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BEFORE THE WASHINGTON UTILITIES AND
TRANSPORTATION COMMISSION

AIR LIQUIDE AMERICA CORPORATION, AIR PRODUCTS AND CHEMICALS, INC., THE BOEING COMPANY, CNC CONTAINERS, EQUILON ENTERPRISES, LLC, GEORGIA-PACIFIC WEST, INC., AND TESORO NORTHWEST CO.,

Complainants,

vs.

PUGET SOUND ENERGY,

Respondent.

Docket No. UE-001952
VOLUME VII
Pages 1439 to 1747

In the Matter of

Petition of Puget Sound Energy, Inc., for an Order Reallocating Lost Revenues Related to any Reduction in the Schedule 48 or G-P Special Contract Rates,

Docket No. UE-001959
VOLUME VII
Pages 1439 to 1747

PORTIONS DESIGNATED CONFIDENTIAL

A Hearing in the above matter was held on January 15, 2001, at 9:30 a.m., at 1300 South Evergreen Park Drive Southwest, Olympia, Washington, before Administrative Law Judge DENNIS MOSS and Chairwoman MARILYN SHOWALTER and Commissioner RICHARD HEMSTAD.

Joan E. Kinn, CCR, RPR
Court Reporter

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The parties were present as follows:

THE COMMISSION, by DONALD T. TROTTER and ROBERT D. CEDARBAUM, Assistant Attorneys General, 1400 South Evergreen Park Drive Southwest, Olympia, Washington 98504-0128.

PUGET SOUND ENERGY, INC., by STAN BERMAN and TODD GLASS, Attorneys at Law, Heller Ehrman White & McAuliffe, LLP, 701 Fifth Avenue, Suite 6100, Seattle, Washington 98104.

AIR LIQUIDE AMERICA CORPORATION, AIR PRODUCTS AND CHEMICALS, INC., THE BOEING COMPANY, CNC CONTAINERS, EQUILON ENTERPRISES, LLC, GEORGIA-PACIFIC WEST, INC., and TESORO NORTHWEST COMPANY, by BRADLEY VAN CLEVE, Attorney at Law, Davison Van Cleve, P.C., 1300 Southwest Fifth Avenue, Suite 2915, Portland, Oregon 97201.

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P R O C E E D I N G S

JUDGE MOSS: Good morning, everyone. We are reconvened in our proceedings in Docket Number UE-001952, styled Air Liquide, et al. against PSE. And I believe this morning we are ready for the Company's case in chief; is that correct?

MR. BERMAN: Yes, Your Honor. Before we present our first witness, I just wanted to note we gave several responses to Bench requests on Friday. I never had an opportunity to explain them, and I thought I might spend just a moment to explain what it was that we had provided on Friday.

JUDGE MOSS: I think that would be helpful.

MR. BERMAN: We have already looked at the response that was provided to Bench Records Requisition Number 8, and I believe that that was marked as Exhibit 25. That was the graph of Mid-C prices, of Mid-C forward prices, and I'm not sure that that needs much more explanation. As has been pointed out, the original Bench request asked for the one year forward prices for the past ten weekdays in addition to providing information for the past ten weekdays.

In our response to Number 8, we provided weekly data going back through August so that you could get a representative sense of how the flat product for

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the year 2001 has varied over time. So that if someone wanted to buy the product for all of 2001 and had tried to buy it in October, you can get a sense of that from the data that we provided.

JUDGE MOSS: And that's what you mean when you say flat?

MR. BERMAN: Well, flat is a little bit complicated. In general, the numbers that we gather, there are people who buy a peak product which gives them energy during the peak hours of the day, or you can buy an off-peak product. A flat product would generally give you one megawatt through all 24 hours of the day.

JUDGE MOSS: Okay.

MR. BERMAN: So the prices that are quoted there would be the prices if you bought one megawatt for all 24 hours of the day. So the graph that we show shows that if you bought one megawatt for all 365 days of the year 2001, 24 hours a day, and that would be the price.

If you want to break it down by months, when you look at the tabular data on the third page of Exhibit 25, you will see that monthly predictions vary. And the data that's in that tabular exhibit only shows the flat product. So if we were to show more data, you could, for instance, see that there might be variations

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in the way the on-peak product varies over time, in the way the off-peak product varies over time, et cetera.

JUDGE MOSS: Do you have a sense, Mr. Berman, of how the flat price relates to those other prices you have mentioned, the on-peak and the off-peak price? Does the flat price tend to strike somewhere in between, or are the on-peak and off-peak, say daily prices, generally higher?

MR. BERMAN: Well, it's almost always the case that the on-peak price is higher than the off-peak price. That is probably always the case except in a very -- on a forward basis. On a single day basis, there might be an odd situation in a given off-peak hour, but on a forward basis, people always predict a higher price in the on-peak than the off-peak. So there's always a higher price.

The flat product is simply buying for all 24 hours in a day. So it would effectively be an hourly weighted averaging of the on-peak for the on-peak hours of the day and the off-peak product for the off-peak hours of day.

JUDGE MOSS: Then there's a number of things we might want to look at and draw on in making inferences about the market situation and conditions, and, of course, the Schedule 48 and the Special Contract

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pricing is an hourly price, isn't it?

MR. BERMAN: In Schedule 48 and the Special Contracts, it provides that an hourly price will be used. As we have discussed, in general there's not a separate price quoted for each individual hour. Instead, the indexes provide a price for the on-peak hours of the day and then a separate price for the off-peak hours of the day. So typically there's one number that applies to all on-peak hours and then to all off-peak hours.

JUDGE MOSS: And that is the basis for the charges that ultimately end up in the customers' bills?

MR. BERMAN: That's right. The one distinction between the contracts being that the Schedule 48 contracts provide for the Mid-Columbia Non-firm Index price, and the Special Contracts provide for the Mid-Columbia Firm Index price.

JUDGE MOSS: That's 1.07, as I recall, firm price less 1.07? Mr. Gaines is nodding in the affirmative back there, so I think I got it right.

MR. BERMAN: If Mr. Gaines is nodding, I will agree with you.

JUDGE MOSS: He's not under oath, but we will take his nod nevertheless.

All right, that clears up my questions,

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thanks.

MR. BERMAN: Okay, so that was the response to Bench Request Number 8. We also provided a response to Bench Records Requisition Number 9. I'm afraid I don't recall what exhibit number you assigned to that.

JUDGE MOSS: 26.

MR. BERMAN: In Number 26, we were asked to provide, basically to update the analysis that showed what are the running totals of cumulative gains and losses for each customer, but to do it on a present value basis, that is to reflect the time value of money in the calculation.

