BEFORE THE WASHINGTON UTILITIES AND

TRANSPORTATION COMMISSION

WASHINGTON UTILITIES AND TRANSPORTATION COMMISSION, Complainant,	Docket No. UE-011570 Docket No. UG-011571
v.	Volume XVII Pages 2102-2228
PUGET SOUND ENERGY, Respondent.	

A settlement hearing in the above matter was held on June 17, 2002, at 9:38 a.m., at 1300 S. Evergreen Park Drive Southwest, Olympia, Washington, before Administrative Law Judge DENNIS J. MOSS, Chairwoman MARILYN SHOWALTER, Commissioner RICHARD HEMSTAD, and Commissioner PATRICK OSHIE.

The parties were present as follows:

PUGET SOUND ENERGY, by Markham Quehrn and Kirstin Dodge, Attorneys at Law, Perkins Coie, 411 108th Avenue, N.E., Bellevue, Washington 98004.

NORTHWEST ENERGY COALITION and NATURAL ENERGY RESOURCES COUNCIL, by Danielle Dixon, 219 First Avenue South, Suite 100, Seattle, Washington 98104 (Via teleconference bridge.)

AT&T WIRELESS, by Traci Kirkpatrick, Attorney at Law, Davis, Wright, Tremaine, LLP, 1300 S.W. Fifth Avenue, Suite 2300, Portland, Oregon 97201 (Via teleconference bridge.)

Barbara L. Nelson, CCR
Court Reporter

FEDERAL EXECUTIVE AGENCY, by Norman J. Furuta, Associate Counsel, Department of the Navy, 2001 Junipero Serra Boulevard, Suite 600, Daly City, California 94014-1976 (Via teleconference bridge.)

INDUSTRIAL CUSTOMERS OF NORTHWEST UTILITIES, by Bradley Van Cleve, Attorney at Law, Davison Van Cleve, 1000 S.W. Broadway, Suite 2460, Portland, Oregon, 97205.

THE COMMISSION, by Robert Cedarbaum, Assistant Attorney General, 1400 S. Evergreen Park Drive, S.W., P.O. Box 40128, Olympia, Washington 98504-0128.

PUBLIC COUNSEL, by Simon ffitch, Assistant Attorney General, 900 Fourth Avenue, Suite 2000, Seattle, Washington 98164.

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JUDGE MOSS: Let's be on the record. Good morning, everyone. We are reconvened in our proceedings styled WUTC against Puget Sound Energy, Docket Numbers UE-011570 and UG-011571. Our subject matter this morning is going to be the PCA. Let's do take brief appearances for the record, since we have 31 parties and we have a changing cast of characters each day, it seems. Ms. Dodge.

MS. DODGE: Thank you. Kirstin Dodge, with Perkins Coie, for Puget Sound Energy.

MR. QUEHRN: Good morning. Mark Quehrn, with Perkins Coie, for Puget Sound Energy.

MR. VAN CLEVE: Brad Van Cleve, for the Industrial Customers of Northwest Utilities.

MR. FFITCH: Simon ffitch, for Public Counsel.

MR. CEDARBAUM: Robert Cedarbaum, for Commission Staff.

JUDGE MOSS: Any appearances through the bridge line?

MS. DIXON: Yes, this is Danielle Dixon, with Northwest Energy Coalition, Natural Resources Defense Council.

MR. FURUTA: And Norman Furuta, Federal Executive Agency.

JUDGE MOSS: All right.

MS. KIRKPATRICK: Traci Kirkpatrick, for AT&T Wireless.

JUDGE MOSS: Any others? Okay, thank you. We have the appearances. We have two witnesses who have previously been sworn, Mr. Lazar and Mr. Lott, and of course you remain under oath. Mr. Story and Mr. Elsea, if you'll please rise and raise your right hands.

Whereupon,

JOHN STORY and JIM ELSEA,

having been first duly sworn by Judge Moss, testified as follows:

JUDGE MOSS: Thank you. Be seated. Did any of the witnesses have a prepared narrative that they wished to -- all right. We have another subject matter to cover first, so let's do that, and then we'll turn to that question that I was in the midst of asking.

CHAIRWOMAN SHOWALTER: I have one little set of questions on time of use, which I'd like to ask now, so we can then move on to the next subject. And maybe Mr. Pohndorf could come to the table here, and the other witnesses are still empaneled. And I will send this out as a bench request, anyway, but I wanted to understand your oral answers first, in case it triggers some other question.

The question I had last Friday was are the meters of customers who are not on time of use tariffs, but who are equipped with time of use meters read four times a day, that is, for PEM-only customers who are not TOU customers, are their meters read four times a day, and if so, can those PEM-only customers get on the Internet and read their daily use in blocks of time?

And Mr. Pohndorf, I think you weren't certain of the answer and you may not be today, but depending on what your answer is, I have another question.

MR. POHNDORF: Okay. Let me tell you my understanding as it is. We have a very large number of customers who have the advanced meters installed, and then there is a subset of those customers where we have the network set up that transmits that metering information in such a way that they can be read four times a day. There are customers who we are reading four times a day who are getting the information kind of out of that subset.

CHAIRWOMAN SHOWALTER: Who are not TOU customers?

MR. POHNDORF: Who are not on the time of use program. In fact, I'm one of those customers. I get the information, but I don't get the time of use billing. They can, as I understand it, those customers who are getting the time of use information on their bill, like me, can get on the Internet and check their usage four times a day.

CHAIRWOMAN SHOWALTER: Okay.

MR. POHNDORF: Or check what it is over those blocks. I guess they can check it as many times a day as they want.

CHAIRWOMAN SHOWALTER: All right. Then my next question is relevant. And that is are all of the directly assigned time of use charges, i.e., the dollar-sixteen a month after removing the ten cents recovered from the conservation rider, are all of those time of use charges solely attributable to the incremental cost of the time of use program? For example, billing for time of use or recordkeeping required for time of use.

And conversely, are the costs associated with personal energy management, but not TOU, for example, the meter reading we talked about or the data processing or the Web page information, are all of those costs fully recovered from general revenues?

What I'm trying to get at is are the proposed new costs for TOU customers only for costs that they only receive -- or for services they only receive as a TOU customer versus anything that they might also receive as a PEM-only customer?

MR. POHNDORF: Mm-hmm. Yeah, I think I understand the question. First of all, that dollar is, as I understand it, a meter reading cost, so that dollar would apply -- it would be a cost to the company from Schlumberger, whether you're a time of use billing customer or the information customer. Then there are the other 26 cents, and I don't know how much of those 26 cents are -- is fully required for ultimate billing and how much of that is data handling that would apply, as well, to the information-only customers.

I think maybe at the heart of your question is that if we recover the $1.26 for the time of use billing customers, are we recovering any of the incremental cost to do the information-based program, because how we have it set up right now is we are recovering the $1.26 for the customers only -- for only the customers who are on the time of use billing.

CHAIRWOMAN SHOWALTER: Under the proposal.

MR. POHNDORF: Under the proposal. Yeah, under the proposal. And what happens with the cost to metered customers who are only on the PEM information, is that in the revenue requirement. Is that --

CHAIRWOMAN SHOWALTER: Yes, that's one way to put the question.

MR. POHNDORF: Yeah. It's my understanding that cost for the information-only customers is not being recovered, but that's just my understanding. I don't know if, Mert, you have a different understanding.

MR. LOTT: Well, I can explain my understanding. My understanding, Chairwoman, is that currently there are information-only customers. If the company wants to continue providing customers with that information, it is not included in the revenue requirement. It's been our assumption that they would provide the information probably not to all the customers that they have been providing it to currently.

That does not stop the PEM program, because the PEM program was there before these four meter reading -- four-time-a-day meter reads and it will continue. In other words, the Web site is there and the ability to go in and check whatever -- I'm not a customer, so I've never checked this, but will be in two months. But the PEM program continues, but the time of use portion of that, unless the company volunteers to do that, and I seriously doubt that they'll spend $1.26 where they can't get revenue to continue it, so I would imagine that, for the most part, the customers who are getting information only will stop getting those four-time-a-day meter reads, would be my understanding.

In other words, there are automated meters out there that will be read the once a month along, you know, where they record the once a month as a permanent reading. Now, I'm not sure exactly what's included in the PEM program, other than I know that when I went up there and looked at -- a long time ago, this is about three to four years ago, when we went up there and looked at the automated meter reading and we went online and we looked at the information, there was timely information on the Web site that I saw related to that particular customer that we were looking up, but that was not this four-time-a-day recorded information and --

CHAIRWOMAN SHOWALTER: Well, that seems at odds with Mr. Pohndorf's testimony that he's just given. I guess there are a couple of questions. Not a few months ago, but today, if I get on the -- I happen to be a time of use customer, but if I were not, but I had -- let's say I'm a time of use customer who then gets off, because -- then will I or won't I today be able to pay to get on the Internet and see my four-times-a-day use?

Another issue has been introduced, which is does the company have plans to abandon the four-times-a-day meter reading for PEM-only customers?

MR. POHNDORF: Let me take both parts of that question. As I understand it, the company has these various buckets of customers. One bucket of customers are the current time of use billing customers. There's another bucket of customers who are the time of use information-only customers. If you opt out of the time of use billing, I'm not certain as to whether you go into that time of use information-only or you just fall off and you don't get time of use information. So I don't quite know the answer to the specific question there.

As far as the company's plans are concerned, I know this is a question that the company is still sorting through, what do we do with all these information customers. Do we continue to provide them information over the Internet and through their bills, or just what do we do with the information-only program, and we have not come to a conclusion on that yet.

CHAIRWOMAN SHOWALTER: But in terms of what the general revenues will cover --

MR. POHNDORF: Yeah.

CHAIRWOMAN SHOWALTER: -- can you answer definitively whether or not they do cover the information-only activities?

MR. POHNDORF: I would say that there are certain activities involved in the information-only program, such as maybe promotional materials, general Web site costs, those sorts of things that are recovered through the revenue requirement. I don't believe that the incremental meter reading cost to get the four-times-a-day information for the information-only customers, I do not believe that that cost is covered in the revenue requirement.

CHAIRWOMAN SHOWALTER: Okay. I think that at least informs me and we'll issue a bench request, anyway, on it. And you now understand what I'm getting at, so --

MR. POHNDORF: I think that's a good idea, because others will be able to give you more specific information through that data request.

CHAIRWOMAN SHOWALTER: Thank you.

JUDGE MOSS: All right. Then, turning back to the purchase cost adjustment mechanism, I was asking if any of the witnesses had a prepared opening narrative statement or if we can just launch right into our questions.

MR. LOTT: The answer was, as far as I know, nobody has an opening statement.

JUDGE MOSS: Okay. Thank you, Mr. Lott. So we're ready for questions from the bench.

CHAIRWOMAN SHOWALTER: Well, maybe we could begin with the mechanics of the PCA and how it works, and you could start to take us through that. I think we understand there are different bands, but let's start first with -- we understand that the sharing bands represent annual figures, and the examples included in the Exhibit C to the PCA agreement appear to be based on annual calculations. First of all, is that correct?

MR. LOTT: Yes.

CHAIRWOMAN SHOWALTER: And then, is the comparison of the actual cost to base cost done annually, monthly, or daily?

MR. LOTT: It would be done on an annual basis. The company, for bookkeeping purposes, would estimate as they went through the year, but it would be done on an annual basis. So you would not run into a question about shaping of cost in particular months versus the actual cost in a particular month.

MR. LAZAR: There is one exception to that, which is if, on a forecast basis, is it expected that there will be very high power costs, a more rapid filing mechanism is provided for. That is there sort of to anticipate a power crunch type situation where it might be desirable to have a surcharge rate in effect during a drought so that customers respond as the drought occurs, rather than wait till the end of collection of annual data.

That's the only exception, is if there's a forecast of a $30 million bulge or deferral amount.

CHAIRWOMAN SHOWALTER: Okay. And where is that forecast?

MR. LOTT: I just want to make something clear. That still does not change that the deferral will be calculated on an annual basis. The company doesn't have to wait for the final deferral and can file ahead of time on an estimated basis, but the deferral would still be on an annual calculation.

And that's -- did you get the reference number?

MR. LAZAR: Yeah, the reference is the second bullet on Point Four, which is on page two of the settlement.

CHAIRWOMAN SHOWALTER: Okay. So there's a projected increase in the deferral balance, but the deferral balance is still whatever it is and is adjusted annually?

MR. LOTT: That's correct.

CHAIRWOMAN SHOWALTER: Okay. So when are the debits and credits to the deferral account done? Are they done annually or do they occur monthly or daily and then you find out what happens at the end of the year?

MR. LOTT: What do you mean by debits and credits? You mean what's actually entered on the company's books? I mean, to me, that's debits and credits. What I would assume is that every month the company will make estimates about whether they are -- whether there's a need to start or a right to start accruing an asset or a liability on their books depending on what's going on in that particular year. So at the end of July, they'll look at it and say, Huh, yeah, we're within a dead band probably, so we won't defer anything. But if something extraordinary starts to happen and it looks like they're going to have a deferral, they would probably, in some fashion, figure out a methodology to accrue a deferral or liability on their books.

Okay. At the end of the year, June 30th, you would now have a full year. You could calculate the actual balances. You would true up any of those monthly entries you may have made approaching that time frame, and you would then make the filing that the company would submit by -- I think it's at the beginning of August. Staff would -- Staff and other parties would review that deferral that was calculated for the year ended June 30th and bring it in front of the Commission for acceptance, whether there was any dollars in it or not.

But that would be the intent, is that by June 30th, the numbers -- or it takes the company a month, of course, to do their accounting, but at the end of June 30th, the actual deferral for the whole year would be calculated and then brought to the Commission for final acceptance.

MR. STORY: John Story, for the company. I agree with Mert. This is a yearly adjustment and we will true it up at the end of the year. But during the year, each month we will make the estimate and book something on the financials.

CHAIRWOMAN SHOWALTER: Okay. And so -- let's say mid-year, you appear to be exceeding the $20 million cap. Am I right that, technically, you don't exceed it until the end of the year, if that should prove to be the case?

MR. STORY: That's correct.

CHAIRWOMAN SHOWALTER: On the other hand, if you project that it will be exceeded early in the year, you have a right to come in and trigger a -- try to get a surcharge approved based on that projection?

