EXHIBIT NO. RG-53HCT
DOCKET NOS. UE-090704/UG-090705
2009 PSE GENERAL RATE CASE
WITNESS: ROGER GARRATT

BEFORE THE
WASHINGTON UTILITIES AND TRANSPORTATION COMMISSION

WASHINGTON UTILITIES AND TRANSPORTATION COMMISSION, Complainant, v. PUGET SOUND ENERGY, INC., Respondent.	Docket No. UE-090704 Docket No. UG-090705

PREFILED REBUTTAL TESTIMONY (HIGHLY CONFIDENTIAL) OF ROGER GARRATT ON BEHALF OF PUGET SOUND ENERGY, INC.

REDACTED
VERSION

DECEMBER 17, 2009

PUGET SOUND ENERGY, INC.

PREFILED REBUTTAL TESTIMONY (HIGHLY CONFIDENTIAL) OF ROGER GARRATT

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PUGET SOUND ENERGY, INC.

PREFILED REBUTTAL TESTIMONY (HIGHLY CONFIDENTIAL) OF ROGER GARRATT

I. INTRODUCTION

Q. Are you the same Roger Garratt who provided in this proceeding prefiled direct testimony, Exhibit No. RG-1HCT, on May 8, 2009, on behalf of Puget Sound Energy, Inc. ("PSE")?

A. Yes.

Q. What is the purpose of your prefiled rebuttal testimony?

A. First, this rebuttal testimony responds to the direct testimony of Scott Norwood, Exhibit No. SN-1HCT, witness for the Public Counsel section of the Washington State Attorney General's Office ("Public Counsel"), with respect to the prudence of PSE's acquisition of the Mint Farm Energy Center. Public Counsel presents arguments opposing PSE's acquisition by mischaracterizing PSE's due diligence findings, taking portions of the record out of context, and selectively elevating particular criteria without considering the findings as a whole. In doing so, Public Counsel misleads the Commission about the acquisition of the Mint Farm Energy Center and PSE's motives for selecting the resource.

Second, this prefiled rebuttal testimony provides an update regarding the total acquisition cost of the Mint Farm Energy Center, which is just under $250 million (including $2.7 million in remaining post-acquisition upgrades).

Finally, this prefiled rebuttal testimony updates the Commission regarding the completion of the Wild Horse Wind Expansion Project. PSE completed the Wild Horse Wind Expansion Project on time and within the budget approved by PSE's Board of Directors. PSE completed the Wild Horse Wind Expansion Project three weeks prior to the projected online date of December 1, 2009. The budget approved by PSE's Board of Directors for the Wild Horse Wind Expansion Project was $107.5 million. The final cost of the Wild Horse Wind Expansion Project is $98.4 million and the levelized cost is $[redacted]/MWh.

II. PSE'S QUALITATIVE ANALYSIS SUPPORTS THE ACQUISITION OF THE MINT FARM ENERGY CENTER

A. <u>Calendar Year 2008 Was a Competitive Environment for Acquiring New Resources to Meet Energy and Capacity Needs in the Pacific Northwest</u>

Q. Please summarize the process used by PSE to acquire the Mint Farm Energy Center.

A. Based on the identified need in PSE's 2007 Integrated Resource Plan ("<u>IRP</u>"), PSE issued a Request for Proposals for all Generation Sources in January 2008 (the "<u>2008 RFP</u>"). PSE asked interested parties to respond by February 29, 2008.

PSE received 31 proposals, including an offer from Wayzata Investment Partners, LLC ("Wayzata") to purchase the Mint Farm Energy Center.

In May 2008, at the conclusion of Phase I of the RFP evaluation process, PSE selected a "candidate" short list. Thirteen candidate proposals, including the Mint Farm Energy Center, moved to Phase II of the evaluation process for portfolio evaluation and additional due diligence.

Concurrent with the Phase II due diligence, PSE initiated discussions with Wayzata to begin exploring a letter of intent and term sheet, mindful of the ongoing evaluation of the other resource alternatives.

At the conclusion of Phase II, nearly all of the candidate projects continued to evaluate well quantitatively in the scenario analysis results. The Mint Farm Energy Center was among the projects identified as having the lowest reasonable cost and risk, together with two wind power purchase agreements and a short-term system power purchase agreement.

On June 5, 2008, PSE and Wayzata Opportunities Fund, LLC executed a non-binding Letter of Intent and Term Sheet to acquire the Mint Farm Energy Center. On September 24, 2008, PSE and Mint Farm Energy Center LLC, then a subsidiary of Wayzata Opportunities Fund, LLC, executed a Membership Interest Purchase Agreement for the purchase of the Mint Farm Energy Center. The acquisition closed during the first week of December 2008, and PSE acquired 100% of the limited liability company interests of Mint Farm Energy Center LLC, including all rights, liabilities, permits, licenses and real, personal and intangible property owned or held by Mint Farm Energy Center LLC relating to the facility as of the closing date. Immediately following the acquisition of the membership interests, PSE dissolved the Mint Farm Energy Center, and all assets and obligations under the Mint Farm Energy Center became those of PSE.

Q. Please summarize the market environment during this time.

A. The Mint Farm presentation to the Board of Directors describes the market environment during the 2008 RFP and Mint Farm due diligence periods as follows:

> The market continues to experience significantly higher capital costs across all technologies fueled by the continued rise in global energy and commodity costs. Dramatically increased demand from the rapidly developing BRIC nations (Brazil, India and China) has driven up the price of oil and core construction commodities such as steel and copper. The effect on energy supply is a marked increase in both fuel costs and costs of new construction. PSE's resource cost comparison provides a look at the 20-year levelized cost at PSE's 2004, 2006 and 2008 RFPs. PSE's 2008 RFP has seen levelized cost increases of 39 percent on average for gas projects proposed compared to those proposed in the 2006 RFP (See Figure 2). Accordingly, the risk of cost escalation of future generating capacity is extremely high.

Exhibit No. RG-7HC at page 31.

In addition to rising commodity prices, an increased demand for electric generation capacity intensified the competition for resources. Concurrent with PSE's 2008 RFP at least six other utilities were conducting requests for proposal solicitations, namely B.C. Hydro, Idaho Power Company, Portland General

Electric Company, PacifiCorp, Southern California Edison, and Pacific Gas & Electric Company. This demand for resources, combined with a shortage of available modern merchant projects at prices discounted from new construction, provided equipment manufacturers and construction contractors ample leverage to increase prices and boost margins.

At the time PSE began its 2008 RFP process, the Mint Farm Energy Center was one of three remaining merchant gas plants from the early 2001-2002 construction boom of combined cycle combustion turbine plants in the Pacific Northwest. Early during PSE's RFP evaluation process, this number was reduced by one when PacifiCorp announced its acquisition of the Chehalis Generating Facility, a 520 MW natural gas-fired combined cycle plant. *See* RG-7HC at page 40.

The wind industry experienced similar competitive market forces. Wind projects were being built quickly, wind developers charged increased premiums for new wind resource contracts, and wind turbine supply for future purchases was severely limited. Most of the major wind turbine suppliers were fully booked with orders through mid-2010.