We recognize that there are those who might disagree about what the appropriate present value adjuster might be, and so we did three different calculations using a 6%, 7% and 10% figure, and so you can get a -- there's a range of different available options there depending on which you think is the best number. And we present for each customer at each location the cumulative totals relying on the 6%, 7%, and 10%.

And as might be expected, the cumulative totals are different using the present value adjustment than you would find if you were to just use the raw numbers.

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JUDGE MOSS: And I noticed in that exhibit as I was reviewing it that there's a reference to compounding. Can you explain to me a little bit the basis for the compounding; how was that done?

MR. BERMAN: Your Honor, it was compounded monthly using the specified interest rate, so the theory would be that basically if, for instance, the customer in April of '97 had saved $10,000, you would assume that they could have taken that $10,000 and stuck it into an interest bearing account compounded monthly at either 6%, 7%, or 10% interest rate, and that $10,000 would be carried forward to get the present value of receiving $10,000 that period of time ago. And so each entry in the table for each month that the payments are made would be compounded monthly in that fashion.

JUDGE MOSS: And that same principle is applied when the customer pays more than it would have under the other rate schedule as well?

MR. BERMAN: That's right. If the customer paid more in any past period, then that would be reflected as well, except you would have a number that goes in the other direction.

JUDGE MOSS: Sure, I just wanted to be sure I understood the exhibit. And, of course, I will mention in connection with this one, and it's true with all of

them, if other parties wish to run their own analyses in response to the records requisitions, they may do so, and so that's something that is available to you if you feel that maybe there are some accounting conventions that might be considered differently.

MR. BERMAN: We also provided a response to Bench Records Requisition Number 7. I'm assuming that that's Exhibit 24.

JUDGE MOSS: You assume correctly.

MR. BERMAN: This related to the discussion that occurred on the record relating to the Southern California Edison case in which I had asserted that Southern California Edison had prevailed in its filed rate argument in the federal court in Los Angeles. I think it's worth noting that one could read this transcript differently in that the end result of the hearing that is reported in this transcript is that Southern California Edison's motion for summary judgment in that case was denied.

But if you read carefully, you will see that the federal judge found that the filed rate argument did apply to the wholesale prices that were paid in California, but he noted the applicability of the so-called Pike County Exception, which provides that though the state regulator is required to pass on

wholesale procurement cost, that the state regulator does not give up its right to assess whether those wholesale procurement costs were prudently incurred.

And the CPUC in that case had raised a question as to whether the costs incurred by Southern California Edison were prudently incurred. The federal judge found that there was a fact question concerning prudence and held over the case to assess the limited issue of whether or not there was any imprudence by Southern California Edison.

So I stand by the proposition that this says that the state regulator must pass on costs that were wholesale procurement costs that were incurred by the utility. It must allow the utility to pass on those costs to retail customers even if those costs were incurred in the wholesale markets of today. But there is an issue of whether the costs were prudently incurred.

JUDGE MOSS: And I appreciate your candor in bringing that to the Bench's attention. I did review the transcript and found it to be consistent with the remarks you have made to some extent at least. And I will just note that the Natahala Power decision on which the state and the complainant in that case relied in the argument to the judge is, of course, the font, if you

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will, of that principle, and the Pike exception is noted, and the judge did leave that question open by denying the motion for summary judgment by the plaintiffs in that proceeding.

MR. BERMAN: And the final Bench request response we had provided on Friday was the response to Bench Records Requisition Number 1. I'm not certain what -- I guess that was Exhibit 27.

JUDGE MOSS: Well, yes, let me make the record clear on this point, because the way things came in, it led to a dispersal, if you will, of the responses. The responses to Records Requisition Number 1 are reflected in part in Exhibit numbers 106, 203, and 302 in connection with individual witnesses' testimony. But then there was a supplemental response which is marked as Exhibit 27, and that includes -- I don't actually recall whether it's all of the service agreements or just the balance of them that were not reflected in the other three exhibits that I mentioned. So just so the parties understand, all the material is in there, all the service agreements are in the record, but they may bear different exhibit numbers.

MR. BERMAN: It was our intention to provide in that response the balance of the service agreements, so various of the Complainants have put on witnesses,

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and we have either ourselves or by tendering them to Staff made sure that each of the service agreements were entered into the record, but several of the Complainants had no witness, and so this covers each of the Complainants who had no witness.

JUDGE MOSS: All right.

MR. BERMAN: I would note that though we have a service agreement for each of the customers, as you will see when we get into Mr. Gaines's deposition, there have occasionally over time been letter agreements of one sort or another that related to particular detailed aspects of the service that's provided. And in gathering together the service agreements, I believe we did not necessarily capture every one of those more detailed letter agreements. Mr. Gaines will have as one of his exhibits one of the detailed letter agreements relating to Air Liquide. There may be some other letter agreements out there, and we did not try to hunt them all down.

JUDGE MOSS: Okay. Does that conclude what you had to present?

MR. BERMAN: Yes, it does, Your Honor.

JUDGE MOSS: Okay. Does anybody else have anything preliminarily before we have Mr. Gaines take the stand?

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MR. CEDARBAUM: Yes, Your Honor. This morning I distributed to the Bench and the parties the Staff response to Bench Request D-1. This was prepared on Friday, so for anyone who can't read my writing, it says in my writing staff response in the upper left-hand corner. The cover sheet is the Bench request itself. If you want me to replace that with something more artful, I can do that.

JUDGE MOSS: That's quite all right. That's been marked as Exhibit 28.

MR. CEDARBAUM: And I would just note for the record the responsive pages were printed off of the NYMEX web site this past Friday. That was the source of the documentation that was provided in the underlying response.

JUDGE MOSS: All right, give me half a second.

All right, go ahead, Mr. Cedarbaum, anything else?

MR. CEDARBAUM: No, that's it.

MR. BERMAN: Your Honor, with respect to Bench Request D-1, as I explained on Friday, Mr. Gaines's job is to engage in power procurement and will be describing at some length how Puget Sound Energy does that. And in the midst of his explanation, we

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expect he will answer Bench Request D-1 on the stand. If you have further questions about D-1 that you feel that Mr. Gaines hasn't gotten into, he is very knowledgeable about this information and will do his best to give you further information on that.

CHAIRWOMAN SHOWALTER: I'm sorry, which exhibit is D-1?

MR. BERMAN: D-1 was a Bench request and the Bench request that asked about how --

CHAIRWOMAN SHOWALTER: Oh, 28.

MR. BERMAN: -- that asked about NYMEX markets and so forth. We did not provide a written response to that, so there is no exhibit for our response. I was just saying that Mr. Gaines will address that in his oral testimony.

CHAIRWOMAN SHOWALTER: I'm just trying to key into what document you're talking about, and I understand you're talking about Exhibit 28.