MR. STORY: Well, the trigger for the surcharge is 30 million deferred.

CHAIRWOMAN SHOWALTER: I'm sorry.

MR. STORY: The 20 million, we would look at that, anyway, just to see if we should have a deferral put on the books. And you're correct, we would look at the remaining part of the year and try to true up the estimate.

CHAIRWOMAN SHOWALTER: Maybe we could turn to the examples that you've provided us that show how this would work in a typical and an unusual year or set of years, and just walk us through it. First of all, just tell us where it is.

MR. LOTT: You're trying to look at, like, Exhibit C; is that what you're referring to? Or do you want to go through all the calculations Mr. Elsea created here that fall into his calculation of an annual deferral?

CHAIRWOMAN SHOWALTER: Yeah, Exhibit C is --

MR. LOTT: Exhibit C is intended to demonstrate how the $40 million cap, the cumulative cap would work. And it tries to show it under various scenarios of actually exceeding that $40 million cap and what the company would be then liable for once they exceeded the $40 million cap. I'm looking at Example One. I just want to make sure everybody's looking at Example One.

CHAIRWOMAN SHOWALTER: Is everybody on Example One?

MR. LOTT: Just trying to -- Jim, you want to --

MR. ELSEA: Sure. The place to start on Example One of Exhibit C is line 16, column C, where you see the credit for 5.83. That is the difference between the allowed level of power cost and the normalized level that's going to be set for this settlement. And that's 5.83 million, and that's on an annual basis. So that number came from Exhibit B, and we can go back to that, if you'd like. But so for the first year --

CHAIRWOMAN SHOWALTER: Can you just go over that again, the allowed level and the normalized level?

MR. ELSEA: Yes. It might be helpful to turn back one page to Exhibit B.

CHAIRWOMAN SHOWALTER: Okay.

MR. ELSEA: The nature of the PCA is to calculate the difference between actual -- or what we've called actual and allowed power costs and the normalized level that's set in rates. And the allowed power costs are in lines four through 28, and it starts off with the fixed component and the return on our production rate base in line five, and then other fixed costs, which include items such as production O&M, property taxes. And that level of cost out into the PCA periods will not change from the normalized level that was agreed to as part of the revenue requirements in this settlement. So those numbers won't change from period to period as we're calculating the PCA deferral.

Lines nine through 16 represent variable components of the allowed power cost, and they will change. They will be based on actual bookings for the year. So we're adding up the fixed components, which don't change, the variable components, which will be a result of actual conditions through line 18, and that's the subtotal, and then there are some adjustments that were agreed to in the collaborative related to prudence, Colstrip availability, contract prices and new resources. And that comes down to line 28, which is a total allowable cost, and we're comparing that total allowable cost with the normalized baseline costs that were in this settlement. And the normalized baseline rate can be seen there on line 31. It's the $44 per megawatt hour, $44.463 per megawatt hour. That normalized rate is multiplied times our actual delivered megawatt hours during this PCA period to come up with a baseline normalized cost.

CHAIRWOMAN SHOWALTER: So just so I know which way this is going --

MR. ELSEA: Okay.

CHAIRWOMAN SHOWALTER: -- does this mean that, in this particular example, the total allowable costs were less than the baseline power costs, because line 28 is less than line 31, and does that mean that, in this example, the company didn't need

to spend as much money as the baseline would provide
for?

MR. ELSEA: That's correct.

CHAIRWOMAN SHOWALTER: So was this a good
month or time period for the company?

MR. ELSEA: Actually, if I looked at this
example, I would say that, except for the Colstrip
adjustment, this month was just about as forecast.
But it appears that there was a penalty on Colstrip
in the example that we've done, which created this
credit, which looks like our costs were lower, but
really it's saying our allowed costs are lower.

CHAIRWOMAN SHOWALTER: All right. Well,
maybe good is not a very good term.

MR. ELSEA: Right.

CHAIRWOMAN SHOWALTER: But in --

MR. LOTT: Absent looking at those
adjustments between lines 21 and 24, the company's
costs were below those that were pro formed into this
rate case. But, I mean, Jim is referring back up to
the adjustments on lines 21 to 24, so the
quantitative -- or qualitative statement good doesn't
necessarily apply, because you have to look at what
those adjustments were for.

CHAIRWOMAN SHOWALTER: Right. But given

the assumptions that are going into what is baseline in this particular time frame that they didn't -- the costs did not get up to baseline; is that correct?

MR. ELSEA: That's correct.

CHAIRWOMAN SHOWALTER: All right.

JUDGE MOSS: Just again, for the clarity of our record, that was Mr. Elsea you were referring to as Jim. We have two Jims, even on this witness panel, so it's potentially possible that our record will not be clear if we don't use surnames.

MR. LOTT: Yes, I'm very bad at that. I'm sorry.

CHAIRWOMAN SHOWALTER: All right. Keep going.

MR. ELSEA: All right. So as you pointed out, line 33 is the difference between the baseline costs on line 31 and the allowable costs on line 28, and because that $5.8 million is a credit, that is -- and I'll just go ahead and use your term, it is to the good. Our allowed costs were less than our normalized costs set in rates.

And the lines 37 through 40 are there to show how that difference of $5.8 million of credit would be shared between the customer and the company. And because that 5.8 million is within the dead band of 20 million, there is no amount that flows to the customer on line 43. But the total difference of 5.8 million is important, so that's the company's share, is the 5.8 million credit, and that does flow to Exhibit C.

CHAIRWOMAN SHOWALTER: And this page that we're looking at, Exhibit B, is the annual exercise?

MR. ELSEA: Yes, it is.

CHAIRWOMAN SHOWALTER: So 5.8 million is within the $20 million dead band. Now, then, what did you say does happen to the 5.8? I understand it goes over here as a credit, but --

MR. LOTT: Now, because the $40 million cap, he carries it forward to Exhibit C, so now turn to Exhibit C, column C, line 16.

CHAIRWOMAN SHOWALTER: Okay. And I think, just so -- I think I understand where this is going. Tell me if I'm right. That the 5.8 million does not exceed 20 million, so nothing is done about it at that time. However, the 5.8 million does count against the cumulative $40 million cap.

MR. ELSEA: That's right, yes.

CHAIRWOMAN SHOWALTER: And that's what we're seeing on the next page, Exhibit C?

MR. ELSEA: That's correct. And that's why it's important to be looking at both the company's share and the customer's share, because the company's share will be measured against that $40 million cap, and it is a cumulative over the four-year period.

CHAIRWOMAN SHOWALTER: Okay.

MR. LOTT: Yes. So now you're at column C, line 16, the $5.83 million. That is also in column G, which was the company's share of that amount, and it's also for the cumulative cap in column J. And it's also in column K, because that is the cumulative cap without the cap. In other words, if there hadn't been a cap, that's what the balance would be. Since that's the first year, it's spread into each one of those columns.

CHAIRWOMAN SHOWALTER: Commissioner Hemstad, did you have a question?

COMMISSIONER HEMSTAD: Well, I think I'll hold my question, which is a more generalized one, until later.

MR. LOTT: Second thing Mr. Elsea did was to assume, in the second year, that the result of Exhibit B was a $30 million number. You can see that on line 17, column C.

CHAIRWOMAN SHOWALTER: And what does that mean?

MR. LOTT: That means that the company had a bad year.

CHAIRWOMAN SHOWALTER: I see.

MR. LOTT: And the cost exceeded -- the cost exceeded the baseline by $30 million. That $30 million was spread between the customers and the company, based on the formulas that are in Exhibit B again, but that's the five million and the 25 million you see is in column D and column G.

CHAIRWOMAN SHOWALTER: And now, why is the 30 million divided by five and 25?

MR. LOTT: The first 20 million went to the company, the second ten million was split 50/50 between them, so you had five million to the customers, 25 million to the company. For the cumulative cap, with the cap number, you take the 25 million and subtract the 5.83 million and you get the 19,170,000 shown in column J. And since that's not in excess of the $40 million cap, you have the real company share shown in column K of the 19,170,000.

CHAIRWOMAN SHOWALTER: And when we say share, the company's share --

MR. LOTT: The company --

CHAIRWOMAN SHOWALTER: -- what do we mean?

MR. LOTT: The company's income statement has absorbed that loss. That would be -- that would have been flowed through their income statement. That's what their earnings per share that they would include to their stockholders would include.

CHAIRWOMAN SHOWALTER: All right.

MR. LOTT: This is before tax, of course. The company would get the tax benefits of those. This example continues, then, trying to get to this particular case, so in -- on line 18, year three, he added another $30 million, it's another poor year, two poor years in a row. And again, the sharing between those would have been what's shown in columns D and G, a five million and 25 million. But as can be seen over in column K, 25 million took the company over their $40 million cap.

Mr. Elsea, I think, can better explain exactly, then, how he calculated the cumulative percentage -- I mean, the cumulative dollars, but in essence, once he got to the $40 million cap, he then took one percent of that dollars -- once he exceeded the $40 million, he took one percent of this company's share and put that into -- so he took the one percent of the $4,170,000 shown in column H, and he put that into the company's share. And so when you add the 25 million, which was the company's share, subtracting the $4.17 million in column H, which was that over the cap, and then added back one percent of that amount, you then get to the total of 40 million-oh-four, or 40,000 -- $40,040,000 shown in column J, and that would compare -- so the company now has exceeded their cap, and the ratepayers are going to pay the difference between -- would pay the difference. And the ratepayers' share, the difference between the J and the K, instead of just continuing to apply the annual sharing band.

CHAIRWOMAN SHOWALTER: Which is L?

MR. LOTT: Actually, I don't -- no, because it should only be 4.13 million is the difference, so -- L is just how much you're over the cap, over the 40 million cap using the normal annual sharing.

CHAIRWOMAN SHOWALTER: So the 4.13 is just not shown here because that's a different mechanism?

MR. ELSEA: Actually, it shows in column E.

CHAIRWOMAN SHOWALTER: Oh, yes.

MR. ELSEA: Columns D, E and F are the customers' portion.

CHAIRWOMAN SHOWALTER: Right.

MR. LOTT: Okay, now --

CHAIRWOMAN SHOWALTER: Just so I understand, this is just what happens to an assignment of burdens between the shareholders and the ratepayers. It doesn't describe itself a triggering of a rate change, or does it?

MR. LOTT: No, this doesn't. The triggering of the rate change is written into the documents. The company will be allowed to file -- after one of these annual filings, they'll be allowed to file when they're around $30 million or more. Again, we don't -- if they're 29.7, we don't want to say you're not around your $30 million. But when they're around $30 million, they will file a tracker. Or in the instance that -- for example, last August, when they knew that they were in trouble for this coming winter, they would have probably filed a tracker at that time based on the estimates for the winter of 2001-2002.

So there's two circumstances that will cause the company to file for a tracker. One is when their cumulation gets over this $30 million number, or two, when they think and they have good reason to think that they're going to be above the $30 million in the near future and it's a good time to tell customers that there's a problem. We don't have hydro, we're going to have high costs.

And that, to us, was very important. You know, going back to previous Commission orders, it's a good idea to have a reason to tell the customers, you know, there's a problem out here. You know, you can help us by -- because the hydro is bad or prices are wrong.

CHAIRWOMAN SHOWALTER: Okay. Just tell me if this is conceptually right. What I envision is an annual exercise, and then also a cumulative tracker. And on the annual exercise, I envision a bell curve, which shows a dead band of 20 million at the center of it, plus or minus, and then that bell extends out for other increments, and in the center of the bell curve, the company accepts all of the cost or benefit, and as the bell curve extends out, the company takes a smaller and smaller proportion of either the cost or benefit until you get out to a one percent -- one to 99 percent ratio, is it, or is it just the five and 95?

MR. LOTT: No, it's actually the five and 95. I'll tell you that we kind of designed the PCA pre this $40 million cap. But the company was having problems with this first four-year period, and so kind of look at the two things as separate.

The $40 million cap explained in Exhibit C is kind of separate from the long-term PCA mechanism that we have, and the attempt in Exhibit C was we were looking at -- Staff was looking at probable hits to the company. In other words, we didn't expect the company to be sitting out here getting banged for $50 million a year, but the company was very concerned about that, as you heard Mr. Gaines talk the other day. And when the company proposed trying to limit their risk during this equity building period, it seemed like something that Staff and Public Counsel had little problem accepting that consideration and realizing that we needed to get them through this first four-year period.

So it is like one cap laid on top of another mechanism. The mechanism, as we designed it, was without the $40 million cap, and the $40 million cumulative cap was laid on top of it with an intent to help the company achieve their equity ratios during that first four years.

CHAIRWOMAN SHOWALTER: All right.

MR. LOTT: That's how I kind of view it, is everything besides the $40 million cap was one design and the $40 million cap was laid over the top of it in order to protect the company from, you know, from the problems during that first four years.

CHAIRWOMAN SHOWALTER: But, well, just keep telling me if my concept is correct or not. I envision this bell curve exercise going on every year.

MR. LOTT: Yep.

CHAIRWOMAN SHOWALTER: And we see where in the bell curve the assignment of responsibility is. And if it's within the $20 million dead band, it's all assigned to the company and we go out the bell curve, but at the same time we're doing that four bell curve years in a row, we're keeping track of how much to the bad the company has accepted or -- including anything in the $20 million dead band each year; is that correct?

MR. LOTT: That's correct.

MR. STORY: That's correct.

MR. ELSEA: I'd like to help you clarify this by looking at the fourth year on Exhibit C, because each of the first three years, at lines 16, 17 and 18 are just as you described, the bell curve, we shared the $30 million between the company and the customer. In the fourth year, there was another year with $30 million of cost overrun, if you will, and in that case, when you do the bell curve sharing and move $25 million to the company, which is in column G, that exceeds the cap -- not only does it -- well, the cap was exceeded the year before, but not only does it exceed the cap in that year, but if you look at column F, that's the cumulative deferral balance. And column F will show you that, yes, we can see that year four is going to put us over the $30 million trigger, and if we anticipated year four from the beginning, we would be able to put a surcharge on rates to be able to have people control their usage and possibly help us lower costs during that period. So I think the fourth year serves as a good example of what you were talking about.