Q. How did this competitive market climate affect PSE's 2008 RFP process?

A. The competitive climate affected both PSE's process and several individual proposals. PSE's 2005 RFP quantitative screening and qualitative due diligence processes took six months to complete. During that RFP, several of the best proposals were withdrawn from consideration because they were sold or contracted to other utilities in the Pacific Northwest or California. PSE recognized that a shorter evaluation timeline would improve PSE's ability to compete for the best resources in the marketplace. As a result, PSE identified areas where it could streamline its analytical processes to respond to favorable resources more quickly. These process improvements enabled PSE to shorten the analytical period for the 2008 RFP from six months to four months. As a result, PSE planned to finish all analyses by July 2008. This effort was successful, and PSE selected its Final Short List on July 9, 2008.

This shortened timeline proved useful in the 2008 RFP at a time when there were rapid developments in the market. As discussed above, PacifiCorp purchased the Chehalis Generating Facility early in PSE's RFP evaluation process. Additionally, developers withdrew two wind project proposals from consideration before the end of Phase II of PSE's RFP evaluation process. These occurrences reinforce the fact that calendar year 2008 was a competitive environment for acquiring new resources to meet energy and capacity needs in the Pacific Northwest.

B. <u>PSE Had Both a Capacity and Energy Need.</u>

Q. Did PSE have a clear need for new capacity resources during the 2008 RFP?

A. Yes. As discussed in the Prefiled Rebuttal Testimony of Mr. W. James Elsea, Exhibit No. WJE-21HCT, PSE updated its capacity and energy need from the 2007 IRP for the 2008 RFP. The updated capacity need in the 2008 RFP was

208 MW in 2011, 760 MW in 2012, and greater than 800 MW in 2015. The Mint Farm Energy Center was the only acceptable natural gas resource on PSE's Candidate Short List that filled PSE's need in 2011.

Q. Why was the Mint Farm Energy Center the only acceptable natural gas resource on PSE's Candidate Short List that filled PSE's need in 2011?

A. During Phase II of the 2008 RFP, PSE evaluated five natural gas resources—three ownership proposals and two tolling power purchase agreements. Only four of the five resources were selected for either the Final Short List or the Continuing Investigation List. *See* Exhibit No. RG-3 at pages 211-16. Of the remaining four natural gas resource proposals, the Mint Farm Energy Center was the only resource available to meet PSE's need in 2011.

The [redacted] power purchase agreement was not a suitable fit to meet PSE's need in 2011 because PSE has a long-term tolling power purchase agreement for the output from the facility through [redacted]. Thus, the [redacted] power purchase agreement could not have met PSE's need in 2011.

The [redacted] ownership proposal was not a suitable fit to meet PSE's need in 2011 because firm transmission is not available until approximately 2015, when the Bonneville Power Administration projects that it will complete its planned upgrades to the I-5 corridor.

The [redacted] ownership proposal was not a suitable fit to meet PSE's need in 2011 because it required the construction of a new generation facility, which could not be completed in the desired time period.

The Mint Farm Energy Center, on the other hand, has adequate transmission and gas transportation, is permitted to be a baseload resource, has a low heat rate, has low ownership risk and fills both PSE's short-term need in 2011 and PSE's long-term need. As a result, the Mint Farm Energy Center was the only acceptable resource acquisition to meet PSE's needs in 2011.

C. Resource Acquisition Decisions Must Focus on Long-Term Value

Q. Why did PSE purchase Mint Farm even though the acquisition created a surplus capacity need in 2009 and 2010?

A. PSE's resource acquisition process analyzes the long-term value that a new resource adds to PSE's electric resource portfolio because the resources that PSE acquires through that process will remain a part of PSE's electric portfolio for one, two, three, and sometimes four decades. As Commission Staff acknowledges in its testimony, the resource acquisition process is "lumpy," and acquisitions do not always perfectly align with load demand, whether those resources are currently in service or being constructed. *See* Exhibit No. DN-1HCT at page 15, line 19, through page 16, line 7. PSE must focus on the long-term value of the resource, rather than risk losing resources that have long-term value for the sake of trying to time resource acquisitions perfectly. It would be improper for PSE to reject a proposal simply because its attributes provide extra short-term capacity.

Q. Does Public Counsel agree that PSE must focus on the long-term benefits of a resource?

A. Public Counsel's testimony does not clearly address the long-term benefits of a resource. Instead, Public Counsel erroneously asserts that PSE did not have a need to acquire the Mint Farm Energy Center because the plant would create short-term "surplus capacity on PSE's system through 2011." Exhibit No. SN-1HCT at page 9, lines 5-6. However, Public Counsel does acknowledge that the Mint Farm Energy Center "may ultimately benefit PSE's customers in the long run." Exhibit No. SN-1HCT at page 21, line 4.

D. <u>Quantitative and Qualitative Analyses Support PSE's Acquisition of the Mint Farm Energy Center</u>

Q. Is Public Counsel's suggestion that "three other gas-fired bids were higher than Mint Farm" valid?

A. No. Public Counsel's suggestion that "three other gas-fired bids were higher than Mint Farm" is invalid for at least three reasons.

First, as discussed in the Prefiled Rebuttal Testimony of Mr. W. James Elsea, Exhibit No. WJE-21HCT, Public Counsel inappropriately focuses on portfolio benefit and portfolio benefit ratio to the exclusion of levelized cost. As discussed in Mr. Elsea's rebuttal testimony, Public Counsel's failure to consider all of the quantitative analyses together takes the quantitative analyses out of context and leads to the false conclusion that PSE did not act prudently in acquiring the Mint Farm Energy Center.

Second, quantitative analyses alone should not dictate the proposals that PSE should acquire. PSE's resource acquisition decisions also reflect a variety of qualitative and commercial analyses; the quantitative analyses are just one component of PSE's entire analysis. Public Counsel's suggestion that "three other gas-fired bids were higher than Mint Farm" is overly simplistic and focuses exclusively on the portfolio cost benefit metric to the exclusion of any other qualitative or quantitative consideration.

Third, Public Counsel ignores the fact that PSE's decision to acquire the Mint Farm Energy Center is not a rejection by PSE of any other proposal identified on the Final Short List or the Continuing Investigation List.

1. <u>Public Counsel Improperly Focuses Solely on the Results of Only Two of the Quantitative Analyses Performed by PSE</u>

Q. What did PSE's quantitative analysis demonstrate with respect to the long-term value of the Mint Farm Energy Center?

A. As discussed in the Prefiled Direct Testimony of Mr. W. James Elsea, Exhibit No. WJE-1HCT, the Prefiled Rebuttal Testimony of Mr. W. James Elsea, Exhibit No. WJE-21HCT, and in the presentation to the Board of Directors, Exhibit

No. RG-7HC, the Mint Farm Energy Center had one of the lowest levelized costs per MWh of all of the natural gas proposals considered in Phase II of the 2008 RFP. The portfolio benefit of $44 million and benefit ratio of 0.05 for the Mint Farm Energy Center also documented that the facility saves costs to the customers when compared to the generic portfolio of resources.

These quantitative results reflect that the Mint Farm Energy Center was acquired at more than a 30% discount from new construction costs, is a low heat rate plant, and was built and designed to be a baseload resource. PSE has identified future energy and capacity needs, and the Mint Farm Energy Center will play a critical role in fulfilling these resource needs.

Q. How does Public Counsel respond to this quantitative analysis?

A. Public Counsel focuses much attention on whether the Mint Farm Energy Center was the least cost natural gas proposal in the Phase I and Phase II analyses in the 2008 RFP. Public Counsel implies that PSE should have acquired the [redacted] power purchase agreement because (i) other proposals (notably the [redacted] power purchase agreement proposal) have higher portfolio benefits and portfolio ratios than the Mint Farm Energy Center and (ii) the [redacted] power purchase agreement proposal provides "more than double the system economic benefits attributed to the Mint Farm project." Exhibit No. SN-1HCT at page 13, lines 7-8.