MR. BERMAN: I think 28 is the Staff response to D-1, yes.

JUDGE MOSS: I guess I should clear up. The E-mail that's part of the Bench request response to D-1, the one we're talking about, it's got the name Warman, Alan P, at the top. Was that part of the Staff's

response?
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MR. CEDARBAUM: No, I believe that came from Complainants.
MR. VAN CLEVE: That's Complainants'.
JUDGE MOSS: Okay, so we have Complainants' response, Staff's response, and we will hear from Mr. Gaines on this subject on the stand, so we will have a very thorough response to Bench Request D-1.
Anything else before we call Mr. Gaines?
All right, Mr. Gaines, it appears that you are the man of the moment.

Whereupon,
WILLIAM A. GAINES,
having been first duly sworn, was called as a witness herein and was examined and testified as follows:

JUDGE MOSS: Just a moment, Mr. Berman.
(Discussion on the Bench.)
JUDGE MOSS: Let's take up one more preliminary matter, and I actually did communicate this to the parties by E-mail yesterday, but you may not have seen that, and I think I have asked this before, but frankly my notes are inadequate to the task. I have been handed at some point or another exhibits, this will be for Complainants I think, DWS-23 and 24, and I think
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I asked you about this on Friday night but I forgot, what are those again, are those going to be supplemental exhibits or keys to some other exhibit?
MR. VAN CLEVE: Your Honor, I believe that those will be cross exhibits for Mr. Gaines.
JUDGE MOSS: Okay, well, that will come in then in due course.
All right, your witness, Mr. Berman.

D I R E C T   E X A M I N A T I O N
BY MR. BERMAN:
Q. Mr. Gaines, could you state your full name and business address for the record.
A. Yes, my name is William A. Gaines. The business address is 411 - 108th Northeast, Bellevue, Washington.
Q. And who is your employer?
A. Puget Sound Energy.
Q. And what position do you hold at Puget Sound Energy?
A. I serve as the Company's vice president for energy supply.
Q. And what are your responsibilities and duties in that position?
A. My responsibilities include the planning,
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acquisition, and management of all of the Company's bulk power and gas supply as well as the electric transmission and gas transportation arrangements to move

that power and gas from the markets to the load center.
Q. How long have you held that position?
A. Since February of 1997.
Q. What other positions have you held at the Company?
A. I have held a variety of positions in the power management area in the Company for about the last 22 years.
Q. What is your educational background?
A. My educational background includes a Bachelor's of Science Degree in Electrical Engineering with specialization in power systems and a Master of Business Administration Degree with specialization in corporate finance.
Q. Why don't we get right into it then. Could you please, are you familiar with the merger rate plan that applies to Puget Sound Energy?
A. Yes, I am.
Q. Could you please explain to me your understanding of the merger rate plan and how it applies to Puget Sound Energy resource management?
A. Yes, at a top level, the merger rate plan
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provided that for a five year period the Company would charge a stipulated set of retail rates and that during that period it would be free to manage its supply resources and with the objective of reducing the costs of those resources so that the revenues derived from the retail rates would be sufficient to cover the Company's costs.
Q. And could you please explain to me the Schedule 48 and Special Contracts and how they relate to resource management for Puget Sound Energy?
A. Yes. Under Schedule 48 and the Special Contracts, the industrial customers insisted on purchasing power at essentially the wholesale market rate. And so -- and also there was an understanding at the time that those schedules and contracts were put into effect that the Company would no longer have on obligation to plan and acquire resources for those loads. And so in the Company's power planning and management activities, it no longer does that, but rather uses either its own resources or purchases from the markets to serve those index price loads.
Q. Is it correct that the merger rate plan governs rates for customer classes other than those served under Schedule 48 and the Special Contracts?
A. Yes, it does, it governs rates for all
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customer classes.
Q. Would the merger rate plan, would the merger rate plan have made sense if not for Schedule 48 and the Special Contracts?
A. Well, Schedule 48 and the Special Contracts were an essential part of the understanding reached in the merger rate plan. And in reliance on that plan, the Company has undertaken certain activities with respect

to its resource acquisitions and management that it would have done differently absent that plan.

Q. Could you describe for me some of the things that Puget Sound Energy has done in reliance on Schedule 48 and the Special Contracts?

A. Yes. Probably one of the most notable things that it has done is it has allowed its resource package through attrition to be at a level that is closer to the core or embedded price load level rather than the total load level including Schedule 48 and the Special Contracts. Had we not had Schedule 48 and the Special Contracts in place, we probably would have acquired additional fixed price supply to serve those loads.

In addition, in the nearer term, the company has been engaging in a series of risk management or hedging activities around its existing resource portfolio, taking into account the need to serve some

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fixed price loads and some floating price loads, and has tried to arrange its portfolio in a way that it has the appropriate sets of resources to receive each of those classes of loads.

Q. How would it impact Puget Sound Energy if the deal in Schedule 48 and the Special Contracts were to be disrupted mid-stream, and if you could focus on the resource planning aspects of that question?

A. Well, the specific actions that the Company would need to take would be dependent upon how the Special Contracts and Schedule 48 were restructured. But generally, as I indicated earlier, the Company has allowed some attrition to occur in its load resource balance in reliance on Schedule 48 and the Special Contracts, because probably the safest thing to do from a financial risk point of view is for the Company just to buy in the wholesale spot market the power that's necessary to serve these loads.

Q. Now when you say attrition, could you just so the record is clear explain what attrition means?

A. Yes. The Company continues to experience growth in its retail loads, and it has not in the last five years added additional resources to cover that growth. There have also been some reductions in the amounts of power to which the Company is entitled under

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certain of its long-term power purchase contracts.

Q. Is it possible to undo the attrition that has been allowed to occur over the past several years?

A. It's really not possible to undo it, no.

Q. So in order to make up for that if you have a new obligation to serve customers, what would you have to do?

A. The Company would need to go in to the marketplace and either purchase power at present prices or construct resources at present costs.

Q. Could you please explain to me your understanding of the respective risks born by various classes of customers and Puget Sound Energy in the deals that we have discussed?

A. Yes. In connection with the Schedule 48 tariff and the other Special Contracts which have indexed based pricing, the customers through the development of those tariffs and contracts agreed to bear the risks and benefits of the market costs, and the Company is no longer required to acquire long-term fixed price supply for those customers.

Q. Would you agree that in contrast to the Schedule 48 and Special Contract customers, that Puget Sound Energy has agreed to bear some measure of risk when it comes to serving other customer classes through

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the merger rate plan?

A. Yes, that's right, the other customer classes purchase their power at a price that is at least reflective of the company's embedded cost of service. And to the extent that the company's actual costs vary from the costs that are assumed in those rates, that risk falls on the Company.