CHAIRWOMAN SHOWALTER: Okay. So if you look at the -- by the end of the third year, you've gone just over the $40 million cap; correct?

MR. ELSEA: Right.

CHAIRWOMAN SHOWALTER: But by the end of the next year, you're at the $40 million cap, but there is an extra, you know, $30 million or so that needs to be covered somehow. So where in this process either would there be a trigger for a surcharge or could there be a trigger for a surcharge?

MR. LOTT: Looks like it would be at the end of year three, when the cumulative deferral would be over $40 million. Therefore, it's obviously over the $30 million. So the company would be filing a surcharge -- wait a minute, I'm looking at the wrong space. It's at the end of the year four. I'm looking at the wrong column. So someplace either at the end of year four or someplace during year four, when the company realized that that was going to happen.

CHAIRWOMAN SHOWALTER: And what line are you calling year four, 19?

MR. LOTT: Year four, that's line 19. You see the balance, the deferral balance goes up -- in column F, as Mr. Elsea was explaining the $43.88 million is the deferral balance to be recovered. So either at the end of year four or sometime during year four, when the company knew that this was going to happen, the company would have filed a deferral filing.

CHAIRWOMAN SHOWALTER: Okay. Now let's assume that that happens and there is a surcharge to collect some or all of that expected $30 million, that is, the amount in column K that exceeds the 40 million, or might it be more than the $30 million?

MR. LOTT: Well, they might have filed -- let's say the company -- say the company really thought things were really going to be bad, and they filed for $70 million. And --

CHAIRWOMAN SHOWALTER: Actually, but I guess this is one of my questions. Is the entitlement -- or I don't know if it's entitlement or expectation. Is the expectation that the company will collect only the amount that exceeds 40 million, or that once you get up to 40 million, you kind of go back into the 40 million and start collecting some of it?

MR. LOTT: You try to bring the deferral balance back to zero, or close to zero. So the company, at the end of year four, would file a case for $43.88 million.

CHAIRWOMAN SHOWALTER: And where did -- oh, I see.

MR. LOTT: That's the balance in column F. So the company would actually make a rate filing to recover their full deferral balance at that time.

CHAIRWOMAN SHOWALTER: All right.

MR. LOTT: Now, they may have made an estimated filing before that, but if they waited until the end of year four, saw this result, they would file for the whole $43.88 million.

CHAIRWOMAN SHOWALTER: So at that point, let's say there is a surcharge, it's to collect

43.88, does any of that revenue count against or offset a $40 million cap going forward, or once you're at 40 million, you're at 40 million, and basically anything else that's added must be added, although there would be the possibility, I guess, of some good years that would subtract from it.

MR. LOTT: The $40 million cap is the company's absorption of cost, not deferral. It helps create the deferral. In this case, the deferral has been changed by about $26 million because of the $40 million cap. At the end of the four-year period, the company has -- so now the $40 million cap has ended, the company has full right to receive the full $43.88 million.

CHAIRWOMAN SHOWALTER: I see.

MR. LOTT: If that result had happened a year earlier, there would be some concern that the cumulative cap might reverse some of the deferral, because the company might have a decent year and things might reverse, but, in this particular case, because there's no question about it, 100 percent of the $43.88 million is the company's money, and there's -- and it could go the other way. If these numbers were reversed, it would be the ratepayers' money. There would be no question about it. That was a deferral.

Once the normal bell curve, the annual bell curve numbers are calculated, absent the $40 million cap, those deferrals are the company's money to collect. There's just an agreement that they would wait to file until a trigger balance of approximately $30 million was reached. And again, it's -- an important column is the column F, and that's the column -- that's the column that will trigger a deferral filing.

CHAIRWOMAN SHOWALTER: All right. And I think you answered this question just now, but I'm just going to ask it again. In this Exhibit C, it just so happens that it did take four years to reach the $40 million cap, and the $40 million cap is a cap for a four-year period under the agreement, but if the $40 million cap were reached in the year two at the end of year two, and the surcharge were triggered, then the whole thing simply happened in the first two years; is that correct? And in year three --

MR. STORY: Actually, if you look at --

CHAIRWOMAN SHOWALTER: -- there's no cap, because you already absorbed the 40 million?

MR. LOTT: I'm looking at Example Three,

Chairwoman. Is that a good one? Or Four. Three or Four. They're kind of the reverse of each other, so let's look at Four, since that's the one where the company would be charging a surcharge.

MR. STORY: Example Three.

MR. LOTT: You're right. Example Three is the one they'd be charging the surcharge. Sorry. In Example Three, you can see these are all just numbers Mr. Elsea projected in his run. So the first year he has a bad year of $30 million, which the company had to absorb 25 million. The ratepayers -- there would have been a $5 million deferral that would be sitting on the company's books with the company having full right to recover that $5 million. No questions.

The second year, we had an extreme year, similar to last year. There was a hundred million dollar extra cost. Under the proper scenario, without the four-year cap, the ratepayers would have paid $64 million of this balance, the company would absorb $36 million. Unfortunately, that $36 million now crossed over the four-year cap by $21 million.

CHAIRWOMAN SHOWALTER: When you said the ratepayers would have paid, did you mean that --

MR. LOTT: No, would have absorbed. That means on the deferral side. So if you look at column

D.

MR. STORY: Assigned.

CHAIRWOMAN SHOWALTER: They are responsible for that.

MR. LOTT: Assigned. Responsible's a good word.

CHAIRWOMAN SHOWALTER: Okay.

MR. LOTT: Okay. They would have been responsible for 64 million out of the hundred million dollars, but they're going to get more than that. And the reason why they're going to get more than that is, assuming this $40 million cap -- remember, that's four-year cumulative, so you really don't know what the balance of that is going to be until the four years is up, but there is what is shown in column H and I as reductions in the company's portion, therefore increases in the ratepayers portion, and column I is then the one percent of the column H amounts, and that's why, in column E, you see 20.8 million, and that's -- that is column H and I being transferred over to the customers, because the company's exceeded the cap.

Now, there's two things that happen in this year. Number one, the $40 million cumulative cap has been at least temporarily exceeded. Number two, the

$30 million balance was exceeded, as you can see by column F, showing $89.8 million. Even without the cumulative cap being exceeded, $30 million was exceeded. The company would obviously, sometime during year two or at the end of year two, file for a deferral mechanism to recover all or most of the $89.8 million. They may be very careful about collecting the portion that's in column E, because that could reverse on them, but they would definitely recover $69 million at that point in time, and I think that they would probably file for the full $69 million. They might file for more than $69 million. And that's what would be filed for at that time.

CHAIRWOMAN SHOWALTER: All right.

MR. LOTT: But there's two caps being exceeded there. Number one is the $30 million trigger. It's not really a cap, but the $30 million trigger. In other words, the deferral was exceeding $30 million, and that's what has them file a rate proceeding.

The other cap, which is the cap, which is the four-year cumulative cap, is they exceeded their $40 million share, as can be seen by adding lines 42 and 43. Those two numbers add up to 51 -- 61. Boy, I'm good today. Sixty-one million dollars, so that's why they're $21 million over that cap, and they only take one percent of that portion, so that means they, as shown in column I, are responsible, then, for $200,000, which shows that the company's total share of cost at that -- in column J, is at $40,200,000.

CHAIRWOMAN SHOWALTER: All right. And so in this scenario, things get better in the fourth year.

MR. LOTT: Yeah, it kind of flip-flopped, and this is kind of important, because the cumulative cap, remember, runs through the full four years. It's possible that in one year they exceed, as they did in both years two and three, shown on lines 43 and 44, but in year five -- I mean, four, then the company has reversal of that amount, and you see in column H the $36 million number.

And so basically, in that last year, the company is going to absorb most of the costs -- I mean, the ratepayers are going to get most of the benefits back, not all. I mean, you can play around with these numbers. If you have an exceedingly good year in that last year, you could have actually had a full reversal of all prior -- of all prior amounts over the cap. In this case, we still were left slightly over the $40 million cap, as can be seen in column J.

CHAIRWOMAN SHOWALTER: But if J happened to be under 40 million, let's say it was 35 million, then what happens?

MR. LOTT: Yeah, in other words, this number over here became 120. I played with that just one time and it made that number negative 120. Now your total cumulative cap would have been un -- there's a -- remember I told you originally when they, back in year two, they had a deferral balance showing of $89.8 million there in column F, but 20.8 of that had to do with them exceeding their cap? If you had this huge turnaround in the fourth year, that's why they need to be careful that -- there's no ban on them filing for it, but that's why they need to be careful in years one, two, and three about filing for some of that cumulative cap, because it could potentially reverse, and then they would owe money back to the ratepayers, because they charged for something that now did not exceed the cumulative cap.

CHAIRWOMAN SHOWALTER: Okay. Stop right there. Let's say they did do the surcharge that did cover that original 20 million and now there's a big reversal and now it's under 40 million at the end of four years. Where is it in the agreement that shows that that is owed back to the ratepayers?

MR. LOTT: Well, it would come out, and Jim -- I mean, Mr. Elsea has calculated these things correctly. Remember, at no place in the schedule does he show when the company's actually going to file for rates. We would be looking in this calculation at the actual year-to-year numbers and accumulate the totals. So when you go down, what is the customers' responsibility over this period of time, you can see that in column F, Mr. Elsea has properly calculated at the end of those four years, $25.9 million.

Now, if the company had actually gone out and collected $80 million back in year two because of the severe situation that struck the company, then the company would be owing -- let's assume they collected $80 million. The company, instead of having a deferral of $25.9 million in there, in other words, since they would have had a big credit that would have been received from the customers, let's say 60 million, as I said, this balance would be now a credit of 35 million. Instead of an asset for the company, it would be a liability to the ratepayers of 35 million, and the company now would have to refund.

So if they -- you would have a refund at that point in time to the customers because of this reversal. And part of that reversal is a reversal of the $20.8 million that was accrued in column E because they exceeded the cap. And you know, it's -- these four years are all going to play together in that calculation.

And again, there's nothing to stop the company from filing 89.8 million. In fact, I would expect that they would file for something very close to that.

I mean, we created a rather severe situation here, one year that exceeds costs by a hundred million dollars, and then, two years later, it -- they are below the projected cost by a hundred million dollars, just to show you how extreme that is in the weather normalization adjustment, standard deviation. In other words, where two-thirds of the population fall is only $20 million from the center line, so you're talking about something five times one standard deviation to get to those two years that are included in this example.

So these examples are put in here to show what would happen in these strange things. I just want to point, strange things do happen. Look at the last two years, so --

CHAIRWOMAN SHOWALTER: Okay. Is the answer to my question on page two of the settlement agreement, third bullet?

MR. LAZAR: Yes.

MR. QUEHRN: Yes.

CHAIRWOMAN SHOWALTER: Where the sentence reads, The cap is removed at the end of the fourth year and any deferred balances associated with the cap are set for refund or collection at that time?

MR. LOTT: That's correct.

CHAIRWOMAN SHOWALTER: Thank you. You raised one thing, and that is this bell curve is symmetrical, conceptually, in that there can be $20 million, or the outer bands can be positive or negative, and they operate symmetrically on the ratepayers and the shareholders. But in reality, isn't it the case that it's more likely that we'll be at the ends of the bell curve on the expensive side of the bell curve than the other side.

And by that, I mean, isn't it more likely -- I hope it's not very likely, but it's more likely that the company will build toward the $40 million cap to the bad for the company than it would be the reverse and the ratepayers would stand to gain simply because there's a limit to how cheap the resources can ever be in four years?

MR. LOTT: When you look at the 40-year water study, and Mr. Elsea ran this scenario, you would never have a surcharge or a refund. The only thing that varied is the hydro, consistent with what actually happened during the 40-year hydro study. There would be a balance, by the way, at the end of that 40 years, because the population in the 40-year study itself, which only varies hydro, is not perfectly symmetrical. There are, however, other factors, and my guess is that you're right. But if you look at the last two years, two years ago, the company had an extremely good year and it wouldn't take -- and it's when they can sell their resources on the market. And if they can sell their resources on the market and the market price is high and they can sell, they could have a very good year.

Hydro is probably not the thing that will drive a very good year; it's a good market and them having power to sell. If you have an average year with good market prices, then they will make money and that will be there for the ratepayers. A very great hydro year probably will not be -- and they could guess better than I would, but a very great hydro year is not necessarily the year that would be their best year. It would be a great market year with decent hydro.

CHAIRWOMAN SHOWALTER: Maybe we could turn to a different subject. And if you would look at the settlement that's on page six, it's under paragraph 12, and it says that the parties will verify in due course the accuracy of the specific numbers, making up the power cost baseline rate.

Has that verification occurred and are you asking for approval of a specific power cost baseline rate?

MR. LOTT: At this time, Staff is not ready to verify Mr. -- the company's numbers. We're fairly confident that the company utilized the record that they have in front of them to calculate these numbers, but we need a couple months to actually go out and go through this. This is not something we were doing during the proceeding.

The company worked very hard over a few days. I suspect the company would want to check their own numbers and make sure that they pulled off the right numbers. We needed to get something in front of you that showed how the numbers were calculated.

We agree with how the company's put together the numbers. And I think that's -- as we looked through what they pulled off and what they're attempting to pull off, I think Mr. Elsea has a couple minor name changes that he told me about, but other than that, we're comfortable with what's included in there; we're just not comfortable that we know what the numbers are, and we would like to have time. They are the numbers that come from that pro forma statement that's included in the revenue requirements. And I think that that's the important part about this, is that -- the fallout of that revenue requirement calculation and what was included in that. So they are what they are.

CHAIRWOMAN SHOWALTER: Normally, you would think, if we approve a general rate case, there would be a compliance filing and, before the rates went into effect, we would all know with a fair amount of specificity what would happen. Now, I guess we will know, because it's in the settlement, a rate, but I guess I'll ask the attorneys.

Is it a problem that we would be approving an order without having pinned down specifically, prior to rates going into effect, what this baseline rate is, baseline rate?

MR. CEDARBAUM: Well, I don't think it's a problem, and I think that way because you're not really, in this situation, you're not really approving a rate to ratepayers; you're approving the base from which you are -- the company would be calculating a deferral, at least that's my understanding.