Q. How does Public Counsel reach its conclusion that "the estimated system production cost benefits provided by three other gas-fired bids were higher than Mint Farm, and the expected economic benefits of the [redacted] PPA bid were more than double the level of estimated benefits for the Mint Farm acquisition"? (Exhibit No. SN-1HCT at page 20, lines 7-11.)

A. To reach this conclusion, Public Counsel improperly focuses exclusively on the portfolio benefits and portfolio benefit ratios developed by PSE as part of its quantitative analysis. *See* Exhibit No. SN-1HCT at page 11, line 15, through page 12, line 3.

Q. What criteria does PSE use to analyze the cost of a proposed resource?

A. PSE considers two broad categories in analyzing the cost of a proposed resource: (i) resource cost and (ii) portfolio cost impact. Public Counsel focuses exclusively on the last cost category. As discussed in the Prefiled Rebuttal Testimony of Mr. W. James Elsea, Exhibit No. WJE-21HCT, portfolio cost is just one component of PSE's quantitative analysis.

Q. What factors does PSE consider in analyzing resource cost?

A. In analyzing resource cost, PSE prefers proposals that provide the lowest reasonable cost throughout the project life, taking into account the price of the proposal and other factors that affect PSE's overall cost. Such factors include, but are not limited to the following:

(i) capital cost,

(ii) financing cost,

(iii) operation and maintenance cost,

(iv) fuel and fuel transportation cost,

(v) fixed and variable power purchase agreement cost,

(vi) transmission cost,

(vii) ancillary services,

(viii) integration costs,

(ix) transmission system upgrades,

(x) cost to rebalance debt/equity ratio for imputed debt and consolidated debt,

(xi) cost of credit facilities,

(xii) transaction costs and other management costs, etc.,

(xiii) cost to meet environmental compliance, including capital improvements and/or capacity limitations and restrictions, and

(xiv) renewable energy credits.

Public Counsel's analysis fails to address many, if not all, of the resource costs listed above.

Q. What factors does PSE consider in analyzing portfolio cost impact?

A. In analyzing portfolio cost impact, PSE prefers proposals and combinations of proposals that result in the lowest impact on PSE's revenue requirements and rates when included in PSE's existing generation resource portfolio. Although Public

Counsel's analysis does address portfolio cost impact, it inappropriately does so to the exclusion of all other cost considerations.

Q. Did PSE present evidence of the various resource cost considerations that PSE considered?

A. Yes. The Prefiled Direct Testimony of Mr. W. James Elsea, Exhibit No. WJE-1HCT, the supporting exhibits to such prefiled direct testimony, the Prefiled Rebuttal Testimony of Mr. W. James Elsea, Exhibit No. WJE-21HCT, the supporting exhibits to such prefiled rebuttal testimony, and the RFP overview documentation, Exhibit No. RG-3HC, provide extensive evidence regarding the resource cost considerations that PSE considered. Additionally, the workpapers of Mr. W. James Elsea provide several DVD-ROMs of raw data and modeling results used by PSE in its analysis. Given the extensive quantitative analysis provided by PSE in support of its acquisition of the Mint Farm Energy Center, it is unclear why Public Counsel focuses on one cost category to the exclusion of all others. In short, Public Counsel's quantitative analysis is incomplete and fails to consider all of the evidence presented.

2. Public Counsel Ignores Most of the Qualitative Analyses Performed by PSE

Q. Does Public Counsel suggest that PSE failed to demonstrate the qualitative benefits of acquiring the Mint Farm Energy Center?

A. Yes. Public Counsel asserts that PSE's presentations to its Board of Directors "appear to present an unduly favorable assessment of the Mint Farm facility which deemphasizes concerns identified by the Mint Farm due diligence analyses." Exhibit No. SN-1HCT at page 13, lines 8-10. In an attempt to support this assertion, Public Counsel cites snippets of a due diligence report prepared by North American Energy Services Company ("NAES"). However, Public Counsel fails to acknowledge the overall assessment of NAES, discuss the due diligence performed by PSE itself and its other consultants, or take into account the plans that PSE included to address the few areas of concern raised by NAES as cited by Public Counsel. Moreover, Public Counsel only minimially references the extensive, 230-page presentation made by PSE to the Board of Directors that fully addresses all aspects of the acquisition, including the few areas of concern cited by Public Counsel. Again, Public Counsel's suggestion is overly simplistic and selectively focuses only on the few concerns raised by NAES without regard for PSE's proposed mitigations.

a. The NAES Due Diligence Report Did Not Raise Any Significant Concerns With Respect to the Mint Farm Energy Center

Q. With respect to the Mint Farm Energy Center, did the NAES due diligence report raise significant concerns that rendered its overall assessment of the plant as unattractive?

A. No. As discussed in detail below, the NAES due diligence report did mention issues with specific components of the plant, but none of these issues, individually or in the aggregate, caused NAES to render its overall assessment of the plant as unattractive. Please see Exhibit No. RG-54 for a copy of the NAES due diligence report. In fact, the NAES due diligence report concluded as follows:

> The plant facilities and equipment appeared to be in good condition, particularly considering that construction of the plant was suspended for approximately four years. There were no obvious signs or indications of leaks and housekeeping was good. The construction punchlist was down to one item when the due diligence visit took place. From an operational perspective, the plant is essentially brand new with little run time.

Exhibit No. RG-54 at page 3. Given this conclusion, it is difficult to understand why Public Counsel would suggest that PSE misled its Board of Directors in any fashion when it provided the following conclusion in its report to the Board of Directors, which is substantively similar to the conclusion of the NAES due diligence report:

> The overall conclusion of PSE's technical due diligence team is that the plant is clean, quiet, well designed, and in near new condition. While plant construction was interrupted for a period of approximately five years, components of the plant that had been installed were properly laid up to prevent corrosion.
>
> Operations and maintenance at the plant appear to have been carried out by conscientious and experienced personnel guided by good procedures.

Exhibit No. RG-7HC at page 168.

Q. Did PSE address in its report to the Board of Directors the issues of concern raised in the NAES due diligence report and cited by Public Counsel?

A. Yes. PSE addressed in its report to the Board of Directors the issues of concern raised in the NAES due diligence report and cited by Public Counsel. *See generally* Exhibit No. RG-7HC. As discussed below, PSE also included projected costs to mitigate such issues in the report.

b. <u>Public Counsel Fails to Acknowledge Many of the Qualitative Factors Considered by PSE in Acquiring the Mint Farm Energy Center</u>

Q. Does Public Counsel acknowledge all of the qualitative factors considered by PSE in acquiring the Mint Farm Energy Center?

A. No. Public Counsel fails to consider many of the qualitative factors considered by PSE in acquiring the Mint Farm Energy Center.

Q. What qualitative factors does PSE consider in acquiring resources?

A. PSE employs a multifaceted and structured evaluation process to assess the merits of proposals with regard to meeting PSE's need. PSE considers a number of quantitative and qualitative factors designed to compare proposals with diverse attributes.