Q. If the company's obligations under Schedule 48 and the Special Contracts were altered, would that vary the risk that the Company bears under the merger rate plan?

A. Absolutely.

Q. Could you explain?

A. Well, again, it would depend on the manner in which the Schedule 48 and Special Contract arrangements were altered. But if, for example, they were altered in a way that required the Company to serve those customers at fixed rates, it would put tremendous risk on the Company, because it no longer has fixed price supply to serve those loads. It would need to go into the market and acquire supply at today's costs.

Q. In your understanding, does Schedule 48 or the Special Contracts provide an obligation to do least cost planning to serve the Schedule 48 and Special Contract customers?

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A. No, the Company has no obligation to plan resources for those customers.

Q. And does the Company do least cost planning or long-term planning to serve those customers?

A. No, it does not.

Q. Is it correct that Puget Sound Energy occasionally enters into discretionary wholesale transactions?

A. Occasionally when its resources are surplus to its retail load needs.

Q. How are the revenues associated with your discretionary wholesale transactions treated under the merger rate plan?

A. During the period of the rate plan, the Company enjoys the benefits and bears the burdens of activities in the wholesale market, either sales or purchases. And, of course, post the rate plan under normalized rate making, those revenues would be credited

against costs, power costs for embedded cost service.
Q. So at least during the rate plan, it's part of the deal that Puget Sound Energy gets to keep the benefit of any discretionary wholesale transactions that are profitable to the Company?
A. Yes, that was the understanding in the rate plan.
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Q. In your view, if the profits from those discretionary wholesale transactions were taken away from Puget Sound Energy, would that be consistent with the merger rate plan?
A. Not in any way.
Q. Do Schedule 48 and the Special Contracts obligate Puget Sound Energy to serve the Schedule 48 and Special Contract customers ahead of discretionary wholesale transactions?
A. No, the Company's obligation to serve those customers is spelled out by the terms of the contracts and the tariffs, and generally they provide that the quality of service is dependent upon the availability of power in the wholesale market.
Q. Now you have referred to the quality of service, is it correct that quality of service means whether they get service or not?
A. That's correct.
Q. With respect to the pricing of service, is there anything that links the pricing of service to -- that provides -- let me rephrase that.
With respect to the pricing of service, is there anything that obligates Puget Sound Energy to ensure that the pricing is somehow better than the pricing for transactions in the discretionary wholesale
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market?
A. No, nothing.
Q. I would like you to take a look at an exhibit that has been marked with several different numbers. It was introduced in the Schoenbeck testimony as Exhibit 605. It's also been marked in the Puget Sound Energy set of exhibits, but we can stick to 605 if that's what's easiest.
JUDGE MOSS: What is the PSE number?
MR. BERMAN: It was 1525, Your Honor, and oddly enough, it may be that there are several PSE numbers for it, because it was used as an exhibit in several locations.
JUDGE MOSS: All right. Well, to the extent possible where we've got exhibits already in the record such as this one, we'll just rely on the one that's in the record, and you won't need to reintroduce it in the record later. So make a note that 605 is the same as 1525, and perhaps if you have other numbers, we will sort that out too.
BY MR. BERMAN:
Q. Do you have Exhibit 605 in front of you?
A. Yes, I do have it.

Q. Could you explain what this exhibit is?
A. This is a graphical depiction of the
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Company's monthly loads and resources for the year 2001. It's one of the tools that we use internally in managing the Company's loads and resources. And I note that it is a snapshot of those loads and resources as of June 12th, 2000.
Q. When you say it's a snapshot as of June 12th, 2000, does that mean that it's different today?
A. I would imagine it would be quite different today. There are a number of things in the Company's underlying power supply portfolio that are quite dynamic and changing.
Q. When you say that they're dynamic, does that mean that they change on an annual basis or a monthly basis, or what does that mean?
A. Well, in a limit, they change on a real time basis, they're constantly changing.
Q. Could you explain how it is that these things can change on a real time basis?
A. I could give some examples. For example, the Company's hydroelectric supply varies as a function of snow pack and stream flow, and we all know how dynamic the weather is. The loads and resources also vary with thermal plant availability. So, for example, if there are either forced or scheduled outages of thermal generators, it would have an effect on these resource
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bars.
And also, these bars are intended to depict the fixed versus variable nature of the Company's power supply resources, and it also depicts which resources are in the money and to what degree. And so as the power and gas market prices change, it would change the top portion of these resource bars.
Q. This exhibit has four pages. Could you walk us through each of the four pages and explain what each of the four pages mean?
A. Yes. The first page, and it's denoted by the second line of the title at the end with -A, this chart was built based on an average, an assumption of average hydro electric conditions, and it's for each of the 12 months of the year 2001.
If we turn to page two, it's the same chart, but it's built on the assumption of critical or worst case hydro electric supply.
CHAIRWOMAN SHOWALTER: I think it's actually page three of the exhibit; am I right?
JUDGE MOSS: That is correct.
THE WITNESS: Yes, that's right, I'm sorry.
A. Pages four and five of the exhibit are a longer term look at the loads and resources going all the way out through the year 2008. And again, page four
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is built on an average hydro assumption, and page five is built on a critical hydro assumption. All of those

snapshotted as of June 12th, 2000.

Q. Looking, for instance, at page five, could you give a general description of what that means that the bars seem to be declining in general each year whereas the line seems to be going up each year?

A. Yes, the decline in the resource bars is reflective of the expiration of various of the Company's long-term power supply contracts. The upward slope of the lines is reflective of anticipated load growth. And so you can see that by the time we get to the year 2002, at least under this set of assumptions, the Company no longer has adequate firm resources or at least economic firm resources to serve even its embedded cost loads, let alone the index price loads.

Q. Is this what you meant by attrition earlier on in your discussion?

A. Yes, exactly, it's the increasing divergence between the load line and the resource bars.

Q. So if you suddenly assumed an obligation to serve the Schedule 48 and Special Contract customers, would you have to do something to alter this graph or let's say alter the resource picture?

A. Yes, certainly to alter the resource picture.

And again, it would depend upon the nature of the service that was required to those loads and the pricing characteristics, but likely the Company would have to acquire additional supply in order to serve those loads.

Q. Is it fair to say that on a long-term basis that Puget Sound Energy simply doesn't plan to serve the Special Contract and Schedule 48 customers?

A. Yes, that's correct.

Q. And that's reflected in the resource graphs that are shown here in Exhibit 605?

A. Yes, that's right.

Q. Shifting from the long-term planning, could you explain how Puget Sound Energy serves customers on a day-to-day basis?