And I'm assuming that that verification by Staff and other parties would take place and whatever corrections might need to be made to those deferrals could also be made. So it's not a rate that you're actually not -- that you're approving without the complete accuracy that you would need; it's the basis from which the deferrals would happen.

CHAIRWOMAN SHOWALTER: So we're approving a mechanism and what is done under that mechanism comes forward with some more particularity a little bit later?

MR. CEDARBAUM: I think that's correct. And our witnesses can verify that or agree or disagree with that. And again, as Mr. Lott indicated, that -- the reason why Staff was comfortable proceeding this way is that the presentation of the company included in the exhibits to the stipulation were ones that Staff agrees with.

The numbers are what they are. They can't change, it's just a matter of verifying that the numbers on the exhibits are the exact numbers that should be there. And if there are any corrections that need to be made, that can be done on a going forward basis without any actual rate implications at that time.

MR. LOTT: Just to clarify that, from Staff's viewpoint, one of the advantages in our revenue requirement presentation of this case is it is specific adjustment to adjustment. We didn't just come out and say, Here's the revenue requirement. We have before you a full pro forma statement and a specific rate of return with all the calculations.

And therefore, Staff believes that what's included in there is something that is on the company's books. We have audited that to a large extent, but this is something we will verify to make sure that the company is not cheating themself or cheating the customer by having made a mistake in pulling these things off in a two to three-day period over a weekend, working 12 hours a day. And that's my assumption of what they did. They did this -- worked very hard to get this completed and double checked, but Staff had no chance to repeat that work at this time.

CHAIRWOMAN SHOWALTER: All right. Sticking on the subject of verification, if you look at paragraph 13 on this same page six, the second line, it says, Exhibit B, based on the company's presentation, and is subject to verification.

MR. LOTT: That's referring to Exhibit A, again. Exhibit B refers to Exhibit A.

CHAIRWOMAN SHOWALTER: Okay. So --

MR. LOTT: The $44 that Mr. Elsea was talking about earlier on line 31 is based on Exhibit A.

CHAIRWOMAN SHOWALTER: All right. So are you asking for our acceptance or approval of the figures in Exhibit B or is --

MR. STORY: The methodology.

CHAIRWOMAN SHOWALTER: -- Exhibit B a matter that's subject to later verification?

MR. LOTT: It's the methodology. And we're just not saying that the $44.463 on line 31 is correct. The other numbers are calculations that Mr. Elsea made for the example.

MR. STORY: Right. They're just pulled out of the air. It is the methodology that we're asking for approval on.

CHAIRWOMAN SHOWALTER: All right.

MR. LAZAR: It is the methodology that we've reached agreement on. As a practical matter, it could be as late as the first PCA filing in August of '03 that the Commission might be asked to deal with a difference of interpretation of what numbers belong where. We don't think that's likely. We think we've got a tight mechanism. But the annual filings that are due under this mechanism will be subject to review, so --

MR. STORY: I would just add to that, what Mr. Lazar said a little bit. The company would need a little bit more settlement as to the numbers. We are looking for people to verify these numbers very quickly, like it says in the settlement, so that we can go ahead and book the appropriate amounts.

We agree with Mr. Lott, is that these numbers were pulled out very quickly, and we tried to tie them into a moving revenue requirement. We have not had the chance, either, to go back and truly verify that they matched the revenue requirement that was being developed at the same time, and we -- that's just an audit process.

CHAIRWOMAN SHOWALTER: All right. Then, on the question of the power cost baseline rate, is this intended to be a unit rate, that is, dollars per megawatt hour, or a total dollar amount?

MR. LOTT: Yes, it is a unit cost, and that number is shown, as estimated by the company at this point in time, As $44.463 per megawatt hour. And that's the number we need to verify.

CHAIRWOMAN SHOWALTER: Right, okay. Also, before we leave this page six, I have some questions on page -- on paragraph 11.

JUDGE MOSS: I just wanted to interject a question. Are there plans to somehow inform the Commission when this verification occurs and what the results of that are? I understand there will be reports periodically and a suggestion was that it will be in the company's interest to get this verification at an early date, so those reports would accurately reflect what's actually occurring. So is there some mechanism by which the parties intend to inform the Commission of the status of things?

MR. LOTT: I had personally, one person, fully intended to do that. And maybe a good idea would be, as soon as this docket is completed, to open up a docket Staff investigation to report back to the Commission on that very subject, so that the Commissioners would have an item to track; also, so I have something to charge my time to. But I think that would be a good idea. I mean, just something -- you know, I had intended to do that, and I figured after the gas case was completed or even while the gas case was being completed, Staff could start a full review of those numbers.

JUDGE MOSS: Should the Commission make that a condition of any approval, then, that there be such a filing or --

MR. LOTT: I think they should just require that such a -- I think condition of approval would be the wrong word, but --

JUDGE MOSS: Well, that's how we require things.

MR. LOTT: You just required it. Oh, I see what you mean by condition. Sorry.

JUDGE MOSS: Right. It's just a mechanism.

CHAIRWOMAN SHOWALTER: I'm going backwards a little bit, but while I'm on this page, I have a question about paragraph 11. This is one of those paragraphs that read as if it's an expectation of the parties to the Commission, but that if the Commission approves, it may take on some different meaning. It says, One objective is to have the new power cost rate in effect by the time the new resource would go or goes into service, and it's -- then it's the next two sentences I'm concerned about. It says, Upon receipt of such filing, hearings would be scheduled to review the appropriateness of adjusting the power cost rate. And then the second sentence is, Those hearings would consider only power supply costs.

And seems to me, if we approve this, that arguably the Commission is binding itself to what can or cannot be considered, whereas if the word said could, we would not be. And I'm wondering what the parties intend. Do you intend us to be approving something that sets out definitively what kind of hearing can be had and what it considers, or is this sort of the first category, if this is how we see it working?

MR. LOTT: This, from my intent, when we originally were talking to the company, knowing that they needed new resources, was an attempt to -- for the limitations that we put into this, in other words, this three-year concept and there's the fact the company can't just, you know, for 25 years keep coming in for these things, was to go to single-issue ratemaking related to production costs so that the company could adjust their power cost baseline, production cost baseline, the 44 -- whatever it was that we have included in this $44 per megawatt hour.

It was intended so that the company could come in for that without having to justify whether their overall costs were -- had improved or they had suffered attrition or suffered positive attrition to their rate of return, or negative attrition. And the intent was to be able to allow the company to be able to file those single-issue ratemaking cases.

And so say I don't know whether we're saying we're binding the Commission, but the intent was to allow them to file these things along the guidelines that we included in the stipulation.

MR. STORY: I would agree with what Mr. Lott was saying. It's on the parties that we're trying to make this determination right here as to what would be allowed in a power cost rate. It's the sentence that's following all that, It is contemplated that this review would be completed within four months, I think addresses more the Commission. If the Commission finds that something has to be done other than what we've contemplated, that's where the Commission has discretion.

CHAIRWOMAN SHOWALTER: Well, but that sentence is pretty clear. It's contemplated. But then the next one is, Within 30 days following the four-month review, the Commission would issue an order. Again, if that's a prediction of the parties about what we'd do, it's different when we say it, and so if we say, the Commission will issue an order, then that means we will. If we say here the Commission may issue an order -- I'm just trying to understand how much the parties expect us to pin down in this paragraph exactly what will and won't be heard, what can and can't be heard, and what time lines it is, and then we have to figure out for ourselves how comfortable we are with binding that.

My sense is you want to be pretty certain that the company's entitled to bring a single-issue rate case before us and that we would say in this order that we will entertain that idea and we will not hear arguments from the parties that, No, no, no, you can't do this, because that would be single-issue ratemaking, because the parties agreed and the Commission agreed to entertain that. I'm a little less certain on the time lines.

MR. QUEHRN: Mark Quehrn, for Puget Sound Energy. Generally speaking, I don't think there was any intention here to try to hold the Commission's feet to the fire with respect to any time line. Obviously, where the language in here in terms of contemplation and expectation, as far as how quickly the Commission would act, those are things that obviously Commission action is going to dictate what truly occurs.

As Mr. Story said, I think certainly there was an attempt in this agreement to get the positions of the parties specifically stated as to what our expectations were and what our positions would be in those type of -- in the circumstances that are anticipated by paragraph 11.

MR. LAZAR: Our goal here was to have a narrow process and a tight time frame. Obviously, we -- I can imagine circumstances under which the time frame might not work. And if it doesn't work, it doesn't work, but our goal was, and I think all of us shared this, was to have a narrow set of issues addressed and have it addressed in a very efficient fashion, and we would hope that the Commission would join in that efficiency, but if it can't be done, it can't be done.

CHAIRWOMAN SHOWALTER: And as to the scope of the proceeding, how about that? Is that an expectation or is that a desire on the part of the parties, not only to bind themselves, but to, for example, prevent the Commission from requiring something beyond what would be the power cost rate special case?

MR. QUEHRN: Again, Mark Quehrn, for Puget Sound Energy. I think the scope of the proceeding would initially be determined by the subject matter raised in the filing. And consequently, I don't know that such a filing would otherwise raise other issues, in terms of what's being anticipated for this power cost-only rate review.

Beyond that, I think this is a desire and I would -- you know, we can hear other counsel on this point, too -- that it be clear as an aspect of approving the settlement that were such a proceeding initiated, that it would not be something that the Commission would refuse to hear or undertake on the basis of some concern such as single-issue ratemaking or something else. Yes, we do want you, again, to approve this as an appropriate procedure, as a means of accomplishing these objectives. No, I don't think we are as concerned if it's 33 days or, you know, again, as practical circumstances would dictate when these proceedings are heard.

MR. LAZAR: There is one protection in here in this regard already in paragraph nine. If the cumulative effect of the PCA increases go beyond five percent increase in general rates, that triggers a general rate case filing where everything would be on the table.

In some other jurisdictions that I have worked in, commissions have, on occasion, taken power cost adjustment type filings, ruled on the issues that were capable of being ruled on, but bifurcated the case and continued hearings on items that couldn't be resolved within the time line that was traditional for power cost adjustments.

And I don't know if there -- I've had experience with that in other states. It might be possible that the Commission would use that kind of a mechanism here. We're hopeful that these will be pretty well-defined, pretty easily understandable proceedings.

CHAIRWOMAN SHOWALTER: All right. Similar, just similar use of the word would, which I think is confusing, is on the previous page five, beginning at paragraph eight, where it says, In addition to the yearly adjustment for power cost variances, there would be a periodic proceeding specific to power cost. And then, in the third sentence says, In either case, the company would submit -- it seems like, at least in that last sentence, it would be, In either case, the company may submit, because you're saying the company's entitled to submit the power cost-only filing.

And I'm not sure about there would be a periodic rate proceeding. The company's entitled to have a periodic rate proceeding. I don't know, but the word would just doesn't prescribe or allow; it's in the subjective tense or some kind of tense.

MR. LAZAR: As a practical matter, it's sort of unavoidable. The company has some very large resources that expire during the next few years, that it will have to acquire some sort of replacement resource to replace. So while you're certainly correct that the company has this right and conceivably could not; as a practical matter, it's going to happen.

CHAIRWOMAN SHOWALTER: I'm just trying to get the words down to, if we are approving this agreement, what is it that this Commission is approving, prescribing, prohibiting, allowing, predicting, and the word would is a particularly ambiguous word, I think, coming from us.

MR. QUEHRN: I would like to consult just for a minute on this, if I could, please?

CHAIRWOMAN SHOWALTER: We could take a break and then --

MR. QUEHRN: Thank you.
JUDGE MOSS: We'll be in recess for 15 minutes.
(Recess taken.)
JUDGE MOSS: Back on the record, please.
CHAIRWOMAN SHOWALTER: All right. I think I finished with my woulds and coulds. Oh, unless you have another answer. Maybe we're not. I'm sorry.
MR. QUEHRN: Well, actually, the Chairwoman asked a very good question, and I just wanted to confer, since we were really speaking to the intent of the parties.
Referring us back to page five, paragraph eight, you had asked the question about the first would in the sentence, and should that would be a could. And I think the answer is it could more accurately -- the word could more accurately reflects the intent of the parties. In other words, there'd be no point in filing a proceeding if it wasn't necessary. So it is permissive to the company, not mandatory.
CHAIRWOMAN SHOWALTER: Actually, wouldn't it be can? There can be periodic proceedings?
MR. QUEHRN: I haven't worked through all the grammarical implications of can. I have could.

Could works. But I think it's the same concept.

CHAIRWOMAN SHOWALTER: All right. Well, we'll contemplate it further and clarify what is meant here is that it's permissive for the company to bring periodic proceedings.

MR. QUEHRN: Right. And just in fairness to the other discussion, in any case, the -- what goes with that filing, the second and third woulds, if you will, in the paragraph, that it would always be the company's burden to meet the requirements that are laid out in the paragraph.

CHAIRWOMAN SHOWALTER: Okay. Do you have any comments on paragraph 11, any further comments?

MR. QUEHRN: I had felt, Chairwoman, that we had covered that. Again, that we're looking for the Commission to approve the procedure, but with the understanding that it's an expedited procedure, but obviously the specificity of 30 days is not something that I think, under the circumstances, that we would, again, I think as I said before, expect to hold the Commission's feet to the fire, something like that. That's not the intent. The intent is just to make clear that these processes need to move along on a narrow scope and as quickly as we can.

MR. CEDARBAUM: Commissioners, just for the record, for Staff, that's also my understanding of Staff's intent, as well, with respect to paragraph 11, that there's a substantive side of that. That would be the power cost type proceeding, being single-issue ratemaking, and that is something that the parties are agreeable to and are asking the Commission to also agree to.

But with respect to the process, that these are expectations of the parties and if the Commission can meet them, great; if for some reason the Commission can't meet them, that's not a problem.

CHAIRWOMAN SHOWALTER: All right. So for the single-issue ratemaking, you want it clear from the Commission that that is okay. The other part is somewhat aspirational.

MR. CEDARBAUM: I think that's correct.

CHAIRWOMAN SHOWALTER: All right. A follow-up question on the power cost baseline rate. You said that it was intended to be a unit rate, that it's something like the unit rate of $44.463 per megawatt hour, but that is subject to verification. My question is what is the divisor that produces that? That is, there's -- I assume that in order to get this dollar per megawatt hour, you have to have dollars on the top divided by something that produces that figure, and what is the something? Is it current load levels or what would it be?

