain/loss on utility property[14] and addressed in PSE's next general rate case.

Q. What are the costs built into rates for the transmission system assets proposed to be sold pursuant to the Colstrip Transmission System Purchase and Sale Agreement?

A. Similar to any other transmission asset, the cost of service associated with the transmission system assets is primarily the return on rate base for those assets along with the associated depreciation expense. The Colstrip Transmission System assets are treated the same as PSE's other transmission assets and are depreciated on the same schedule.

Q. Is PSE proposing to defer the recovery associated with these costs?

A. These assets are no different than PSE's other transmission assets. PSE proposes that no deferral is necessary because (i) the overall balance in transmission accounts continues to increase, representing amounts not in rates, and (ii) the

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[13] The Colstrip Transmission System Purchase and Sale Agreement includes an initial purchase and an option purchase closing date. The price of each sale will be based on the net book value just prior to the respective closing date. *See* Roberts, Exh. RJR-7.

[14] Gain/Losses on the sale of utility property are governed by Dockets U-89-5 2668-T, U-89-2955-T, Findings of Fact 19, and the Stipulation and Order of Dismissal dated May 26, 1992, Washington Court of Appeals No.29404-1.

difference between the net book value at the time of sale and the revenue requirement associated with these specific assets is minimal.

VI. ACCOUNTING FOR THE NORTHWESTERN ENERGY PURCHASE POWER AGREEMENT

Q. Please provide an overview of the cost components of the proposed NorthWestern Energy PPA.

A. According to the confirmation for the NorthWestern Energy PPA,[15] the contract price includes both a fixed and a variable cost component. According to the Uniform System of Accounts for electric utilities, PSE must charge the costs associated with the NorthWestern Energy PPA (both fixed and variable costs) to FERC account 555, Purchase Power,[16] an account included in PSE's PCA mechanism.

However, PSE's requested rates in Dockets UE-190529, *et al*. include approximately $18.6 million of production operations and maintenance costs associated with Colstrip Units 3 & 4.[17] These production operations and maintenance costs are not subject to the PCA mechanism. Therefore, PSE proposes that, on an interim basis, for purposes of calculating the monthly PCA

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15 *See* Roberts, Exh. RJR-8C.

16 18 CFR Part 101, FERC account 555, states, in part, as follows: "A. This account shall include the cost at point of receipt by the utility of electricity purchased for resale….. B. The records supporting this account shall show, by months, the demands and demand charges, kilowatt-hours and prices thereof under each purchase contract."

17 Associated FERC accounts are included in FERC accounts 500, 502, 505, 506, 507, 510, 511, 512, 513 and 514.

imbalance, PSE will include the amount of the Colstrip Unit 4 production O&M costs approved in rates as a credit to actual costs for purposes of calculating the PCA imbalance in order to align with the PPA structure. Such treatment would continue until the NorthWestern Energy PPA (and the sale of PSE's interests in Colstrip Unit 4) are reflected in general rates in a future general rate case.

Q. Is PSE recommending this as a permanent change to the PCA mechanism?

A. No. PSE is not recommending a permanent change to the PCA mechanism. PSE's proposal is merely to recognize that the sale of PSE's interests in Colstrip Unit 4 and the purchase of some of the output of Colstrip Unit 4 pursuant to the NorthWestern Energy PPA could have unintended consequences in the PCA mechanism. Aligning the costs established in rates with the change in the cost structure that occurs with the NorthWestern Energy PPA will allow PSE to offset costs with amounts included in rates and flow both through the PCA mechanism. This treatment will ensure that the PCA benchmarking will work as intended until the next general rate case where the costs can properly be aligned in rates.

Q. Does the accounting treatment of production operations and maintenance costs include the major operations and maintenance amortizations for Colstrip Unit 4 already in rates?

A. No. The major operations and maintenance amortizations for Colstrip Unit 4 that are included in PSE's existing rates are based on actual unit overhaul costs that occurred prior to the sale. Under the existing ratemaking structure for major operations and maintenance, PSE defers and amortizes these overhaul costs over a period of time that matches the time until the next major maintenance event; therefore, it is appropriate for the amortizations to be included in rates until PSE has fully amortized the costs.

Additionally, PSE's proposed rates in Dockets UE-190529, *et al*. include the Colstrip Unit 4 major maintenance event scheduled to be completed in June 2020. PSE will be responsible for the payment of its pre-closing share of these overhaul costs because these costs will be incurred prior to the closing of the Proposed Transactions. Regardless of whether the Commission approves PSE's or Commission Staff's proposal for the Colstrip Unit 4 major maintenance event in Dockets UE-190529, *et al*., the eventual deferred balance and any approved amortization should continue in base rates until the balance is fully amortized. In other words, the treatment of these events need not change as a result of the Proposed Transactions.

Q. Please explain the Third Exhibit to the Prefiled Direct Testimony of Susan E. Free, Exh. SEF-4.

A. The Third Exhibit to the Prefiled Direct Testimony of Susan E. Free, Exh. SEF-SEF-4, provides PSE's requested treatment of the production operations and maintenance costs in the determination of the PCA imbalance.

PSE has included in rates $18.6 million in production operations and maintenance costs for Colstrip Units 3 & 4 in Dockets UE-190529, *et al*. One-half of these costs ($9.3 million per year, or $0 8 million per month) are assigned to Colstrip Unit 4. Upon the closing of the Proposed Transactions, PSE will continue to pay a portion of these costs through the fixed cost component of the NorthWestern Energy PPA.

The amount to include in the PCA imbalance calculation for the production operations and maintenance costs will be based on the Colstrip Unit 4 share of the operations and maintenance costs built into current rates. This will ensure that PSE does not under-collect due to the previously fixed production operations and maintenance costs being re-characterized as power costs under the NorthWestern Energy PPA. If this accommodation is not made, PSE could inappropriately share the under-recovery of costs with customers if the under collection were to exceed the first $17 million sharing band.

The Third Exhibit to the Prefiled Direct Testimony of Susan E. Free, Exh. SEF-4, outlines PSE's proposal to create a new line in the PCA Exhibit B, which removes $0.8 million monthly (or whatever appropriate amount is approved in Dockets UE-190529, *et al.*) from Total Allowable Costs, commencing on the closure of the Proposed Transactions and ending when PSE can appropriately reflect this change in power costs and operations and maintenance costs in its next rate case.

VII. CONCLUSION

Q. Does this conclude your prefiled direct testimony?

A. Yes.