A. Yes. At the top level, what we have tried to do is arrange our portfolio in a way that month by month we have fixed price resources or resources whose costs do not vary with market available to serve our fixed or embedded price retail loads. And so that we have variable priced resources or resources whose prices do generally vary with market available to serve the index price loads such as Schedule 48 and the Special Contracts. And we use a variety of techniques including physical power purchases and sales and financial hedges to try and arrange our month-by-month portfolio supply

that way.

Q. Now you have referred to month-by-month, on a day-to-day basis, is there a distinction in the way you serve these different classes of customers?

A. Not so much on a day-by-day basis.

Q. Would it be fair to say that in any given hour, for instance, that you have a set of load, and you

work to serve it given the resources that you have?
A. Yes, that's right.
Q. In earlier testimony in the case, there was a reference to a lot of wholesale trading that was engaged in by Puget Sound Energy, some reference to 3 million data points, et cetera. Could you explain how that wholesale trading fits into the picture of serving the various sorts of load on a day-to-day basis?
A. Sure. The Company's overall objective is to manage its supply portfolio in a way that makes supply available at the time that it is needed for loads and to minimize the price risk to the Company. And so the data that was provided in response to the Complainants' data request was a download of all transactions that the Company had done in the wholesale market from January through November of last year, and it included all sorts of things.
It included hour-by-hour transactions that

the Company might do if it was surplus or deficit with respect to its loads. It includes day ahead transactions, which is the way that the Company balances the bulk of its supply and deficit. And it also included a very large volume of forward market transactions that the Company enters into either for hedging purposes or for economic optimization purposes.
Q. Just to get a sense of what you're talking about, if you could turn to page three.
CHAIRWOMAN SHOWALTER: Of Exhibit 605?
Q. Of Exhibit 605. Recognizing that this is a dynamic picture so the bars on this graph may not be exactly appropriate, when we look at March 01, there's a suggestion there that there's not quite enough resources in March 01 to actually serve all of the core customers plus the Schedule 48 and Special Contract customers. Would Puget Sound Energy engage in some sort of transactions to deal with that difference?
A. Yes, what the Company would try to do is supplement its fixed price resources so that the solid part of the bar would be as tall as the line marked with triangles. In other words, it would try to arrange fixed price supply to serve its fixed price loads. And it might do that either by purchasing fixed price supply or by entering into a fixed for floating price swap and

converting some of what is shown here as variable priced supply into fixed price supply or some combination of those things.
Q. When you say a fixed for floating price swap, could you explain what that is?
A. Swaps are also known as contracts for differences, and so it would be an agreement with a counter party where the counter party would pay Puget a floating price, and Puget would pay the counter party a fixed price related to the volume of power that needed to be swapped.
Q. Is that another word for a hedge?

A. Yes, it's one form of a hedge.

Q. On a day-to-day basis, if Puget finds after it's engaged in the types of transactions you have referred to that it has some excess supply, what does Puget Sound Energy do with that excess supply?

A. If it has excess supply that's economic, it generally sells that excess supply into the wholesale markets, usually on a day ahead or even an hour ahead basis, fairly short term.

Q. How does Puget Sound Energy decide where to sell that supply?

A. It tries to sell the supply into the market where it can derive the highest value.

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Q. Does transmission impact where you can sell your supply?

A. Yes, it does. The Company has transmission rights to various points on the Northwest grid, and although the bulk of its transactions are done at the Mid-Columbia, it does frequently utilize the transmission rights to move surpluses to points where they might have greater value.

Q. You said the bulk of the transactions are done at the Mid-Columbia. What is the Mid-Columbia?

A. The Mid-Columbia is a -- it's the middle stretch of the Columbia River in Washington state where a number of federal and non-federal hydroelectric projects are located and where many utilities have generation and transmission rights. And so it has become a trading hub, if you will, in the wholesale power market.

Q. Why would Puget do the bulk of its transactions at the Mid-Columbia?

A. A large part of Puget's supply portfolio is power generated at the Mid-Columbia and purchased from the public utility districts there. In fact, Puget is the largest purchaser of power from the Mid-Columbia project, so it has approximately 1400 megawatts of generation capacity there and has a significant amount

1477

of transmission capacity to move power in and out of that point.

Q. Do you have comparable trading rights at any other electric power trading hub, or do you have comparable transmission and power supply rights at any other electric power trading hub?

A. We do, we have both power and transmission rights at the California/Oregon border owing to our exchange agreement with Pacific Gas & Electric and our ownership interest in the Pacific intertie. We also have power and transmission rights at the Garrison Point in Western Montana associated with our Colstrip supply, and we have 425 megawatts of transmission rights to the Canadian border where we can transact business with BC Hydro.

Q. And do you engage in trading at those other locations as well?

A. We do, although again, the primary trading is done at Mid-Columbia.
Q. And again, why is Mid-Columbia favored over those other locations?
A. It is the primary trading point in the Pacific Northwest. It's where all of the marketers do their business. It's a much more liquid point than other points.

Q. Do you know why the marketers prefer to do trading there?
A. Yes, because of the liquidity and the multiplicity of players with transmission rights and generation at that point. And as we know, it has become the reference point for various indexes and so forth upon which the futures prices and swap and option contracts are based.
Q. And you have referenced certain swap contracts, is it true that Puget actually purchases swaps and options and other derivative products to manage its risks in the power markets?
A. Yes, it does do that.
Q. In general, when you make those purchases, could you describe how that would work?
A. Yes. The derivatives market and hedging techniques can become very complex, but the two basic building blocks are swap contracts and options contracts. And swaps are simply, again, a contract for differences that converts a fixed price into a floating price or vice versa. And an option contract is the right, but not the obligation, to purchase or sell power at a known price at some time in the future. And so those basic building blocks can be used in various combinations to achieve the hedging objective that the

Company might have at any particular point in time.
Q. Who do you buy those products from?
A. There are a variety of participants in the derivatives markets at the Mid-Columbia. Generally, it's the large energy trading companies, Enron, Aquila, Morgan Stanley, Southern Company, Deutsche Bank, so those are the larger players.
Q. Do you just call them up, or is there a way that you arrange that transaction?
A. There is a very active over-the-counter market or broker market, which is conducted, yes, primarily over the telephone.
Q. Is it correct that there's also an exchange that engages in such transactions?
A. Yes, the New York Mercantile Exchange launched futures and options contracts at the California/Oregon border and the Palo Verde point several years ago and then just this last summer launched similar contracts at the Mid-Columbia point.
Q. Do you normally acquire your derivatives on the exchange?
A. No, we do most of our derivatives business in