The quantitative factors, summarized above, are discussed in the Prefiled Direct Testimony of Mr. W. James Elsea, Exhibit No. WJE-1HCT, the supporting exhibits to such prefiled direct testimony, the Prefiled Rebuttal Testimony of

Mr. W. James Elsea, Exhibit No. WJE-21HCT, and the supporting exhibits to such prefiled rebuttal testimony.

Additionally, PSE evaluates each proposal according to the following qualitative criteria: (i) compatibility with resource need; (ii) risk management; (iii) public benefits; and (iv) strategic and financial considerations.

Q. What criteria did PSE use to analyze the compatibility of a proposed resource with PSE's resource need?

A. PSE considered the following criteria to analyze the compatibility of a proposed resource with PSE's resource need:

- timing;
- resource match to monthly need;
- match to monthly need through contract;
- operational flexibility;
- performance within existing PSE generation portfolio; and
- resource mix/diversity.

Please see Exhibit No. KJH-6 at pages 17-18 for further discussion regarding these compatibility considerations. Public Counsel fails to consider all of these compatibility considerations, with the exception of timing, in asserting that PSE's acquisition of the Mint Farm Energy Center was not prudent.

Q. What criteria did PSE use to analyze risk management issues associated with a proposed resource?

A. PSE considered the following criteria to analyze risk management issues associated with a proposed resource:

- status and schedule;
- price volatility;
- resource flexibility and stability;
- resource technology;
- long-term flexibility;
- project risk;
- impact on PSE's overall risk position;
- environmental and permitting risk;
- respondent risk;
- ability to deliver proposed status and schedule;
- experience and qualification of the project team;
- status of transmission rights;
- managerial control;
- security and control; and
- federal regulatory approvals.

Please see Exhibit No. KJH-6 at pages 20-22 for further discussion regarding these risk management considerations. Public Counsel fails to appropriately consider all of these risk management considerations in asserting that PSE's acquisition of the Mint Farm Energy Center was imprudent.

Q. What criteria does PSE use to analyze public benefit issues associated with a proposed resource?

A. PSE considers the following criteria to analyze public benefit issues associated with a proposed resource:

- environmental impacts;
- resource location; and
- community impacts.

Please see Exhibit No. KJH-6 at page 23 for further discussion regarding these public benefit considerations. Public Counsel fails to consider all of these public benefit considerations in asserting that PSE's acquisition of the Mint Farm Energy Center was imprudent.

Q. What criteria does PSE use to analyze strategic and financial issues associated with a proposed resource?

A. PSE considers the following criteria to analyze strategic and financial issues associated with a proposed resource:

- capital structure impacts;
- future exposure to environmental regulations and/or taxes; and
- guarantees and security.

Please see Exhibit No. KJH-6 at page 24 for further discussion regarding these strategic and financial considerations. Public Counsel fails to consider two of the these three strategic and financial considerations in asserting that PSE's acquisition of the Mint Farm Energy Center was imprudent. Indeed, Public Counsel inappropriately suggests that PSE should exclude the effect of imputed debt for power purchase agreements, despite Commission rules and precedent suggesting that the consideration of such effects are not only important but mandatory.

Q. Did PSE present evidence with respect to the various qualitative considerations that PSE considered?

A. Yes. My prefiled direct testimony and supporting exhibits in this proceeding provided extensive evidence regarding the qualitative considerations that PSE considered. Despite the extensive qualitative analysis provided by PSE to support its acquisition of the Mint Farm Energy Center, it is difficult to understand why Public Counsel would focus solely on a few minor issues in one consultant's due diligence report to the exclusion of all other considerations. In short, Public Counsel's qualitative analysis is incomplete and fails to consider all of the evidence presented.

Q. Did PSE consider the fact that the Mint Farm Energy Center is located in a flood plain during PSE's due diligence process?

A. Yes. In PSE's Response to Commission Staff Data Request No. 177, PSE stated that it “did not specifically assess potential risk due to the Columbia River dike system during pre-purchase due diligence process.” PSE never intended to suggest that PSE failed to consider the fact that the Mint Farm Energy Center is located in a flood plain during PSE’s due diligence process. To be clear, PSE did not complete any additional risk assessment of flood hazards at the Mint Farm Energy Center above and beyond the assessment conducted by the U.S. Army Corps of Engineers in 2007. Please see Exhibit No. RG-55 for a copy of the 2007 report by the U.S. Army Corps of Engineers. This report reviews the dike conditions and ongoing maintenance activities in the Cowlitz County Consolidated Diking Improvement District No. 1, in which the Mint Farm Energy Center is located. The report concludes that “the levee and pumping plants appear to be in good condition” and that “the Columbia River Levee top elevation . . . is on average 3 or more feet above the minimum required levee for the 500 year storm event”. Exhibit No. RG-55 at page 2. Based in part on this report, PSE did not consider potential flood events to be a normal occurrence or requiring additional risk assessment, particularly given that the Mint Farm Energy Center is in the 500-year flood plain.

3. PSE's Decision to Acquire the Mint Farm Energy Center Is Not a Rejection of Any Other Resource

Q. Does the fact that PSE acquired the Mint Farm Energy Center mean that PSE rejected the other proposals identified on the Final Short List or the Continuing Investigation List?

A. No. The Mint Farm Energy Center acquisition does not preclude PSE from acquiring any other resources from either the Final Short List or the Continuing Investigation List. Indeed, PSE may acquire any of the resources on the Continuing Investigation List, provided that the resources remain available and the circumstances that originally motivated PSE to place those resources on the Continuing Investigation List rather than the Final Short List, are resolved.

Q. Why did PSE place the [redacted] tolling power purchase agreement proposal on the Continuing Investigation List?

A. PSE placed the [redacted] tolling power purchase agreement proposal on the Continuing Investigation List for a variety of reasons. First, PSE has an existing power purchase agreement with [redacted] for the output of the facility through [redacted]. [redacted]. Second, the [redacted] units are mid-range heat rate natural gas units, and PSE did not project that they would run as a baseload plant. Therefore, PSE would still have an energy need to fill by acquiring power from the market or acquiring another resource. Finally, PSE wanted to take additional time to understand the potential ancillary service and wind integration value that the [redacted] power purchase agreement proposal may provide.

Q. [redacted]?

A. [redacted]. [redacted]. [redacted].

Q. [redacted]?

A. [redacted]. [redacted]

[redacted]. [redacted]. [redacted]. [redacted]. As PSE's need increases substantially from 2012 to 2015 to 2020, a more optimal contract may turn out to be a short-term bridging agreement that fills PSE's capacity need until PSE can acquire or build the significant resources it needs to meet load.

Q. Why did PSE place the [redacted] ownership proposal on the Continuing Investigation List?

A. PSE placed the [redacted] ownership proposal on the Continuing Investigation List for reasons similar to the reason why PSE placed the [redacted] power purchase agreement on the Continuing Investigation List. The [redacted] have a mid-range heat rate and PSE did not project that they would run as a base-load plant. Therefore, PSE would still have energy need to fill by acquiring power from the market or acquiring another resource. Finally, PSE wanted to take additional time to understand the potential ancillary service and wind integration value that the [redacted] could provide.