MR. STORY: It's the test year delivered load. It's shown on line 28.

CHAIRWOMAN SHOWALTER: Line 28 of?

MR. STORY: Of Exhibit A. That's the load that's divided into line 25 on exhibit --

CHAIRWOMAN SHOWALTER: We can't hear you very well because of the --

MR. STORY: It's -- the baseline dollars that we're using are in line 25, the 847 million on Exhibit A, and the test year delivered load is shown on line 28.

MR. QUEHRN: Just to clarify, that's page one of Exhibit A, line 28.

CHAIRWOMAN SHOWALTER: So it's the -- the divisor would be the test year load in megawatt hours?

MR. STORY: Delivered load, yes, that's correct.

CHAIRWOMAN SHOWALTER: Test year delivered load?

MR. STORY: Yes.

CHAIRWOMAN SHOWALTER: Okay. Thank you.

JUDGE MOSS: I have a question for counsel, and I'll direct it to you, Mr. Cedarbaum. I was looking at these provisions in connection with WAC 480-09-310, and I want to focus your attention there on two points. One is that that rule has certain requirements with respect to general rate or rate filings where there would be a greater than three percent increase, but then there are certain exceptions stated in part two or paragraph two of the rule. And I noticed that there's language in here that makes reference to periodic, and I'm wondering if it's the intention that this mechanism, if you will, this single-issue ratemaking filing is intended to fall within the exception providing that periodic rate adjustments for electric utilities as may be authorized by the Commission are not considered general rate increases for companies regulated under Title 80?

MR. CEDARBAUM: Your Honor, I don't have the rule right in front of me. It's a little difficult for me to respond. If --

JUDGE MOSS: All right. Mr. Cedarbaum, I've furnished you with a copy of the rule, and you might take a look there at the first part of the rule, but then look down at numbered paragraph two, and you'll see there's some exceptions.

MR. CEDARBAUM: Your Honor, I'm not sure that the parties specifically contemplated where in this rule this might fall, but I think it would fall within that section of the rule that you've cited me to.

Also, to the extent that there might be some special exception this rule required for these types of filings, then the parties would be asking for that type of exception to be made.

I guess I would also say that, with respect to the filing requirements in the rule that you provided me are somewhat already covered or would be covered by the types of testimony and exhibits that the company would be required to file on a power cost-only rate review.

If you look at paragraph eight of the stipulation, page five, it's fairly detailed as to what must come with that filing, and Mr. Lott may be able to add to that, or add to what I would say, but many of those items are the types of items that would be filed along with a general rate case filing with respect to power cost issues.

JUDGE MOSS: Well, my concern relates to paragraph nine, which requires the company to file for general rates only if the amount exceeds five percent. And it seems that that would either call for there to be an exception under WAC 480-09-310, or for the Commission to, in any order approving this, to grant a waiver.

And so that really is the heart of my question, as to whether we might simply refer in such an order to the fact that this would constitute a periodic rate adjustment, as excepted by paragraph two of the rule, or whether we would need to explicitly consider a waiver. Mr. Quehrn, did you have some comment on this?

MR. QUEHRN: Yes, thank you, Your Honor. I have reviewed the rule, and I think the words, quote, Periodic rate adjustment for electric utilities as may be authorized by the Commission, end quote, would be an appropriate exception to that rule if the PCA settlement is approved for the power cost-only cases.

JUDGE MOSS: And therefore, we would not need to explicitly order a waiver?

MR. QUEHRN: I would be -- that would be my view, yes, Your Honor.

MR. LAZAR: We discussed this within the collaborative, because we knew there was a difference between the five percent language in number nine and the language in the rule, and it was my understanding that this was a periodic adjustment mechanism, and therefore might not be covered by the rule, and that's one of the reasons that the language in number nine is there, is to make sure that eventually, within -- if rates go up quite a bit, that we would see a general rate filing.

JUDGE MOSS: Are you comfortable with the idea that this would fall within the exception stated in the rule, Mr. Cedarbaum, or do you want to follow up with me on that later?

MR. CEDARBAUM: No, I'm comfortable with that, Your Honor. As I stated before, it seemed that that portion of the rule would apply. Again, not being specifically aware of all the discussions that may have occurred, I guess I was backing that up with the notion of the waiver, but it sounds like the parties are clear that that portion of the rule would apply.

JUDGE MOSS: Thank you very much.

CHAIRWOMAN SHOWALTER: All right. I think, as long as we're close to page five, could you turn to paragraph seven? It's about new resources. And it says, New resources with a term of less than or equal to two years will be included in the allowable PCA costs, then goes on to explain a little bit about it.

I guess my question is does this provide an incentive one way or another to engage in short-term contracts versus long-term contracts or building versus contracts? Does it have any effect on that dynamic?

MR. LOTT: It could, yes, and that was one of the other subject matters we talked about in this. We were talking about -- the four people sitting right here sat there one afternoon and we were talking about, along with Mr. Gaines, by the way, talking about that exact issue, and we were concerned about that, and we don't know what will happen down the road.

One of the parts of this mechanism is -- and the whole power supply area is a reemphasis that the parties agreed to to the integrated resource planning process, and that new resources should be coming out of the integrated resource planning process. And in other words, there should be discussion about and the company should be following that process. And if there is unintended consequences that happened, in other words, if it looks like that problem that you've already identified happens, then somebody's going to have to point it out in a prudence proceeding, either if it's less than two years, through one of these mechanisms, or in the integrated resource planning process, or in one of these short-term rate cases, resource-only rate cases.

It is one of the concerns of Staff and even the company was concerned about it, and it's something that's going to have to be watched. And it has not been the company's plan and is definitely not Staff's thought that the company should be going to a market purchase type of portfolio or a short-term type of portfolio. It is Staff's belief that the company should be going to a utility-type portfolio, where they have the resources and control the resources.

If that's a direction that does not come out of least cost planning, if least cost planning moves more toward short-term portfolio, then this portion of this will have to be looked at again to make sure that we're still consistent with the intent of costs flowing through this mechanism.

But I think you can't cover everything, and this is one of the areas that is definitely going to have to be watched to make sure that that incentive doesn't get utilized by the company in a fashion that is not favorable to the ratepayers. And again, our main check on that is through the integrated resource planning process that all the parties, in particular, Danielle Dixon and NRDC were concerned with and brought very heavily to the process is that we needed to reemphasize integrated resource planning process.

MR. STORY: One concern the company had in this area was that if you shorten that time period, our planning horizon generally will go out beyond one year, and what we didn't want to happen was that if we go out and do a quarterly purchase say at this time of year for the third quarter of next year, that that would be considered a new resource outside of this procedure.

Mr. Lott's exactly right. We all had the concern about the incentives, and it would be reviewed in the least cost planning as to the type of resources and the mix that the company is using to meet its load.

CHAIRWOMAN SHOWALTER: I guess I see three mechanisms at play. One is the PCA, which is fairly objective, and I think creates fairly clear consequences and therefore incentives for the company. Another is the integrated resource plan, which is a very soft process in that it doesn't come out with, at least -- correct me if I'm wrong, but it doesn't come out with prescriptive directions or consequences. And then the third is prudence, which is fairly definitive, but it's after the fact.

And setting prudence aside, it seems to me if you look at a PCA versus an integrated resource plan, and what you can anticipate and what you can't, you can anticipate what's going to happen under a PCA, but it's difficult to anticipate consequences of an integrated resource plan or this Commission's review of it. So it strikes me that the PCA is a stronger mechanism than an integrated resource plan, which leads you to wonder whether it is, as you say, a check. It's a process that could be some sort of a check. Now, the prudence is a different question.

MR. QUEHRN: Mark Quehrn. If I may just add a thought here, and this is actually addressed later on in the agreement. There is a commitment on the company's part and as reflected, frankly, in all of these agreements that are before the Commission on -- a commitment on the part of the collaborating parties to aggressively pursue the integrated resource planning process and to do so in a collaborative effort. And I think, as you've heard the witnesses speak and certainly the company's intention to do just that, and make that a -- again, as it says, quoting from the agreement, one of the company's important responsibilities to pursue. And I think that's certainly the way the company is looking at that issue and how it tends to address it in collaboration with the interested parties.

CHAIRWOMAN SHOWALTER: Taking the prudence mechanism, I'm not sure what this sentence means in seven, the second sentence. The prudence of these resources will be determined in the Commission's review of the annual PCA report. Does that mean what it says, that we will be determining whether the company prudently entered into what annually?

MR. QUEHRN: What I'd like to do is this was another issue that was talked about quite a bit in the collaborative, and if I could defer to the witnesses first, and then, if there are legal issues you want to follow up, I'd be happy to do so.

MR. LOTT: The question was is when do you review the prudence of different types of resources. It was agreed in the collaborative that short-term purchases, in other words, those things less than two years, would -- issues related to the prudence of those items would be brought up in the evaluation of the annual deferral. Anything longer than two years would either be brought up -- the prudence of those would either be brought up in a general rate case or in one of these power supply-only proceedings.

CHAIRWOMAN SHOWALTER: So for example, if we were in one of these annual reviews and the company had entered into a 18-month contract, we could determine did you or didn't you get a reasonable price for that contract. That would be one measure of prudence. Would another measure of prudence be, Well, why are you entering into all of these 18-month contracts. Shouldn't you have a better balance and should you really have entered into so many 18-month contracts. Would that be an appropriate question for prudence in this annual proceeding?

MR. LOTT: I would think that that would be a good subject matter to at least bring up and discuss when the party or the Commission thought that the company was going in the wrong direction through their short-term purchasing process. It would also include things like fuel purchases, you know, various hedge mechanisms the company might have used or other things. But my thought was yes.

MR. LAZAR: To the extent the mechanism creates a bias, I think it's a bias in favor of long-term resources, but it's not much of a bias. We tried to keep it as neutral as we could and have a workable mechanism. I think that if the company were using a series of short-term acquisitions and the parties were concerned about it, the annual PCA review would be one venue to take that up in, but the biennial least cost planning process that's addressed in Section E of the stipulation clearly is an additional area that we would expect to take that up.

CHAIRWOMAN SHOWALTER: Why do you say it's a bias toward long-term resources?

MR. LAZAR: The certainty of cost recovery is greater. These long-term resources trigger a power cost-only rate review, where the base power cost is reset and the recovery of those costs is -- would be built into that. If, on the other hand, it was -- were short-term acquisitions and there was not a power cost-only rate review, then any deviation from the costs that are in the power cost rate that's being set at this time would be eating up the dead band. That is, the company would be at risk for those deviations unless and until there were a power cost only-rate review.

The company, I think, is at more risk with short-term resources than with long-term resources.

But if you can buy cheaper in the short run, that may provide a -- some balance to that. You'd have more risk with short-term resources, more certainty with long-term resources, the way the mechanism is set up. But we tried as best we could to keep it as neutral as reasonably possible, given a recognition that there have to be short-term transactions for the utility to maintain loads and resources in balance.

CHAIRWOMAN SHOWALTER: I would have thought that you would have to weigh the dynamic you just described against the certainty that comes with the PCA in terms of what the company's exposure is. I mean, that there is also a measure of certainty in the PCA mechanism and what the company will or won't be liable for under it, whereas the longer term is, in a way, more speculative, isn't it?

MR. LAZAR: The longer term is more speculative, but the way this mechanism is designed is we hope that the long-term resources will come before the Commission for review in those power cost-only reviews prior to those resources being effective or, in the short run, if that can't be done, the mechanism provides for the lesser of the cost or what's embedded in the power cost rate to go into effect in the interim. So say long-term expensive resource, the company has a pretty strong incentive to get a power cost-only review to occur coincident with the resource entering into service.

CHAIRWOMAN SHOWALTER: You just said prior to the resources being effective.

MR. LAZAR: There's language in here.

CHAIRWOMAN SHOWALTER: But I think if you could look at that paragraph 11, page six.

MR. LAZAR: It was the first sentence of that that I was referring to, is to have the new power cost rate in effect by the time the new resource would go into service.

CHAIRWOMAN SHOWALTER: All right. Does this mean that this is before it's used and useful? I'm a little confused.

MR. LOTT: No, the intent of that was so that the company would try to make filings for new resources on a timely fashion that would try to get the new resource or the new rates, the new baseline to go into effect at the same time the new resource. For example, if the company had a new -- I'll just call it -- what did we call those -- a new CT go online and that was going to go online January 1, they would file something so that they would get rates to go into effect at that same January 1 time frame.

CHAIRWOMAN SHOWALTER: Okay. Actually, the sentence says, By the time the new resource would go into service. And maybe what caught my attention is I think Mr. Lazar on the stand here said before it takes effect, or something to that effect.

MR. STORY: Actually, I think what Mr. Lazar was talking about is the last sentence of paragraph seven, of where, if they're not able to get rates adjusted, there is a mechanism to put a knew resource in at a lower than actual -- or the lower of the actual or the embedded cost of power costs.

CHAIRWOMAN SHOWALTER: This is the last sentence of paragraph 11?

MR. STORY: Paragraph seven.

CHAIRWOMAN SHOWALTER: Seven, I see. I was on 11. All right. So this is a bridge, but then it can be reviewed in a power cost only, and that's over in 11, and that is -- that's phrased by the time, which seems to be after the time.

MR. STORY: Yeah, that was the intent. We know that it's not always possible to match these things exactly, so the bridge is in seven, and 11 was the intent to have it in effect.

CHAIRWOMAN SHOWALTER: All right. Then the third piece of this dynamic was the integrated resource plan, which is on page seven, paragraph 16; is that right? This, on the last sentence, has a recommendation, and it -- the last phrase says, With opportunities for public comment prior to final determination.

What do you mean by final determination there? Final determination of what?

MR. LAZAR: This refers back to the incentive penalty mechanism. There is not currently an incentive or penalty mechanism in place to reward or penalize companies for their performance in the least cost planning process or under the least cost plan once it's reviewed and accepted.

And the recommendation here is let's look at incentive and penalty mechanism within the context of the WAC and have public comment on the incentive and penalty mechanisms, is my understanding of what we were trying to get to in this language.