the over-the-counter market with the major energy companies who are market makers at that point.
Q. And why is that?
1480
A. That market just has become more robust and developed more liquidity. It's easier to do.
Q. Do you acquire these derivative products regularly?
A. Oh, I would say that we acquire them periodically. The Company has a risk management process that it conducts internally and looks at its load and resource situation several months at a time into the future and evaluates various alternative hedging strategies. And when it determines to put on a particular strategy, then it goes into the forward market and executes either physical or financial transactions to accomplish that.
Q. Do you have a rough sense of the last time that you acquired a financial derivative product?
A. Yes, for example, we acquired some call options for power supply at the Mid-Columbia for the winter period, November through February of this winter.
Q. Do you recall when you acquired those?
A. I believe it was during the early part of November.
Q. And why did you acquire those?
A. Well, in looking forward, we could see that at least on a peaking basis, we had a deficit of supply, and we wanted to control the price at which we might
1481
have to acquire that supply. So we purchased call options, which again are the right, but not the obligation, to purchase power at a particular location at a known price.
Q. I believe you mentioned that you might engage in financial transactions or physical transactions. Could you explain the difference between the two?
A. Yes. A physical transaction would be just a traditional purchase or sale of power such as the utility has always conducted. And the financial transaction would be one of the financial derivatives products, usually swaps or options, that I mentioned before. And so that's the distinction, although there really is often little or no pricing distinction between the two.
Q. You say there's often little or no pricing distinction between the two. Could you explain that a little more? Is there an adder that one has to pay in order to get a financial product versus a physical product?
A. No, not really. In the power market, as in most mature trading markets, there really is little or no distinction between price for physical transactions or financial transactions. They are fungible as between one another.
1482
Q. Let's talk about the load resource balance

for the coming year. We have several pages on this graph, and there is the average conditions and the critical conditions, and again I'm referring to Exhibit 605. What are the hydro conditions predicted to be for 2001?

A. We are now beginning to receive the initial forecasts of run off for the Pacific Northwest and particularly the Columbia River basin for the run off season in 2001. The latest forecast that we received was on January the 9th, the so-called January final forecast for the Columbia River, and it shows 76% of average run off for the Columbia River at the Dalles over the period January through September of 2001. That is a very low forecast. In fact, it is among the 4 lowest years in the past 30.

Q. I'm afraid I don't have the January 9th forecast with me, but if we turn to Exhibit 1401.

A. Yes, I'm sorry, this was the forecast issued just before that.

CHAIRWOMAN SHOWALTER: Can you wait until we get that, 1401?

MR. BERMAN: 1401.

MR. TROTTER: Excuse me, Your Honor, we're having trouble finding that.

MR. BERMAN: It was tabbed 71 in the books that were distributed by --

JUDGE MOSS: Just to perhaps facilitate things as we move along here, the exhibits that are anticipated for Mr. Gaines on direct examination were furnished by PSE under tab numbers PSE-71 through PSE-78 in three-ring binders that were furnished to everyone.

MR. TROTTER: I don't think we got the binders, but we found it.

JUDGE MOSS: Are counsel ready now?

MR. TROTTER: Yes.

JUDGE MOSS: Okay, and I think the Bench is ready as well, Mr. Berman, thank you.

BY MR. BERMAN:

Q. Looking at Exhibit 1401, could you explain what that is?

A. Yes, this is the January early bird forecast, which is the first forecast of the season.

Q. And did I understand you or is it correct that the January 9th forecast that you have referred to is consistent with this forecast?

A. Yes, it's very consistent. It's different by only 1%.

Q. And on this Exhibit 1401, I see that you have highlighted the Grand Coulee entry; is that correct?

A. Yes, that's right, and the reason for that is that the Mid-Columbia projects from which the Company obtains a significant amount of its power supply are directly downstream from Grand Coulee, and so whatever the run off at Grand Coulee turns out to be will determine the amount of generation that the Company obtains over the forecast period.

Q. And so if we look across at this column where it says percent and then it says 75, that's the number that you were referring to?

A. Yes, that's right.

Q. And now it has gone up to 76, you said?

A. Yes, that's right.

Q. Who puts out this forecast?

A. This is a unit of the National Weather Service, it's the Northwest River Forecast Center that's located in Portland, Oregon.

Q. Is this something that you rely on in your day-to-day business?

A. Yes, very much.

Q. I see that you have put a note on the right-hand side of the first page of 1401. Could you explain that note?

A. Yes, I did a rough calculation of the difference in generation that the Company will

experience between an average stream flow year and a 75% of average stream flow year. And I said here that it is more than 1 million megawatt hours of shortfall. It's actually closer to 1.2 million megawatt hours less generation in a year such as the one that is predicted for 2001 than an average year upon which we typically base our planning.

Q. In the resource stack charts that are shown in Exhibit 605, would the type of year that these forecasts predict make it closer to an average hydro year or a critical hydro year?

A. It would be very close to the critical year, keeping in mind that that earlier exhibit was a snapshot in time which now is six months old.

Q. Now you have said that you might have to acquire as much as 1.2 million megawatt hours of additional power as a result of these forecasts?

A. Yes. The way to think about this from a value point of view is that any of this hydro shortfall, whether it's needed to serve load or whether we're otherwise surplus and sold in the wholesale markets can be valued at the market price. And so it's a simple matter to make an assumption about what the market price of power will be in 2001 and apply it to this generation shortfall, and that will be the value impact on the

Company versus an average year.

Q. So, for instance, if it's 1.2 million megawatt hours and the market price were $100 per megawatt hour, that would be $120 Million?

A. That's correct.

Q. And if the market price were $200 a megawatt hour, then the impact would be $240 Million?

A. That's correct.

Q. Are there other potential contingencies that could impact the amount of value that could be lost to the Company as a result of -- in the electric supply

resource management?
A. There are. There is always the risk of an unscheduled outage of one of the thermal generators. In fact, we did experience that with one of the Colstrip units for a six week period late last summer. Those things are unpredictable, and so they don't show up in the planning, the load resource graphs here, but they do occur.
We also have certain contingent obligations to supply power to third parties, in particular one of our contracts with the Bonneville Power Administration obligates up to supply certain amounts of power to them, and those provisions have not been triggered historically, however, Bonneville has informed us that
1487
in 2001, they will trigger them.
And more recently, the federal government has determined that Northwest utilities should be obligated to provide power to California to supplement supplies there.
And so any of those things will draw on the Company's available resources.
Q. Let's talk about the potential loss of Colstrip. What would be the impact on the Company of a prolonged outage at Colstrip?
A. When we lose a Colstrip generator, the value computation is fairly simple. It's the amount of capacity lost multiplied by the number of hours of the outage multiplied by the difference between the market value of power and the incremental operating costs of Colstrip. And for the purpose of this discussion, we can assume that the incremental operating cost of Colstrip is something less than 10 mils a kilowatt hour.
JUDGE MOSS: Mr. Berman, would this be a convenient point to take a short break?
MR. BERMAN: Certainly, Your Honor.
JUDGE MOSS: Okay, why don't we take 15 minutes and come back at about 5 after the hour.
(Brief recess.)
JUDGE MOSS: All right, we will be on the
1488
record.
Mr. Berman, please proceed.
BY MR. BERMAN:
Q. Just before the recess, we were talking about potential contingencies that could impact the operation of the Company. In doing your planning, do you try to protect yourself from such contingencies?
A. We are trying to do that, and it is much easier, well, it's really not easy in either case, but protecting against price contingencies is one thing, but protecting against volume related contingencies is something else. So, for example, a volume supply shortfall that resulted from poor hydro or a forced outage where timing is unpredictable is difficult to do, but we try.
Q. Does it make sense to look at the earnings

that Puget Sound Energy makes in any given day from its energy sales?