Q. Why did PSE place the [redacted] ownership proposal on the Continuing Investigation List?

A. PSE placed the [redacted] ownership proposal on the Continuing Investigation List because there were too many commercial risks in 2008 to justify acquiring the project. The most compelling reason is that there is no firm transmission capacity available on BPA's system until BPA completes its I-5 transmission corridor upgrade, which BPA projects to complete in 2015. The [redacted] ownership proposal offered an option to purchase the plant in 2012. However, PSE would have to pay annual option payments and since the final cost of the project associated with this proposal would be adjusted by a capital cost inflation index, this posed a cost risk to PSE and its customers. In addition, option payments for an acquisition in 2013 would create significant credit risk for PSE. Finally, the proposal did not provide satisfactory transmission risk mitigation. PSE continues to monitor the [redacted] ownership proposal and BPA's transmission corridor upgrade.

Q. Why did PSE reject the [redacted] tolling power purchase agreement proposal?

A. PSE rejected the [redacted] tolling power purchase agreement proposal because the proposed contractual terms were not operationally acceptable to PSE. The proposal would have required PSE to make economic dispatch decisions based on the average monthly gas price. Because future gas prices are unknown, this proposal would have required PSE to assume unacceptable levels of risk to purchase energy from the facility. Additionally, other proposed dispatch elements were difficult for PSE to model; therefore, PSE's quantitative analyses likely underestimated costs associated with the proposal.

Q. Given these reasons to place three of the five gas resource evaluated in Phase II of the RFP on the Continuing Investigation List, will you please summarize why PSE decided to acquire the Mint Farm Energy Center?

A. Yes. PSE decided to acquire the Mint Farm Energy Center for the reasons described above. Furthermore, as stated in the presentation to the Board of Directors, there were six other RFPs underway in the region concurrent with PSE's 2008 RFP, which is an indication of the large and growing need for resources of all types in the region. *See* Exhibit No. RG-7HC at page 40. PacifiCorp had just purchased the Chehalis Generating Facility, one of the last in-service natural gas plants for sale on the open market. The number of RFPs on the market and the constant acquisitions of resources by other resource-deficit utilities illustrated the competitive nature of the market at the time PSE acquired the Mint Farm Energy Center. The Mint Farm Energy Center is a nearly new, low-cost, baseload resource that enables PSE to meet its energy and capacity needs today and tomorrow. Wayzata was motivated to sell, and PSE acquired the plant at more than a 30% discount compared to the cost to build a new plant. The quantitative analysis proved that Mint Farm would be a valuable addition to PSE's short and long-term portfolio needs and PSE believed that there was a very small likelihood that the Mint Farm Energy Center would still be available during PSE's next RFP.

E. PSE's Resource Acquisition Process Does Not Focus on Returns to Shareholders

Q. Did PSE unduly favor the Mint Farm Energy Center because the acquisition captures a return on equity for PSE's shareholders, whereas the [redacted] tolling power purchase agreement is a straight cost pass-through to customers?

A. No. Any suggestion that PSE unduly favored the Mint Farm Energy Center because the acquisition captures a return on equity for PSE's shareholders is not based on fact. PSE acquires projects solely based on the aforementioned qualitative and quantitative metrics. PSE's acquisition process focuses on (i) a resource's compatibility with PSE's resource need to meet load demand as determined in PSE's biannual IRP, (ii) a resource's short-term and long- term capital and operation and maintenance costs, and (iii) a resource's ability to minimize risk in both the short-term and long-term markets. PSE's resource acquisition process does not focus on returns to shareholders.

Q. Does Public Counsel provide any evidence to suggest that PSE unduly favored the Mint Farm Energy Center because the acquisition captures a return on equity for PSE's shareholders?

A. No. Public Counsel fails to provide any evidence to support its suggestion that PSE unduly favored the Mint Farm Energy Center because the acquisition captures a return on equity for PSE's shareholders.

Q. Does Public Counsel provide any evidence to indicate that the Mint Farm Energy Center would not benefit PSE's customers?

A. No. Public Counsel fails to provide any evidence to suggest that the Mint Farm Energy Center would not benefit PSE's customers. In fact, Public Counsel suggests that the Mint Farm Energy Center will be beneficial to ratepayers: ". . . the plant may ultimately benefit PSE's customers in the long run." Exhibit No. SN-1HCT at page 21, line 4. PSE projects that the Mint Farm Energy Center will benefit customers in both static and dynamic analyses, as well as different IRP scenarios.

F. PSE's Presentations to Its Board of Directors Accurately Reflected the Results of PSE's Due Diligence for the Mint Farm Energy Center

Q. Is Public Counsel's argument that "PSE's board presentations present an unduly favorable assessment of the Mint Farm facility which deemphasizes concerns identified by the Mint Farm due diligence" accurate?

A. No. PSE presented its Board of Directors with a comprehensive, accurate overview of the due diligence findings of both internal and external participants. PSE documented all noteworthy and necessary information in the presentation to the Board of Directors, without regard to whether the information presented the Mint Farm Energy Center in a favorable or unfavorable light.

Q. Is it reasonable to expect that all due diligence findings will be favorable for any given resource?

A. No. It is unreasonable to expect that all due diligence findings will be favorable for any given resource. No resource is perfect. The purpose of the due diligence process is to gain a better understanding of the history of a facility, its associated plant characteristics, the relative strengths and disadvantages of the resource, and any outstanding risks that PSE would have to manage if it were to acquire the resource.

To meet the Commission's prudence standard and PSE's resource standards, PSE has an obligation to document all favorable and unfavorable findings from its due diligence. PSE uses this information to address how it will mitigate outstanding risks if PSE acquires the resource. PSE fairly represented to its Board of Directors both the favorable and unfavorable characteristics of Mint Farm Energy Center and addressed how PSE would mitigate any material concerns. Public Counsel conveniently omits these mitigation plans in its prefiled response testimony.

Q. On what basis does Public Counsel attempt to support its claim that PSE presented an "unduly favorable assessment of the Mint Farm facility"?

A. Public Counsel quotes the following passage from PSE's presentation to its Board of Directors:

> The overall conclusion of PSE's technical due diligence team is that the plant is clean, quiet, well designed, and in near new condition. While the plant construction was interrupted for a period of approximately five years, components of the plant that had been installed were properly laid up to prevent corrosion.
>
> Operations and maintenance at the Facility appear to have been carried out by conscientious and experienced personnel guided by good procedures.

Exhibit No. SN-1HCT at page 13, lines 18-26 (quoting Exhibit No. RG-7HC at page 168). Public Counsel then attempts to identify pitfalls in PSE's assessment of the Mint Farm Energy Center by selectively quoting from the NAES due diligence report. Public Counsel fails, however, to acknowledge that the conclusion of the NAES due diligence report closely resembles the passage from PSE's presentation to its Board of Directors to which Public Counsel refers:

> The plant facilities and equipment appeared to be in good condition, particularly considering that construction of the plant

> was suspended for approximately four years. There were no obvious signs or indications of leaks and housekeeping was good. The construction punchlist was down to one item when the due diligence visit took place. From an operational perspective, the plant is essentially brand new with little run time.

Exhibit No. RG-54 at page 3.

Q. What issues identified in the NAES due diligence report does Public Counsel attempt to raise as issues of concern?

A. Public Counsel attempts to generate alarm by arguing that the presentation to PSE's Board of Directors did not address the following seven issues identified by the NAES due diligence report for the Mint Farm Energy Center:

(i) The NAES due diligence report expressed concerns that NAES was not allowed access to plant design, construction and operational data and operations personnel;

(ii) The NAES due diligence report expressed concerns that several important systems had not yet been fully commissioned, including the Evaporative Coolers, the Steam Augmentation and the Duct Burners;

(iii) The NAES due diligence report expressed concerns that NAES was unable to determine whether Cowlitz County has accepted the noise survey as proof that the plant complies with noise ordinances.