CHAIRWOMAN SHOWALTER: To put into the WAC incentives and penalties, is that what you mean, or --

MR. LAZAR: Well, I don't think we, the parties that were working on this, got that focused on the legal mechanism. We want to -- the parties that were particularly interested in this, two of them are not at the table here, were interested in having an incentive and/or penalty mechanism apply to Puget for its performance as a portfolio manager, and the negotiating parties realized that the one way to approach this was within the Commission's least cost planning WAC, and we've referred to that mechanism.

But whether the appropriate place to implement the incentive or penalty mechanism is through the WAC or through some other means, I don't think we reached that point in the collaborative.

CHAIRWOMAN SHOWALTER: I think it leads to the general question, which maybe isn't before us, is to be addressed later, but do we, don't we have authority to impose penalties for failure to comply with the least cost plan? Is that what you're getting at here?

MR. LOTT: Well, I think what we were talking about is an incentive mechanism that would have both rewards and penalties based on something. We've done rewards and penalties in the past related to conservation. I don't think we've ever had one on the supply side, but I think that this is -- this is, again, it's not something that the parties are agreeing to a particular mechanism or the Commission or anybody else. There are some people that were suggesting -- all we suggested here was that the parties thought it was appropriate to discuss portfolio management and whether there should be rewards or penalties associated with such an incentive mechanism included in those integrated resource planning development.

CHAIRWOMAN SHOWALTER: In any event, though, this paragraph is pretty clear that this is a statement of agreement of the parties and not anything in particular required of the Commission. Am I right on that? Other than the first sentence is a declarative statement, or the first two sentences are, but the rest is that the parties agree this is important and recommend that the Commission address it later. As far as operative language, there really isn't any?

MR. QUEHRN: This is Mark Quehrn, for the company. That's our understanding, yes.

CHAIRWOMAN SHOWALTER: All right.

MR. CEDARBAUM: Commissioners, just for Commission Staff, again, that is also the Staff's understanding. This was a really a placeholder provision for the issue on rewards and penalties and/or penalties, and that we're recommending the least cost process, least cost planning process as a forum for that to happen, but it is a recommendation.

MS. DIXON: This is Danielle Dixon on the bridge line, and I would second what Mr. Cedarbaum just said and, in addition, I think the only operative word in there is to address as soon as possible. My understanding is that the company and the parties plan to begin collaborating on Puget's least cost plan very soon following an order in this case.

CHAIRWOMAN SHOWALTER: Let's see. If you could turn to Exhibit B to the settlement, if you look at line 31, that says $849,710,975. Now, then, if you look at Exhibit A-1, line 25, that says 847,615,110. So are these meant to be the same? Is one subject to verification? Can you explain why these are different, or maybe they don't even mean to be describing the same thing.

MR. LOTT: Remember, this is a unit cost thing. So if you look at that line 31, you'll see the number 44.463. Go back to --

CHAIRWOMAN SHOWALTER: Wait, wait, wait, which exhibit?

MR. LOTT: Looking at Schedule B, you quoted the number 849,000 -- million, sorry, on line

31.

CHAIRWOMAN SHOWALTER: Mm-hmm.

MR. LOTT: That number was based on the unit cost of $44.463 shown over to the side. Now, go back to Exhibit A-1, and right next to the $847 million number is the 44.463. As Mr. Story indicated a little while ago, that that 44.463 was calculated by dividing the 847 million by the line 28 volume numbers of 19,063,000 megawatt hours.

Now, going back to Exhibit B and looking at the line 30, there's the PCA period loads of 19,110,000 megawatt hours. You see that's a slight growth from the one period to the other period, and therefore, when the nineteen-one-ten is multiplied times the unit cost, you will get a slightly higher number.

CHAIRWOMAN SHOWALTER: So my real question should have been why are those two numbers different, and the answer is one's a different year than the other?

MR. LOTT: That's a slightly different volume associated with it; correct.

CHAIRWOMAN SHOWALTER: Okay. I think there's one set of questions concerning page four.

MR. LOTT: Page four of the exhibit or page four of the settlement?

CHAIRWOMAN SHOWALTER: Of the settlement. All right. Let's see. All right. The total revenue requirement here includes both wheeling revenues and costs associated with certain major transmission facilities. Am I right there?

MR. LOTT: Yes.

MR. STORY: That's correct.

CHAIRWOMAN SHOWALTER: All right. Is this calculation consistent with the way power and transmission costs and revenues have been included in the test year and pro forma power costs in the past?

MR. LOTT: Companies -- okay. I didn't quite understand the second part of your question. The -- let me -- I'll answer what I thought was the first part of the question.

CHAIRWOMAN SHOWALTER: All right.

MR. LOTT: The calculations in the company's Exhibit A, that Staff still needs to verify, are consistent with the way things have been pro formed in this case.

CHAIRWOMAN SHOWALTER: And how about compared to pro forma power costs in the past?

MR. LOTT: The pro formas in this case are very consistent with what was done back in the 1992 rate case with restricted power supply. I mean, different adjustments have been done differently, you know, but we are calculating production costs from these pro forma statements. So you know, wages were pro formed differently in 1992 than they were here and --

CHAIRWOMAN SHOWALTER: Okay. Then why have only specific transmission costs and revenues and not all transmission costs and revenues been included?

MR. LOTT: We were trying to get the transmission costs that were related to bringing the power to Puget's system, as opposed to transmission costs moving power through Puget's system. So if you looked at the specific transmission costs that we tried to identify, other than the wheeling costs, they are the Colstrip lines, the Third AC and the Northern Inner Tie. Those are shown -- those were the items that the company identified and Staff and other parties have agreed to now, the company identified as company-owned transmission that related to bringing power to Puget's system, integrated system, as opposed to transmission within Puget's system.

CHAIRWOMAN SHOWALTER: So what are the implications for including these transmission costs and revenues in power costs should the company's proposal to form and join RTO West come to pass?

MR. STORY: At that time, I think there would be a filing required to address the RTO. We did discuss that a little bit in the collaborative, and the intent of this is only if things remain the way they are right now. The RTO would throw a whole different environment into this and we would have to see what the RTO impacts were.

CHAIRWOMAN SHOWALTER: Well, assuming the RTO West proposal looked something like the current one, current proposal, what would the issues be for us to consider vis-a-vis these provisions?

MR. STORY: One concern I think would still be there is that we wanted to make any new purchased power --

CHAIRWOMAN SHOWALTER: Can you get the mike a little closer?

MR. STORY: Sure. One of the concerns we had was to make any new purchased power contract equivalent to the ones that the company currently has, so to bring that power to the company would include some sort of transmission expense if it was outside the company's area. We would still have to do that under the RTO, so that we could make the --

like if it's a purchased power contract from Oregon, we could make it comparable to a company-owned resource within Puget's area. So it would be one consideration.

JUDGE MOSS: Mindful of the hour, it is 12:00, I think we'll take -- the Commission has some other business that needs to be conducted at the luncheon hour, in addition to obtaining nourishment, and so we will take a recess from 12:00 until 2:00. So we'll see you back then, and you can all have a lovely, leisurely lunch on the waterfront on this beautiful day.

(Lunch recess taken.)

JUDGE MOSS: Let's be back on the record. I have one matter to take up, a couple of matters, actually, before we get back into questions on the PCA.

One, off the record, Ms. Dixon suggested that -- or stated that she was concerned that the Commissioners might require some additional clarification with respect to paragraph 16 that we discussed somewhat earlier. And so I will put it to the bench whether they feel that they need some additional clarification from Ms. Dixon with respect to the paragraph 16 on page seven of the PCA issue agreement, the one that Mr. Cedarbaum described as a placeholder paragraph?

CHAIRWOMAN SHOWALTER: No.

JUDGE MOSS: No, the bench does not feel that it requires any further clarification with respect to that paragraph, Ms. Dixon, so we won't need your statement. Thank you.

MS. DIXON: Thank you.

JUDGE MOSS: I have a question, and I'm not sure if it should go to anybody on the panel or maybe counsel would be able to respond to this. It's a clarifying question with respect to what has been referred to as the umbrella stipulation.

And looking at page two of that, there's a Arabic number three, paragraph Arabic number three, and the question relates to the sentence that begins on line 38 and a half. It says, The participating parties that executed the conservation and low income issue agreements present these gas -- I'm wondering if there's a compound verb and the verb should be will present. We had a little trouble understanding the sentence otherwise.

MR. CEDARBAUM: Your Honor, Commissioners, we have presented natural gas rates, or at least a proposed cost recovery mechanism for natural gas rates to recover the cost of the low income program, and we're asking the Commission to approve that.

JUDGE MOSS: In this settlement stipulation?

MR. CEDARBAUM: Yes.

JUDGE MOSS: I don't recall seeing gas rates in the settlement.

MR. CEDARBAUM: Well, the rates themselves would come in a compliance filing, but as far as the low income stipulation, there is a proposed cost recovery, essentially a rate spread proposal on how those costs will be recovered.

MR. LAZAR: It's in the last page of Exhibit G.

JUDGE MOSS: Exhibit G?

MR. LAZAR: Yes.

JUDGE MOSS: Well, let's take a quick look. And that's paragraph 23 there?

MR. LAZAR: No, this is Exhibit G to the umbrella stipulation.

JUDGE MOSS: Oh.

MR. LAZAR: The low income assistance stipulation has a final page, which is the gas rate spread.

MR. CEDARBAUM: Just to add to that,

there's a --

JUDGE MOSS: Wait a minute. Let's get this clear first. I have the settlement terms for low income in front of me. It's a five-page agreement exclusive of the --

CHAIRWOMAN SHOWALTER: I have G.

MR. CEDARBAUM: That's right.

JUDGE MOSS: That's what I'm looking at.

MR. CEDARBAUM: And then, if you turn to the attachment to that.

JUDGE MOSS: Oh, there's an attachment to it. Oh, okay.

MR. CEDARBAUM: Those show the rates that we are -- at a compliance filing will reflect if the Commission were to approve the settlement.

JUDGE MOSS: And that's the third column from the left, rates per therm?

MR. LAZAR: Yes.

JUDGE MOSS: Okay. All right. Well, that clarifies that.

MR. CEDARBAUM: And then, with respect to conservation, we have agreed, in the conservation tab, which is Tab F, to a cost recovery mechanism, and that's -- that's the discussion under subpart L that begins on page nine. And we haven't attached to this part of the agreement a specific per schedule or rate per schedule proposal to kind of carry forward that cost recovery, but, again, that would come in the compliance filing.

JUDGE MOSS: And the gas piece of that is in paragraph 38 there?

MR. CEDARBAUM: Yes, it is.

JUDGE MOSS: Okay, all right. I think that clears that up. Thank you. Now, I have another question, and this goes, initially, at least, to you, Mr. Lott, with respect to some of your testimony this morning. You touched at one point, in one of your responses, on the paragraph four at the settlement terms for PCA. That's on page two of the issue agreement.

And the first bullet there, under Arabic four, includes that sentence, The surcharging of deferrals can be triggered by the company when the balance of the deferral account is approximately 30 million. And your comment this morning, I believe, was to the effect that it was phrased that way because if it was 29.7 million, you wouldn't want to cut off the opportunity. But my -- I'm a little concerned about the lack of precision here in that I can foresee a day when someone might say, Well, 25.1

million is approximately 30 million, or somebody else might say 29.4 is not approximately 30 million, so you see my concern.

So I wanted to get a sense of what specifically the parties had in mind by using this type of a trigger stated in terms of approximately an amount.

MR. LOTT: I see Mr. Quehrn getting ready to answer this question, but I'll give a first attempt at it. My thought was is that when the company's in a position where they're sitting very close to that number and it looks like the number's going to get larger, then I would suspect the company would be filing. If, on the other hand, the company was in a good position and it didn't look like a bad -- did I say that the wrong way? I'll try that again.

If in a year they were sitting, like, at twenty-nine and a half and there was -- the company knew that they had poor hydro, then they might file for the twenty-nine and a half million dollars at that point in time. On the other hand, if the company was in a good hydro situation or a good market situation and the balance had built up to that number, then I would not expect them to be filing.

But I think the intent was they wouldn't file until there was a $30 million balance, generally. But, remember, there was this right to file before the balance actually got to $30 million.

You'll notice that on the refunds, they're required to file when it gets to $30 million, and that was --

JUDGE MOSS: I did notice that.

MR. LOTT: Right. So the company had no option not to refund. That doesn't mean that the Commission or the Staff might not suggest that they hang on to the money, but that the company would have to file.

JUDGE MOSS: Mr. Quehrn, did you have something to add?

MR. QUEHRN: Actually, I was just moving the microphone at the time.

JUDGE MOSS: You have to be careful of your body language in here.

MR. QUEHRN: I understand that.

CHAIRWOMAN SHOWALTER: It's like an auction.

JUDGE MOSS: What is your bid? No, just kidding. All right. Well, my sense, from what you're saying, Mr. Lott, is what is contemplated by this language is something very close to 30 million, 29 and a half, you've mentioned, 29.7 perhaps earlier today. We're not talking about 25 million, for example?

MR. LOTT: No, again, I think it depends on the circumstances. If they're below $30 million and the circumstances do not indicate a situation where the company was coming up short, then -- in fact, we're going to have a good year, then I would suspect they would sit on the twenty-nine and a half million. I think there would have to be some -- and the company might, with a $32 million balance, decide to do the very same thing, knowing that they were having a good hydro year, a good market year, because things turn around by the end of July in some years, you know.

Since you're dealing with October through January and then the hydro starts flowing in the months, my guess, April through June, things may be totally different by the time the deferral had been accumulated than when the deferral was being accumulated, so -- I'm just not trying to be too strict on the company and say that they can't file for a slightly smaller amount.

JUDGE MOSS: And like yourself, while I

look forward to being fully employed in the future, I'm not sure that I really want to have to come in and listen to argument about what approximately means. I wanted to have a better idea of that. Thank you for clarifying that.

COMMISSIONER HEMSTAD: I'd say approximately means about.

JUDGE MOSS: Now, one final piece, somewhat in the nature of housekeeping, before we get back to the PCA questions. Over the luncheon recess, I was able to prepare a set of bench requests that relate to time of use conservation agreement, low income service quality index, and rate design. Some issues we've talked about and some we haven't. So I want to distribute those now.