A. Not really, for a couple of reasons. First of all, the transactions, the power transactions that the Company is engaged in on any particular day may have been engaged in on that day, on the day prior, it could have been engaged in many months prior or even many year prior. And so when you look at an hourly slice of transactions that contains transactions that are entered

1489

into at various points in time, those things are not too meaningful. They're kind of apples and oranges and coconuts, if you will.

The other reason is that the Company's surpluses and deficits vary seasonally and even within seasons, and they're very dynamic. And so there might be a day, for example, where temperatures are warm, hydro is high, company has significant surpluses and is selling, that might be a very good day. There might be another day where temperatures are low, loads are high, low hydro, forced outages, and the Company would be purchasing a significant amount of power. And so those things are quite variable from day to day, and it's really only meaningful to look at the Company's financial situation over longer periods of time.

Q. Does longer periods of time mean on a month-to-month basis?

A. Well, not really even on a month-to-month basis because of the seasonality of loads and resources. So it seems to me to make more sense to look over a longer period of time than that.

Q. So you're saying that you might make money in a given month but might lose money in another month?

A. Exactly, and that certainly has happened over the course of this past year. And make money, again, is

1490

a relative term. We always have to know relative to what. It's a little difficult to look at just a narrow slice of the Company's financial activity and ignore everything else.

Q. Let's switch topics right now and move to the Mid-Columbia Index. Could you explain to me generally your understanding of what the Mid-Columbia Indexes are?

A. Certainly. The Dow Jones Mid-Columbia Indexes, which are the indexes used for pricing under Schedule 48 and the Special Contracts, are an objectively determined indicator of wholesale transaction prices at the Mid-Columbia. They're prepared by Dow Jones. Dow Jones has specific transaction reporting requirements. There are a number of market participants who report data to Dow Jones, probably 15 or 20 at last count. There's an auditing process that Dow Jones does periodically on the transaction data that is reported. And so far as I know, they are recognized as the most objective and verifiable indexes or indicators of market price at the Mid-Columbia available.

Q. Could you explain the process that Puget Sound Energy goes through to report information to Dow Jones for the Mid-Columbia Index?
A. Yes, we do that daily. We look at all of our
1491
transactions for a day, and for those transactions that fall into the reporting requirements as defined by Dow Jones, we accumulate that data and turn it in to them daily.
Q. In what form do you turn it in?
A. I believe we fax it to them.
Q. Does Dow Jones use all the data you provide them?
A. Not necessarily. In talking with the people at Dow Jones who prepare the indexes, they do occasionally do some filtering of data and some reasonableness checking, so that if data falls outside of a range, they may exclude it from the index on any particular day.
Q. Do you know all the criteria that are used by Dow Jones in doing that filtering?
A. No, I don't.
Q. So do you know what percentage of the transactions that you report to Dow Jones are actually reflected in the Dow Jones Index?
A. No, I don't.
Q. Does Puget accurately report the information to Dow Jones?
A. Yes, absolutely.
Q. Does Puget ever make any effort to withhold
1492
information from Dow Jones?
A. Never, and any suggestion that has emerged in this hearing that Puget is in some way manipulating the index is offensive and ridiculous. It just doesn't happen.
Q. There has been a reference to something called net zero transactions. Have you looked into what those transactions are?
A. Yes, I have, and it turns out that during the latter part of 2000, Puget was engaging in some transactions at the Mid-Columbia that were designed to relieve the power scheduling burdon on the public utility districts at the Mid-Columbia. In the daily power scheduling process, many of the transactions need to flow through the control areas that are operated by those PUD's, and they're relatively small organizations and have administrative difficulty dealing with the volume of transactions. So Puget was performing a schedule aggregation service, if you will, taking in a number of schedules from counter parties, aggregating them, and providing then only one aggregated schedule to the public utility districts to ease their scheduling burdon.
Q. So is it fair to say that because you were a scheduling aggregator that you weren't actually doing a
1493

power transaction, you were just providing a service to allow the schedules to work properly?

A. Yes, that's right, Puget -- the transactions had no financial effect on Puget.

Q. Was anything reported to Dow Jones about those transactions?

A. No, we consciously excluded them from the transactions that we reported to Dow Jones.

Q. And why did you exclude them from the transactions reported to Dow Jones?

A. Because they really weren't transactions that we were engaging in as a principal, and we didn't want any of that to distort the index.

Q. Has Puget entered into transactions with other counter parties in an effort to impact the index?

A. No, never.

Q. Has Puget entered into transactions with other counter parties to alter regional market prices?

A. Never.

Q. In your view, does the Mid-Columbia Index overstate spot market prices in the region?

A. No. My belief has been and continues to be that those indexes are the best representation available of spot market prices at those points. And I think that that's reflected generally in the market, because if you

1494

think about it, all of the swap and options transactions that we have been talking about are based on that index. And so all of the major energy companies that trade at that point must have concluded that it's a sufficiently credible index upon which to base the hundreds of millions of dollars of derivative transactions that they do every year.

Q. Is the Mid-Columbia Index thinly traded?

JUDGE MOSS: We have an objection.

MR. TROTTER: I will object to the question as to its foundation without reference as to whether he's referring to the Mid-C Non-firm, Firm, or whatever other index that might be out there or if he's just asking in the aggregate. But as the question is stated, there's no foundation upon which an understandable answer could come.

MR. BERMAN: Perhaps the witness could answer in relation to the various indexes and give his opinions on that.

A. Yes, I do appreciate that, because I think -- I think when we ask about liquidity, we have to talk about it relative to something. And so is the non-firm index more thinly traded than the firm index, yes. Is that new news, no. The Complainants knew that at the time of the complaint case in Schedule 48 last year. In

1495

fact, they were warned by the Company about that and insisted instead that their purchases be based on the non-firm index.