(iv) The NAES due diligence report expressed concerns that the economizer sections of the Heat Recovery Steam Generator ("<u>HRSG</u>") had experienced corrosion;

(v) The NAES due diligence report expressed concerns that the condenser experienced corrosion behind the coatings on the internal hotwell/condenser walls;

(vi) The NAES due diligence report expressed concerns that the Atlas Copco Gas compressors had failed three times since resumption of construction; and

(vii) The NAES due diligence report expressed concerns that there are no warranties on the plant equipment due to the suspension of construction and subsequent release agreements.

Q. Did PSE identify these seven issues in the presentation materials provided to its Board of Directors?

A. Yes. With the possible exception of one issue that was too minor to impose significant cost or risk to affect the acquisition decision, PSE communicated all of the material findings in the NAES due diligence report to its Board of Directors. *See generally* Exhibit No. RG-7HC.

Q. Does PSE share Public Counsel's concern that NAES was not allowed access to some technical data?

A. No. The inability of NAES to access some technical data reflects the nascent operating status of Mint Farm Energy Center during PSE's due diligence efforts. Indeed, the NAES due diligence report acknowledges that "NAES was unable to review plant monthly operating and maintenance reports (as the plant is so new, these essentially do not exist), DCS historian and plant performance data." Exhibit No. RG-54 at page 3. In short, operations of the plant at that point had been so limited that there was no substantial operating data for NAES to review.

Q. Does PSE share Public Counsel's concern that NAES was not allowed access to review design, construction and operational data for the technical due diligence of the Mint Farm Energy Center?

A. No. PSE knew when it retained NAES to conduct external technical due diligence for the Mint Farm Energy Center that NAES would likely not have access to design, construction and operational data. NAES is in the business of operating power generation facilities and, as mentioned in the presentation to the Board of Directors, NAES operates a Siemens-Fuji steam turbine generator in Calgary, Alberta. Therefore, NAES is a direct competitor to General Electric, the manufacturer of the Mint Farm Energy Center combustion turbine and the operations and maintenance contractor for Wayzata.

Furthermore, the owners of the Mint Farm Energy Center and General Electric had concerns about the confidentiality of the potential transaction and would not allow NAES to speak directly with General Electric personnel prior to the execution of definitive agreements. The inability of NAES to interview General Electric personnel is insignificant because NAES was able to interview the then-president and the asset manager of the Mint Farm Energy Center. Both of these individuals had intimate knowledge of plant operations and were able to share this knowledge with both NAES and PSE. In fact, NAES notes findings resulting from these interviews at several points in its due diligence report. *See generally* Exhibit No. RG-54.

Q. Did PSE have access to design, construction and operational data for the Mint Farm Energy Center?

A. Yes. PSE had access to design, construction and operational data for the Mint Farm Energy Center. In conjunction with the NAES due diligence report, PSE conducted a comprehensive review of all technical data. PSE was able to review all design and construction materials and plans via shared documents placed on a secured site and during numerous visits to the Mint Farm Energy Center. During PSE's due diligence period, PSE staff made numerous trips to the Mint Farm Energy Center to review all design and construction materials and talk with plant management. Because there was no operational data due to the youth of the plant, PSE insisted that the owners of Mint Farm Energy Center conduct performance testing prior to PSE's acquisition. The owners conducted this performance testing after NAES had completed its due diligence report. Finally, PSE independently reviewed the operations and maintenance agreements with General Electric.

Q. Did PSE share Public Counsel's concern that several important systems had not yet been fully commissioned?

A. No. As of the date of the NAES visit, the evaporative coolers, steam augmentation, and duct burners were not fully commissioned. The Board of Directors presentation acknowledged that PSE was awaiting the results of an ASME PTC 46 standardized plant performance evaluation conducted on July 9, 2008, only two days prior to July 11, 2008, the date of the NAES due diligence report:

> As of July 16, 2008 PSE continues to await the results of an ASME PTC 46 standardized plant performance evaluation conducted on July 9, 2008. Subsequently all stated plant performance data in this report is based on information provided by Wayzata/GE.

Exhibit No. RG-7HC at page 179. The evaporative coolers, steam augmentation, and duct burners, however, were fully commissioned before PSE completed its planned post-acquisition upgrade.

Q. Does PSE share Public Counsel's concern that NAES could not substantiate that the Mint Farm Energy Center was compliant with noise ordinances?

A. No. The Board of Directors presentation acknowledged that noise issues had been raised with respect to the Mint Farm Energy Center, measures had been taken to address such concerns and no further issues had been reported:

> Upon plant start-up, there were noise complaints by one property owner across the valley. Significant noise reduction measures were taken on the Facility and no further issues have been reported.

Exhibit No. RG-7HC at page 194. Furthermore, there is no specific statement of noise ordinance compliance from Cowlitz County. The county explores concerns over noise ordinance violations only when there is a noise complaint. Because all existing noise complaints had been dismissed, PSE's own due diligence revealed that noise was not a material concern.

Q. Does PSE share Public Counsel's concern that NAES found corrosion in the HRSG?

A. Yes. The corrosion to the HRSG was a significant concern to PSE. Indeed, the NAES due diligence report indicated that corrosion to the HRSG "was the most significant problem found with a potential for future problems." Exhibit No. RG-54 at page 21. PSE highlighted this issue in its presentation to the Board of Directors:

> During the initial start-up period, HRSG tube leakage was discovered. A borescope inspection was conducted, in which low, medium and high levels of corrosion were found on the LP, IP and HP economizer tubes. It is believed by Wayzata and the HRSG inspectors [NAES] that this unusual level of corrosion on a young unit was due to OEM residual test water that remained in the tubing during shipment and storage. The HRSG was not assembled until project resumption in 2006 and as such remained in storage for a significant period of time. Repairs resulted in the replacement of one tube and the capping off of another tube. An acid flush was conducted to remove corrosion and to place it into a chemically controlled condition to slow any further deterioration. Finally, the HRSG was successfully hydrostatically tested. The HRSG has achieved over 2,000 hours of operational time with no unplanned maintenance. In its current condition, the HRSG is stable, yet further inspections will be required to determine the extent of advanced aging and required repairs.

Exhibit No. RG-7HC at page 174. Furthermore, the financial pro-forma supporting the acquisition of the Mint Farm Energy Center in the presentation to the Board of Directors includes both a $110,500 line item for reinspection of the HSRG and a $1,500,000 line item for potential repair. *See* Exhibit RG-7HC at page 80. PSE completed these repairs and now no longer considers this a concern.

Public Counsel's suggestion that PSE failed to account for HRSG corrosion issues illustrates how Public Counsel extracts information and initial findings out of context and elevates that information to misleading and unnecessary concerns. PSE took reasonable steps to notify the Board of Directors of past and potential future mitigation efforts to alleviate the corrosion issues, and included adequate costs in the financial pro-forma to undertake this remediation. Public Counsel's disregard for PSE's proactive management of the HRSG corrosion does not constitute evidence that PSE was not prudent in its acquisition of the Mint Farm Energy Center.

Q. Does PSE share Public Counsel's concern that the condenser experienced corrosion behind the coatings on the internal hotwell/condenser walls?

A. No. The corrosion behind the coatings on the internal hotwell/condenser walls was a minor issue that PSE easily resolved. The presentation to the Board of Directors noted this corrosion:

> The condenser has also experienced corrosion behind the coatings on the internal hotwell/condenser walls. This is not uncommon and can be mitigated by an inspection program and periodic recoating during outages.