And I've also had some discussion, and we may have to supplement this later this afternoon with two or three additional questions, but in the meantime, I'll go ahead and pass these out so you all will have those, and I'll get them filed with the records center for other parties sometime today if we finish before 5:00.

All right. And I think, with that, we are ready to return, and I think Chairwoman Showalter has a few more questions, and the other Commissioners, of course, may have some questions to chime in with, as well.

CHAIRWOMAN SHOWALTER: And I hope not many more, but picking up where Judge Moss left off on the $30 million, assume that we have gotten to approximately 30 million or more and that there is a surcharge. Is there any cap on the surcharge or credit level?

MR. LOTT: There's no cap included in the mechanism. The company would be accruing interest at this point in time one way or the other, and there is no cap placed in here. We talked about that and we thought, depending on the circumstances, you may -- nobody contemplated that you would absolutely or, on the opposite side, never push it out for over more than one year. Again, it depends on the circumstance, you know, price signals are something that -- it could be that raising the prices at that time may be a bad price signal, and therefore spreading it out may be in the company's interest. It is possible for all sorts of situations to exist, but the intent was to amortize the balance over a one-year period and with no cap.

CHAIRWOMAN SHOWALTER: All right. Can there be more than one surcharge or credit in place at one time?

MR. LOTT: Well, I would assume that you would, if you had a second case that came in at that time, you would change the surcharge to recover the balance from that time forward.

CHAIRWOMAN SHOWALTER: So there would only be one surcharge, but it could be the result of two actions?

MR. LOTT: Right.

CHAIRWOMAN SHOWALTER: Then is there anything in the agreement that says that the surcharges or credits can be triggered only annually or can they be triggered or occur one quarter into the July to July year?

MR. LOTT: Well, from a strict deferral basis, it can only be triggered annually, since the deferral is strictly on an annual basis. That is, we tried to make it so that the company could come in and file when they could demonstrate that the balance could climb in that direction. So in other words, if you remember last August, the company knew that they were in trouble for that coming winter, they would have then probably filed a surcharge last August, which is exactly what they tried to do last year, and that would have implemented a surcharge starting probably in September or October, based on that proposal.

CHAIRWOMAN SHOWALTER: All right. Switching areas, I want to ask one follow-up to an earlier question, and it was about what happens if Puget joins an RTO West, and I believe your answers were in terms of what happens to the power costs, but what about inclusion of transmission revenues? Would transmission revenues be affected by the RTO West proposal vis-a-vis this proposal?

MR. STORY: I've not looked at the most current RTO proposals. I couldn't answer that. We could answer that on a per bench request, if you'd like.

CHAIRWOMAN SHOWALTER: All right. If it's not in there, we'll probably add it.

MR. STORY: Okay.

CHAIRWOMAN SHOWALTER: And I want you to know, I understand that RTO West is a tentative proposal at this point and not definitive, but there is a proposal and I think you might at least be able to answer in terms of the factors that might be before this Commission with respect to those transmission revenues.

MR. STORY: Okay.

CHAIRWOMAN SHOWALTER: Last follow-up. I noticed in Mr. Lazar's testimony, which is Exhibit 551, page five. Maybe I got the wrong -- let me see. Page five, lines six and seven. Oh, let's see. I need to see here. All right. Where it says, All of the parties have the right to request changes in the mechanism at any time in the future, do I take it that you are saying that because there's nothing in the settlement that prohibits it, or is there a place in the settlement that expressly reserves that right?

MR. LAZAR: There's nothing in the settlement that prohibits it. There's not a stay-out period, there's not a term to this mechanism. It is perpetual until changed, and the parties have whatever rights they have.

CHAIRWOMAN SHOWALTER: That's all the questions I have.

COMMISSIONER HEMSTAD: Sticking with Mr. Lazar's testimony, I'm at page two, line three. The sentence is, Third, we wanted a mechanism that would be relatively easy to administer. We've had an interesting discussion here today about what would seem to me to be the relative complexity of this -- the proposal.

I guess my question is at two different

levels. Do you really believe this is going to be relatively easy to administer, and secondly, in a much larger context, harkening back to the history of ECAC, that's E-C-A-C, and the PRAM, P-R-A-M, which struck me the public never did understand it, how will a generally reasonably informed member of the public understand this program?

MR. LAZAR: I do think this will be relatively easy to implement. And I say that in the -- you know, in comparison to a general rate proceeding, very easy to administer, as compared to the gas tracking mechanism, only slightly more complex. So from an administrative perspective of the people who work with it, I don't think it's a difficult mechanism.

Turning to the public, I do think this will not be an easy thing for the public to understand. Fortunately, they will very seldom have need to understand it or be affected by it, because, as we indicated in our -- in my testimony, we were interested in a mechanism that wouldn't result in frequent rate changes, the combination of the dead band, the deferral mechanism, the sharing mechanism and the trigger. I think that this mechanism very likely will only be triggered under extreme weather conditions.

This is not a weather-only PCA. It incorporates other factors, but because of the size of the dead band and the amount of the sharing and the size of the trigger, it's almost impossible for me to imagine circumstances that would cause a surcharge to trigger without a severe weather situation associated with it. And as the Commission has said in a number of the PCA orders, the public can understand a linkage between a surcharge and weather.

Also, I will say that I think it is very, very unlikely that this mechanism will trigger a refund. The asymmetry of power costs, as the Chairwoman was speaking to before the lunch hour, is such that it's very, very unlikely that there will be a refund. That means that I think there will be very few rate changes as a result of this mechanism and those that do occur, I'm almost certain, will be associated with extreme weather circumstances that the public will be able to understand. So it won't happen often, and when it does happen, I think that there will be an easy to explain reason for the rate changes.

MR. LOTT: Just to give you my answer to

that. When I look at it, when you go back, we have the PGA that we apply to the gas companies, and we had the ECAC, which you mentioned earlier. Those are very easy mechanisms to administer, generally speaking. There's this hundred percent flow-through and it's fairly easy to calculate. In the ECAC's case, however, there were a lot of problems, because you were measuring only variable costs, and unfortunately the company owns power plants, therefore, the relationship between them.

We tried to correct those things in the PRAM, and the PRAM was also not that difficult to administer, more so than the ECAC, but the PRAM brought in new resources and new resources caused a lot of problems with huge rate increases and huge deferrals related to new resources when the -- other than the, you know, Tenaska, Encogen, and these other new resources coming on, there was no real reason for rate increases or these large deferrals.

This mechanism follows the PRAM much closer than follows the ECAC. It tries to take care of the problems that were included in the ECAC, tries to remove increases that aren't related to fluctuations. It uses those single-issue rate cases in order to deal with new resources, so that the ratepayers will understand when they get one of those type of rate increases, and it will obviously, as Mr. Lazar said, fluctuate for things other than weather -- and that is basically market prices.

And I think that is something else that the ratepayers -- that's the call I get most often, especially from larger customers, is, The price is down, why isn't my rate going down; the price is up, why aren't the rates going up. So I get a lot of calls from middle size customers, not residential customers. They look at the market, for some reason. I don't know why, but they do, and they ask that, both in electric and gas. It's not just gas. They ask that on the electric side, too.

COMMISSIONER HEMSTAD: What's going to happen at the end of the four-year period, attempting to look forward to the -- does this program, by its own terms, terminate or does it continue until revised?

MR. LOTT: No, this mechanism does not end. The only thing that ends at the end of the four years is the four-year cap. After the end of four years, I mean, there are some thing things that will push the company into a general rate case, filing one of those single-issue rate cases. After the end of three years, the company would then have to turn around and file another general rate case. Obviously, anybody that finds a problem with this can bring it in front of the Commission and we can talk about that, but the intent was is this would be an ongoing process, this mechanism would hopefully last for a long period of time, with modifications that take care of unintended consequences, which, if they don't happen, we'll be very lucky. But, I mean, something will go wrong, and hopefully we can correct it, rather than eliminating it just because there's a problem.

MR. LAZAR: You also have the Avista settlement before you. That settlement contains a built-in review period. This one does not. That's a distinction between the two. We're confident that this one is well enough designed that the parties didn't see a need to propose something like that.

CHAIRWOMAN SHOWALTER: But, on the other hand, nothing prohibits any of the parties from coming in and seeking review?

MR. LAZAR: That's correct.

CHAIRWOMAN SHOWALTER: Well, actually, just to follow up to that question, I realize, of course, the company can come in and seek a review, but what is the ability of a non-company party coming in and seeking a modification, I guess through a complaint?

MR. LOTT: Well, in U-8141, Staff and other parties -- that's the beginning of ECAC, but Staff and other parties made a petition to the Commission to reopen, or I can't remember exactly how we reopened it, but we reopened U-8141 to that discussion. And I remember testifying in that proceeding and the Commission putting out an order and telling the company they had to do something in the next general rate case.

In other words, that reopening of U-8141 did not eliminate the ECAC, but it put bounds on the company to do things, and in the next general rate case, the Commission then eliminated ECAC. Of course, any general rate case, the Commission would have the right to relook at this, also.

CHAIRWOMAN SHOWALTER: Right. But what if it's not at the time of a general rate case?

MR. LOTT: That's what I'm saying. I think it would be better for Mr. Cedarbaum to --

MR. CEDARBAUM: A number of processes come to mind. The general rate case is one, but a petition to reopen or rehear, whichever is the appropriate name, would be another. A complaint process would be another if the standing requirements of the statute were met. I suppose, I mean, there's nothing in our agreement that prohibits during any of the annual filings or the power cost-only reviews if something -- there's just some major glitch and a party wanted to propose how to fix that. I don't think that's really anticipated, but not precluded, either.

So it seems to me like there are a number of ways to go. And others might come to mind, but those are the four that come to mind immediately.

CHAIRWOMAN SHOWALTER: Okay.

MR. LOTT: Just a reminder. Every year we would plan to bring the company's calculation of the deferral in front of you. The company, of course, can make a petition at any time, but in our review of those deferrals, we might suggest that there's a problem at those points in time, which is when I would suspect that Staff would probably suggest something.

MR. LAZAR: The mechanism specifically provides that the prudence review of short-term resources would be done at the time of the annual deferral review, and so if those became controversial, that might either cause the Commission to make a decision to reopen the mechanism or the parties to ask the Commission to do so.

CHAIRWOMAN SHOWALTER: Mr. Quehrn.

MR. QUEHRN: Commissioner, I would only add, I think, that it is also the parties' intention that within circumstances that have been anticipated and reflected in the stipulation is that this would be, as Mr. Lazar first said, a mechanism that would survive for an indefinite period of time, until, as I say, either we're in a general rate case or something else would require us to revisit it.

So it's -- I don't think it's intended, particularly during the first four years, that it's going to be revisited.

CHAIRWOMAN SHOWALTER: But can it be, is the question, and can it be revisited on motion of someone other than the company. And I think Mr. Cedarbaum gave the answer yes.

MR. QUEHRN: Well, I don't have any dispute with the procedures that Mr. Cedarbaum is referring to. I mean, they were all there in the law. I would agree with that. I was just adding that I think it is the parties' intentions that this thing is going to be with us for at least four years.

MR. LAZAR: Because we're reasonably certain that there will be a general rate case in the fourth year of this mechanism, because of the way it's structured, that is, if the company requests a power cost-only review after year three, that triggers a general rate case. My guess is that unless there's some egregious problem with it, that that will be the time that the parties would look to fine-tune it.

COMMISSIONER HEMSTAD: I have one other -- call it a practical problem or practical concern. With the annual filings that will occur here that will specify a period of time, and then with possibly other kinds of filings, are we going to find ourselves in a situation where it will be difficult for Commissioners to have the conversations with Staff or any of the parties about how this whole system is working because of ex parte requirements and the like that will make that kind of conversation difficult?

MR. LOTT: I can only answer part of that, I suspect, and that is that there will be Staff reviewing those deferrals and trying to bring a recommendation to you. I don't know whether those are things where there's an ex parte rule or not, and I don't know, but there will be other Staff that can talk about the policy, and talking about the policy about what's going on is a different matter than reviewing the deferrals that are in front of you at that time.

MR. CEDARBAUM: Commissioner, I guess it seems to me like it would work an awful lot as the PGA mechanism works now in terms of deferrals. I mean, there are filings made by the company, but I don't think that prevents any discussion ongoing with the Commissioners and Staff.

Now, you know, once a filing is made, that's subject to Commissioner review and approval, according to paragraph four on page two. That's the deferral, annual report. And I would expect that could come before the Commission in open meeting for approval, and so you would have similar processes for that.

Now, if there's a power cost-only review case actually filed, and that's going to go to hearing, that's a different animal.

So I think sort of the ongoing way this could work in terms of the deferral filings is pretty analogous to how a PGA works today. It wouldn't present any major obstacles to any ongoing discussion.

COMMISSIONER HEMSTAD: That's all I have.

CHAIRWOMAN SHOWALTER: Mr. Lazar, I have one more now that we had turned to your testimony. I have a little question mark on page four of your testimony, Exhibit 551. And it's line seven through 11. You're talking about the relationship of the return on equity to this surcharge versus utilities able to recover a hundred percent of prudently incurred power cost. Can you just explain this dynamic a little bit more?

MR. LAZAR: Yes. Exhibit B to the settlement stipulation, which is the revenue requirement stipulation, sets forth a specific capital structure and rate of return by element. That was negotiated at the time of the -- that the return on equity component of that was negotiated as part of the interim, and the interim committed the parties to negotiating a PCA that equitably shared risks.

This PCA mechanism, in my opinion, does equitably share risk in recognition of the return on equity that was allowed. A mechanism that had, say, a $5 million dead band and a $5 million trigger, rather than a $20 million dead band and a $30 million trigger, would assign much more risk to the ratepayers than the mechanism that's before you.

CHAIRWOMAN SHOWALTER: I see.

MR. LAZAR: And the Commission has been very clear in the past that one of the conditions for a power cost adjustment mechanism needs to be a cost of capital adjustment. The cost of capital adjustment needs to be of the right order of magnitude to fit with the PCA.