Exhibit No. RG-7HC at 176. PSE reviewed the condition of the condenser and deduced that a simple cleaning of the condenser's tubes, tubesheets, and flushing of the strainers would provide a quick, inexpensive fix to the condenser corrosion. Accordingly, PSE considered the repair to be minor in nature and included it into planned post-acquisition upgrades for the Mint Farm Energy Center.

Q. Does PSE share Public Counsel's concern that the Atlas Copco Gas compressors had failed three times since resumption of the suspension?

A. No. Public Counsel cites the following section of the NAES due diligence report, which states that the Atlas Copco Gas compressors failed three times since resumption of the suspension:

> The Atlas Copco gas compressors have experienced three (3) failures since resumption of the suspension. Initial failures were related to the suspension period layup. Foreign Object Damage (FOD) was indicated to as the cause of the third failure. NAES was not provided any reports on the damage and was not provided with root cause analysis on the failures.

Exhibit No. RG-54 at page 4.

Public Counsel, however, fails to acknowledge the next two sentences of the NAES due diligence report, in which NAES states that the Atlas Copco gas compressors were rebuilt and that future failures were unlikely:

> Both units were rebuilt by the OEM. There is no reason to believe these failures will repeat themselves but the compressors should be watched closely for a while.

Exhibit No. RG-54 at page 4. Unlike Public Counsel, PSE's presentation to the Board of Directors noted the failures of the gas compressors and pointed out that the gas compressors had been rebuilt:

> Since operation, the compressors have failed on three occasions; once on the first machine, and twice on the second. The third failure was believed to be caused by improper lay-up during construction intermission. The units have been rebuilt and have experienced no further failures after approximately 2,000 hours of operation.

Exhibit No. RG-7HC at page 169.

Q. Does PSE share Public Counsel's concern that there are no warranties on the plant equipment due to the suspension of construction and subsequent release agreements?

A. Although PSE would have preferred the plant equipment to be under warranty, PSE understands that it is rare for plant warranties to cover performance risks for plant equipment that is several years old. Indeed, it would have been rare for the plant equipment of any of the natural gas plants proposed in response to the 2008 RFP to have been under warranty. PSE informed the Board of Directors that most of the plant equipment was not under warranty:

> Due to time lag between component purchases and final plant assembly, all components, with the exception of the catalyst plates, are not covered under warranty.

Exhibit No. RG-7HC at page 179.

Q. Please summarize PSE's position with respect to Public Counsel's concerns about PSE's qualitative analyses.

A. Five of Public Counsel's seven "concerns" about the qualitative analysis are baseless because they focus on minor findings of a single due diligence report without regard to the fact that PSE could and did easily resolve these "concerns". Contrary to the assertions of Public Counsel, the presentation to the Board of Directors specifically identified all but one of NAES's seven "concerns." Of the seven “concerns” identified, the corrosion to the economizer sections of the HRSG and the corrosion behind the coatings on the internal hotwell/condenser walls were the only two issues of substance. PSE developed proactive plans to repair those issues in the post-acquisition updates to the Mint Farm Energy Center, included costs for the repairs and factored those costs into its economic analyses.

G. <u>PSE Has Adequate Resources to Operate the Mint Farm Energy Center</u>

1. <u>PSE’s Strategy to Pursue Long-Term Firm Gas Transportation to the Mint Farm Energy Center</u>

Q. Do you agree with Public Counsel’s assessment that the lack of firm gas transportation was another risk associated with the acquisition of Mint Farm?

A. No. The presentation to the Board of Directors and my prefiled testimony in this proceeding discussed in detail the various strategic options available to PSE to acquire firm gas transportation. PSE developed a strategy based on its knowledge of the supply and demand for transportation in the region. Please see the Prefiled Rebuttal Testimony of Mr. R. Clay Riding, Exhibit No. RCR-5T, for additional detail regarding PSE’s gas transportation strategy and implementation.

Q. Why did PSE wait to acquire firm gas transportation?

A. To operate the Mint Farm Energy Center, PSE needs gas transportation capacity on both the Northwest Pipeline and Cascade Natural Gas systems. PSE manages its gas transportation need as a portfolio, and PSE is exploring alternatives to meet the electric portfolio needs as a whole rather than the needs of a single plant. The Prefiled Rebuttal Testimony of Mr. R. Clay Riding, Exhibit No. RCR-5T, describes the strategy with respect to gas transportation to meet the needs of the electric portfolio.

2. PSE Has Adequate Firm Transmission Resources for the Mint Farm Energy Center

Q. Does PSE have firm transmission for the Mint Farm Energy Center when the facility is generating at full capacity?

A. No. PSE has 293 MW of firm point-to-point transmission from BPA to PSE's service territory. The Mint Farm Energy Center baseload generating capacity at ISO conditions is 296 MW. PSE therefore does not have 3 MW of firm transmission to cover all of the baseload generation gross of station service.

Q. Is the firm transmission deficit of 3 MW a risk to owning the Mint Farm Energy Center?

A. No. The firm transmission deficit of 3 MW is not a risk to owning the Mint Farm Energy Center, and PSE has identified a couple of methods to manage this minor issue.

To meet short-term needs, PSE uses existing committed firm transmission rights to redirect transmission to the Mint Farm Energy Center. PSE can also purchase short-term firm transmission to cover instances when the project is capable of producing in excess of 293 MW and the facility is economic to dispatch.

For long-term management of the Mint Farm Energy Center, PSE submitted a transmission request to BPA under BPA's 2009 Network Open Season to acquire an additional 12 MW of firm transmission for generation from the Mint Farm Energy Center. This additional amount would bring total firm transmission for the facility to 305 MW. PSE's analysis of the operational data suggested 305 MW is the appropriate amount needed to transport power from Mint Farm to PSE's service territory during particular weather events when Mint Farm is capable of generating more than its capacity amount at ISO conditions. This transmission will most likely not be available until BPA is able to complete the I-5 Corridor upgrade, which BPA anticipates will be complete by 2015.

3. <u>PSE Does Not Need Back-Up Fuel for the Mint Farm Energy Center</u>

Q. Is the lack of back-up fuel for the Mint Farm Energy Center a concern to PSE?

A. No. The lack of back-up fuel for the Mint Farm Energy Center is not a concern. Public Counsel asserts that "PSE is aware that Mint farm had no backup fuel capability and therefore the output of the plant could be restricted if the natural gas supply to the plant is ever curtailed . . . ." Exhibit No. SN-1HCT at page 16, lines 7-9. Public Counsel, however, fails to acknowledge that it would be nearly impossible to permit a baseload combined cycle combustion turbine in Washington for both natural gas and oil due to the high-polluting emissions of oil. Furthermore, Public Counsel is, in effect, questioning the firmness of firm gas transportation. Although it is possible that the fuel supply could be curtailed, it is not likely. Moreover, potential curtailment is but one of the many challenges associated with resource acquisition and management. These risks will always exist, and it is PSE's responsibility to manage those risks.

III. UPDATED MINT FARM ENERGY CENTER ACQUISITION COSTS

Q. How do the actual acquisition costs of the Mint Farm Energy Center compare with the projected acquisition costs?

A. The actual acquisition costs of the Mint Farm Energy Center are nearly $8 million lower than the projected acquisition costs in the presentation to the Board of Directors and $3 million less than the projected acquisition costs provided in the initial filing in this proceeding. The total acquisition cost of the Mint Farm Energy Center is just under $250 million.