If we had a hundred percent flow-through PCA, we would think that the stipulation return on equity was too generous. If we had a zero flow-through PCA, as is the current case in rates today, arguably the return on equity stipulation would have been too -- well, it would not have been generous enough as the balance between the structure of the PCA and the level of the return on equity that were important for us in the negotiations.

CHAIRWOMAN SHOWALTER: So in lines 10 and 11, where you're contrasting this PCA with a utility that gets a hundred percent recovery, i.e., it's a lower risk to that other company?

MR. LAZAR: Right. The Nevada Commission has recently issued two orders, one for Nevada Power, one for Sierra Pacific Power. The return on equity for Nevada Power was 10.2 percent; the return -- or I think, and for Sierra Pacific was about the same.

And one was 10.17, the other was 10.2. In that state, there is a statutory guarantee of a hundred percent recovery of prudently-incurred costs. Now, in that jurisdiction, there was a little prudence disallowance in the amount of some $400 million, but that was within the prudence review part of it, not within the statutory flow-through part of it. They received much lower returns on equity, but their mechanism exposes their companies to less risk than this mechanism exposes PSE to.

CHAIRWOMAN SHOWALTER: So what you're saying, in the lines seven and eight and nine, is that you, in your view, the risk that -- the risk allocation between shareholders and ratepayers appropriately corresponds to the 11 percent return on equity?

MR. LAZAR: Yes.

MR. QUEHRN: Madam Chairwoman, if I could add here -- Mark Quehrn, for Puget Sound Energy. I think the operative word here is range. As Mr. Lazar has testified, there is a range of different types of PCAs among various jurisdictions that look at the degree of risk that's being shared between the customers and shareholders and return on equity, and I think this does fall within the range, but we would just want to make it clear for the record that there is a range.

COMMISSIONER OSHIE: I have a question for the panel. On page five, paragraph six, entitled Adjustment for Availability of Colstrip, I really have two questions, and they can -- the first question is why was this section of the -- included in the agreement, its purpose, and two, does it matter to the parties why Colstrip would be made unavailable to the company?

MR. STORY: This paragraph was added. It was a concern in the ECAC that when a plant went down, we were recovering the plant costs in rates and also recovering the replacement power costs. So to address that issue, we came up with this mechanism of adjusting the revenue requirement down for Colstrip when it was out for any long period of time, and this would be a long period of time if you got an average availability factor down below 70 percent.

So it's, in essence, giving some of the money back that we collected for plant recovery when we're actually getting recovery on the replacement power cost.

COMMISSIONER OSHIE: I guess I don't have a good feel for what the long period of time would be at 70 percent.

MR. LOTT: Well, I just want to explain how we got to this number, but this is the four plants combined, so they have one, two, three and four, and they get about -- even though one and two are substantially smaller plants, they're not substantially smaller for Puget because of a lot larger percentage ownership. So basically, you have four plants that run at about an average of 85 percent capacity -- I mean, not capacity, availability each year.

These plants, during the last ten years, when combined together, never dropped below the 70 percent number that we have here, although it got very, very close in one year, if I remember, on a combined basis, because not only did the two -- one or two went down for a substantial time, the other plants were having some problems at the same time, so there was a substantial reduction in availability. But even in that worst year, they didn't go below 70 percent.

When we went to the company and tried to talk to them about this, we said, Well, we could give you a reward, you know, a scenario that gave you benefits and minuses, which is what the PRAM had had in it. In other words, it chose an 85 percent number. If it did better than 85 percent, the company got to keep the benefits; if it went below 85 percent, it cost them money. We asked them whether that's what they wanted. They said no. We said, Okay, we still want to protect against very bad years. And after working this out, this was a mechanism that only looked at years in which there was a substantial hit in one of those plants, probably six months, along with the rest of the normal outages of those things.

You asked what type of availability, you know, did we consider, you know --

COMMISSIONER OSHIE: I was --

MR. LOTT: -- the reasons for the availability and shortage.

COMMISSIONER OSHIE: Right, exactly, Mr. Lott.

MR. LOTT: And obviously, if the company had a very good reason for an availability, you know, the plants going down, such as -- this is something they would probably know about ahead of time, and that's something they could bring to the Commission in one of these rate case-only proceedings.

I'm trying to think of, in my own mind, we were trying to think about what type of events would take this out. Obviously, a major breakage in one of their turbines, the structures. Something would have to severely happen in one of those plants. And in fact, they did, in the early years of Colstrip Three and Four, have two major outages at Three and Four, I believe. I can't remember which ones went down. Three went down before Four came in for a six-month period, and I think Four went down for another six-month period, or something like that, back in the late '80s. These are very major outages.

And again, it's the availability. It's not the capacity factor. If for some reason these plants aren't running, but are available to run, this thing does not apply. It's only when they can't run. And so therefore, I'm trying to think, politically, for example, maybe, if for some reason, for air reasons, they were told they couldn't run because they didn't meet clean air requirements, I think the company would probably have to file a rate case, you know, a power cost-only rate proceeding immediately to change the results. I think that if there were some other major reason why one of these plants went down, you know, something that stopped Colstrip from being operable for some reason or another, other than just a major break at one of these plants, then I think the company would probably come before the Commission with some type of request. I mean, that was -- I mean, we were trying to -- but I can't think of what that situation would be, but --

MR. LAZAR: The genesis of this language is the prior Commission orders in the '81 Puget proceeding, U-8141, where the ECAC was created and then eliminated, the '88 water power PCA case, and the '99 water power Avista general rate case, where the Commission made it very clear in the multi-part test that a PCA mechanism should be weather-related. The unavailability of Colstrip, should it occur, is not likely to be weather-related.

So by normalizing Colstrip availability, as was done in the PRAM, we take that non-weather factor out of the calculation, and that's part of the reason that I testified earlier that I think it's very unlikely that this mechanism will trigger without a corresponding significant weather event that the public would understand. There are non-weather things tracked in here, but a bunch of the big ones have been normalized out.

COMMISSIONER OSHIE: That's it. Thank you.

MR. ELSEA: Well, I might add that

sometimes Colstrip is unavailable to us because of weather conditions such as fires in Montana, where we can't get the power out of Montana to the state of Washington.

COMMISSIONER OSHIE: And would that trigger the adjustment clause under paragraph six?

MR. ELSEA: I think --

COMMISSIONER OSHIE: That's really -- that's the heart of my question --

MR. ELSEA: Right.

COMMISSIONER OSHIE: -- whether a work stoppage or other force majeure occurrence would trigger the language, operable language within paragraph six?

MR. ELSEA: Yes, I agree with Mr. Lott that it would trigger it, but in those circumstances, the company would probably come in for a resource-only rate case.

The number is also, just to reiterate, the availability number of 70 percent, it's all of -- all four units of the plant out for three months, or two of the units out for five or six months, which can happen, but is unlikely.

MR. LAZAR: The corresponding line in the exhibit, Exhibit A-1, line five, is the production rate base. That is, the investment in these plants remains in rate base and a component of rates throughout the mechanism. And what this provision does is it provides that the ratepayers are assured of getting something for that payment.

A problem that we had in the ECAC is when Colstrip went down, the fixed costs remained in rates and the replacement power costs for the outage flowed through the ECAC and, in our opinion, the ratepayers were paying twice for power they only received once. This provides assurance that the ratepayers will pay once and only once for the power they receive.

COMMISSIONER OSHIE: Okay. Thank you.

CHAIRWOMAN SHOWALTER: This really is my last question, I think. On page seven of the agreement, paragraph 15, this is a sentence that begins with, Unless otherwise ordered by the Commission, and then there follow two phrases. One is changes in rates to PCA shall be charged on a basis, and then the second is, and changes in rates attributable to adjustments in the power cost rates shall be charged, et cetera.

And my question is does the phrase "unless ordered by the Commission" apply to both parts of the sentence, both phrases starting with the words "changes in rates?"

MR. QUEHRN: Yes.

CHAIRWOMAN SHOWALTER: Thank you.

JUDGE MOSS: Okay. I have one more. I guess it was Friday, Mr. Gaines testified briefly and punted the ball. He mentioned that there were three things about the PCA that were of particular significance to the company, and my notes reflect that one was the $40 million cumulative cap in the first four years, the second was the accelerated power cost rate review, and we've talked a good bit about those today. The third, I believe, was cost and benefits regarding the hedging mechanism. And I was -- I want to ask to be pointed to the parts or part or parts of the settlement terms that he was referring to with that last point.

MR. LOTT: I believe Mr. Gaines was talking about he wants to talk about the hedging activities that the company might be able to do. I don't think there's anything in this statement that says exactly -- I mean, the company hedges purchases today, and those are costs that the company incurs related to the purchase of power, and they would be in the 555 account, which is purchased power account.

They also hedge fuel costs. As you

remember, we were talking about that in the interim portion of this case, they've hedged substantial portions of the fuel costs. So those type of hedging costs would obviously flow directly into the mechanism, because those costs would be either the fuel expense or they would be the purchased power cost that the company's currently talking about.

Mr. Gaines has again and again brought up the subject of wanting to discuss the possibilities of doing different types of hedging activities. His plan was to talk -- have a -- he wants to sit down with some of the other parties, in particular, Staff and anybody else that wants to, and go over the type of activities the company thinks that they can do and talk about whether those are part of power costs. And that would also be part of this integrated resource planning discussions that would be taking place.

Now, I would -- maybe Mr. Story or Mr. Elsea can talk more about what he was talking about, but that is the way Staff recalls the discussions on hedging.

MR. STORY: Yeah, Mr. Lott is correct. There are a lot of costs in the power cost accounts that we've identified for the PCA that would fall under the definition of hedging, and we just want to make sure that everybody's clear as to the type of hedges that would be allowed in the PCA. To do that, we're going to meet with Staff and other interested parties within the next few weeks to go through those and identify the types of hedges that we're talking about to go into the PCA. It will mean that for hedges that are considered more risky, that they would consider staying on the company's side, that we would have to identify them out of those accounts.

JUDGE MOSS: Okay. But there's nothing specific in the mechanism that speaks to the point. Okay, fine.

MR. STORY: No.

JUDGE MOSS: Thanks. Any other questions from the bench? Do the parties have anything further to offer for our record at this time?

MR. QUEHRN: Your Honor, I have just a procedural question with respect to the bench requests that was handed out.

JUDGE MOSS: Yes.

MR. QUEHRN: In terms of responding to this request, should our responses be regarding what I think would be Exhibit 576?

JUDGE MOSS: Actually, that's right. 576

is the next exhibit number, and those will be the responses to bench requests. And I didn't give them any special designation, so --

MR. QUEHRN: And then it is a request to all parties, not just to the company, it appears.

JUDGE MOSS: I directed it to all parties, because our experience in this proceeding has been that sometimes a question will prove more appropriate for one party than another. But the company should take the principal initiative in assuring that all the questions are responded to. And I suppose in this vein I should say, too, I have included tomorrow's date as -- I'll call it an aspirational date. I'm sure the company will be as interested as we are in getting the answers to the Commission at the earliest possible point in time, so we probably won't fine you a thousand dollars a day or anything if it takes a little extra time, but --

MR. QUEHRN: We will respond promptly, Your Honor.

JUDGE MOSS: Mr. Cedarbaum.

MR. CEDARBAUM: I guess maybe you've answered my question, but it was also with respect to the bench requests. It sounds like you're expecting -- or are you expecting one answer from the company, and that we should try to get input into that answer to the best we can?

JUDGE MOSS: Yeah, I want to be flexible here. The preference is to have one answer. If the parties have some disagreement, though, or if somebody feels like an answer is not complete or what have you, then certainly they would have the opportunity. That's the other point, is I don't want to cut you off from the opportunity if you have something to say on the question.

MR. CEDARBAUM: Okay. Would it be then appropriate if -- we can try to work with the company and hopefully they can provide us drafts and we'll work back and forth, but if they were to provide responses tomorrow and we wanted to add to that, could we do that the next day?

JUDGE MOSS: Sure, but you might just want to have a bench request collaborative in the spirit of the proceedings. All right. Do counsel have anything further? All right. The witnesses are excused. Appreciate your testimony very much in this and other panels, for some of you. Our -- well, I think, in light of the outstanding bench requests, I don't think -- I think the only other exhibits to be furnished, Mr. ffitch, would be the public comments, which you'll get to me in due course?

MR. FFITCH: That's correct, Your Honor. They're being prepared and sent out to you today.

JUDGE MOSS: All right. Well, I'll say that we are standing in recess, in light of the fact that we do have some more matters coming into the record. One further thing.

CHAIRWOMAN SHOWALTER: Well, just -- there was an unanswered question about transmission revenues, and we could either add to our bench request when we file it or you can work it in somehow, but I think the expectation was you were going to respond to that.

MS. HARRIS: May I ask a clarification on the RTO type? Are you looking at the revenues or the costs of transmission? Earlier today, we were talking about the different costs of transmission, and then later on this afternoon it was on the different revenues maybe that we would receive for our transmission facilities. Is it both, Chairwoman?

CHAIRWOMAN SHOWALTER: I've now forgotten where this came up, but there was -- in a portion -- it was a table, had to do with the table of establishing revenues, and there was -- there were some transmission -- at the moment, I don't remember if it was costs or revenues -- put one in one place and some others in the other place. And my question was how would these be treated or affected if RTO West, as proposed, came into being.

You are welcome to take the question for what it is. If you see meaning in the question and factors at issue both in this settlement and potentially in RTO West, the question really is what's the potential interrelationship.

MS. HARRIS: Okay, thank you.

JUDGE MOSS: And I don't see any reason why the response to that can't be included in the response to the bench requests. You understand the question?

MS. HARRIS: I understand the question.

JUDGE MOSS: All right. As I mentioned earlier, too, we may need to supplement the bench requests. If so, I'll get an official copy out today and I'll e-mail that, as well, so people will have that right away if we do supplement it. What you have now is a courtesy copy. You'll notice it's unsigned.

All right. If there's nothing further, any closing remarks from the bench?

CHAIRWOMAN SHOWALTER: Well, you tried very hard and did your part, and we're trying very hard and hope to do ours.

MR. QUEHRN: Thank you.

JUDGE MOSS: Thank you very much. We're in recess.

(Proceedings adjourned at 3:12 p.m.)