Q. Has PSE completed all planned post-acquisition upgrades to the Mint Farm Energy Center?

A. As of October 2009, PSE still has some remaining post-acquisition upgrades to the Mint Farm Energy Center and estimates that these upgrades will cost $2.7 million to complete. The total cost of the upgrades to bring the Mint Farm

Energy Center within PSE's operating standards is $7.2 million, over $3 million less than estimated for the May 2009 GRC filing. For further information on the progress of the post-acquisition upgrades to the Mint Farm Energy Center, please see the Prefiled Rebuttal Testimony of Mr. L. Ed Odom, Exhibit No. LRO-13CT.

Q. Does the total acquisition cost of the Mint Farm Energy Center of just under $250 million include the $2.7 million in some remaining post-acquisition upgrades?

A. Yes. The total acquisition cost of the Mint Farm Energy Center of just under $250 million includes the $2.7 million in some remaining post-acquisition upgrades.

IV. PSE COMPLETED THE WILD HORSE WIND EXPANSION PROJECT ON TIME AND UNDER BUDGET

Q. Is the Wild Horse Wind Expansion Project commercially operating?

A. Yes. The 44 MW Wild Horse Wind Expansion Project entered commercial operations on November 9, 2009.

Q. Did PSE complete the Wild Horse Wind Expansion Project on time and within the budget approved by PSE's Board of Directors?

A. Yes. PSE completed the Wild Horse Wind Expansion Project on time and within the budget approved by PSE's Board of Directors. PSE completed the Wild Horse Wind Expansion Project three weeks prior to the projected online date of

December 1, 2009. The budget approved by PSE's Board of Directors for the Wild Horse Wind Expansion Project was $107.5 million. The final cost of the Wild Horse Wind Expansion Project is $98.4 million, or $2,240/kW and a levelized cost of $[redacted]/MWh.

Q. What cost savings did PSE realize with respect to the completion of the Wild Horse Wind Expansion Project?

A. PSE saved an additional $4 million by controlling costs and timelines during construction. The Wind Turbine Supply Agreement with Vestas America came in under budget because [redacted] were lower than projected. PSE did not use about $700,000 of budgeted contingency and budgeted AFUDC came in under budget by bringing the plant online ahead of schedule.

Q. Other than reduction in capital costs, what else has changed in the proforma?

A. PSE has updated the proforma to reflect (i) the earlier commercial operation on-line date, (ii) updated property tax rates, and (iii) the wind integration rate provided in PSE's supplemental filing dated September 28, 2009. Additionally, at the time PSE made the recommendation to the Board of Directors on November 4, 2008, PSE projected it would have a tax appetite to capture the production tax credits generated by the Wild Horse Wind Expansion Project. With the various tax incentives passed in the American Recovery and Reinvestment Act, however, PSE's tax appetite has changed, and PSE now projects that it will not have a tax appetite to realize production tax credits in the year they are generated. Should PSE use these tax benefits, PSE projects carrying costs for the deferred tax account for the production tax credits to add a net present value of $4 million to the lifetime cost of the project. These projected cost increases offset the cost savings realized during the construction of the project. The levelized cost, assuming production tax credits, would change slightly to $[redacted]/MWh. If PSE had the appropriate tax appetite, the construction cost savings and reductions in operation and maintenance expenses would reduce the levelized cost to $[redacted]/MWh.

V. COST TO ACQUIRE FREDONIA UNITS 3 & 4 IS KNOWN AND MEASURABLE

Q. Did PSE prudently acquire Fredonia Units 3 & 4?

A. Yes. PSE prudently acquire Fredonia Units 3 & 4. Please see the Prefiled Direct Testimony of Mr. W. James Elsea, Exhibit No. WJE-1HCT, and the supporting exhibits thereto, and my prefiled direct testimony, Exhibit No. RG-1HCT, and supporting exhibits thereto, for a discussion of the process by which PSE acquired Fredonia Units 3 & 4. Commission Staff reviewed the acquisition and determined that PSE prudently acquired Fredonia Units 3 & 4:

> PSE satisfied all prudence factors and the decision to acquire the Fredonia generation units was made appropriately by PSE management. Therefore, I conclude that the Fredonia peaking units purchase was a reasonable and prudent choice for acquisition by PSE when that decision was made.

Exhibit No. DN-1HCT at page 32, lines 5-8.

Q. Does PSE know when it will acquire Fredonia Units 3 & 4?

A. Yes. At the time it filed it direct testimony on May 5, 2009, PSE estimated that PSE would acquire Fredonia Units 3 & 4 sometime in January 2010. PSE now knows that it will acquire Fredonia Units 3 & 4 on January 13, 2010.

Q. Are the acquisition costs known and measurable?

A. Yes. The cost to acquire Fredonia Units 3 & 4 is based on the unamortized lease balance as of December 31, 2009. The unamortized lease balance as of December 31, 2009, will be $42,347,993. *See* Exhibit No. RG-56 at page 6. This cost is known and measurable.

Q. Please describe the recommendation of Commission Staff regarding the cost to acquire Fredonia Units 3 & 4.

A. Commission Staff recommends that because PSE has not yet acquired Fredonia Units 3 & 4, the acquisition costs are not known and measurable. In other words, the acquisition costs are projections of what ultimate acquisition costs will be. As Commission Staff suggests that only "known and measurable" costs for both capital and operations and maintenance costs be included into rate base, Commission Staff removes the cost of the acquisition from rate base and reinserts the ongoing cost of the lease. *See* Exhibit No. KHB-1CT at page 36, lines 13-21.

Q. Does PSE agree with Commission Staff's recommendation?

A. No. PSE objects to Commission Staff's recommendation. First, it is known and measurable that PSE will acquire Fredonia Units 3 & 4 on January 13, 2010, just weeks after the filing of this prefiled rebuttal testimony and prior to the commencement of the rate year. Second, the costs to acquire Fredonia Units 3 & 4 are known and measurable and will be $42,347,993. Third, Commission Staff reviewed PSE's analysis and decision to acquire Fredonia Units 3 & 4 and concluded that such acquisition was prudent. Based on these three facts, it is unclear how Commission Staff could reach the conclusion that the acquisition of Fredonia Units 3 & 4 is not known and measurable.

VI. CONCLUSION

Q. Please summarize your conclusions.

A. PSE had an identified need for energy and capacity in 2011. PSE's IRP process informed PSE's resource acquisition strategy. PSE issued the 2008 RFP to meet its resource needs. PSE evaluated the resource alternatives using current information that adjusted for appropriate factors and risks. PSE informed and involved its Board of Directors during the resource acquisition process. PSE kept contemporaneous records of its evaluation and decision processes. In short, PSE's acquisition of the Mint Farm Energy Center was prudent.

Public Counsel presents arguments opposing the PSE's acquisition by mischaracterizing PSE's due diligence findings, taking portions of the record out of context, and selectively elevating the important of particular criteria without considering the findings as a whole. In doing so, Public Counsel attempts to mislead the Commission about the acquisition of the Mint Farm Energy Center and PSE's motives for selecting the resource. The Commission should not be swayed by such tactics and should instead conclude that PSE's acquisition of the Mint Farm Energy Center was prudent.

Q. Does that conclude your prefiled rebuttal testimony?

A. Yes.