BY MR. BERMAN:

Q. Although the non-firm index may be more

thinly traded than the firm index, is it your view that
the non-firm index overstates spot wholesale prices in
the region?
     A.   No.
     Q.   In general, how does the non-firm index
prices compare to the firm index prices?
     A.   Well, that's an interesting question. In the
first several years of the index, if you looked at an
average, the non-firm index generally tracked a couple
of mils below the firm index. The experience this year
has been quite different. There have been periods when
the non-firm index price is significantly below, and I
believe on average it has been below for the year, but
there have also been periods where it's significantly
above. And so there has been quit a lot of volatility
in the delta between the two indexes, particularly in
the latter half of this year.
     Q.   I think you said you warned the Complainants
about the non-firm index. Could you elaborate on that
just a little bit?

     A.   Well, in the proceeding that is now being
referred to as the complaint case, the Company pointed
out that the non-firm index was based on less
transaction volume than was the firm index or than was
the blended index which the Company was advocating in
that case. But notwithstanding that, the customers
insisted and finally prevailed in obtaining pricing
based on the non-firm index presumably because, at least
at that time, it was tracking a couple of mils lower
than the firm index.
     Q.   Let's switch topics again. You have
discussed a little bit in your testimony some ways in
which Puget Sound Energy has worked to manage risk. In
your view, do the customers have any options for
managing risk?
     A.   Yes, that was the purpose of the optional
price stability provision that was inserted in Schedule
48. However, I have to say that even without that
provision, the customers are always free to use the
derivative markets and the market makers in order to
hedge their risk directly.
     Q.   Is it your understanding that some Schedule
48 and Special Contract customers have entered into
hedges or derivative products on their own?
     A.   Yes, I understand that they have.

     Q.   And is it your understanding that some
customers have also arranged price stability through the
good offices of Puget Sound Energy?
     A.   Yes, there have been a few that have done
that.
     Q.   Has Puget Sound Energy discussed hedging
options with the customers over the years?
     A.   Well, it has. The Company has spent a
significant amount of time presenting tutorials to the
customers about hedging techniques, introducing the

customers to major players in the wholesale power and derivatives markets, has acted as a facilitator or a sleeve, if you will, for hedging transactions with certain customers. And so there's a tremendous history, I would say, over the last two years of the Company trying to provide information and assistance to the customers in this area.

Q. You said a sleeve, could you explain what that word means?

A. Simply a middle person in the transaction. Some of the customers for various reasons found it preferable to do their transactions directly with Puget, and so Puget stood in between, if you will, the customer and the actual provider of the derivative product.

Q. You have reviewed the response to Puget Sound

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Energy's response to Bench request Number 2; is that correct?

A. Probably, but I don't recall which one it was.

Q. That is the very, very thick response that has various options and hedging E-mails and presentations.

A. Oh, yes, I remember it, yeah.

Q. Does that response contain materials that demonstrate the discussions between Puget Sound Energy and the customers over the past several years?

A. It does. I think what you will find in that data response is a number of presentation materials that are in the nature of tutorials and backgrounders for the customers about hedging, put on both by the Company and by various third party dealers who the Company has brought in and introduced to the customers. I think in that package of material, you will also find some specific pricing indications that were provided to the customers and at which they could have executed hedges at various points in time.

Q. In those materials, there are a number of references to Duke/Louis Dreyfus; could you explain that?

A. Yes, there was a period of years early in the

1499

Schedule 48 effective period where the Company had a loose alliance with Duke Louis Dreyfus, who at the time was one of the early power trading and marketing companies. And so early in the period, we did use Duke/Louis Dreyfus as a facilitator and as a source of information and price quotes for the customers.

Q. Does that alliance still exist?

A. No, it does not.

Q. Since that ended, have you continued to offer various price stability options to customers?

A. We have. We meet with the customers periodically and also on their specific request, and we provide indicative price quotes weekly to a number of the customers showing them forward market prices out many months at which they could fix the price of their power.

Q. Could you take a look at Exhibit 1408, which appeared at tab 78 in the materials that Puget distributed prior to the hearing.

A. Yes, I have it here.

Q. I will wait a moment until everyone else has found it.

Could you explain what the materials at Exhibit 1408 are?

A. Well, these are examples of the forward price

1500

information that we send to the customers weekly, and so it's become more or less a standard format like this where every week we provide a spreadsheet showing the forward market prices out through the end of 2001 and on for a couple of years into the future. And these are swap prices, if you will. These are prices at which the customers could fix their power price if they so choose.

Q. Could customers really do deals at these prices, or is this all just theoretical?

A. Customers could really do deals at these prices. These are the prices at which the Company executes derivative transactions for its own purposes, so there's no question but what these prices are achievable.

Q. Let's talk about other options for dealing with the current market situation. Is it correct that Puget Sound Energy has looked into obtaining temporary additional generation?

A. Yes, we're working on that presently, as are a number of utilities in the area. The City of Tacoma has already installed a number of temporary diesel generators in its tide flats area just because of the market price of power, really for the same reasons, I think, that a number of the industrials are doing it.

Q. We have heard talk during the hearing about

1501

air emission issues related to diesel generation. If there are air emission issues, how could utilities like the City of Tacoma acquire temporary generation and intend to rely on it?

A. I think it depends a lot on how long the entity would intend to operate the generator. My understanding is that there are temporary permitting arrangements that allow operation for the short term without special air emissions reduction equipment. But then after that, there's a more formal longer term permitting process which usually requires BACT, best available control technology. So if an entity were planning to rely on those generators for the long run, it would likely be obligated to install this state of the art control technology which is available.

Q. You say it is available. Is there control technology that can be applied to temporary diesel generation to control air emissions?

A. Yes, it's a technique that's also used for combustion turbine power plants. That's called

selective catalytic reduction.
Q. Is that kind of like a catalytic converter?
A. Yes, it's very much like a catalytic converter in an automobile.
Q. I believe one of the witnesses in the
1502
Complainants' case said that control technology is only available for permanent generation; is that true?
A. That's not my understanding, no.
Q. And has Puget Sound Energy investigated the availability of control technology for temporary generators?
A. We are presently investigating it, and we are told that it is available.
Q. Does Puget Sound Energy use diesel fuel currently to generate power?
A. We have been using diesel fuel these last two months or so in our combustion turbines because of the relative price of diesel versus natural gas here in the Northwest.
Q. That may confuse some folks who thought that your combustion turbines burned natural gas; could you explain?
A. Well, our combustion turbines are dual fuel, so they're capable of burning either natural gas or a liquid fuel such as diesel or jet. And it is true that historically natural gas has been less costly than liquid fuel on a per million btu basis, but with all of the activity in the gas market in the last couple of months, we actually have a situation here where Number 2 diesel fuel is less costly, and so that's what we have
1503
been doing.
Q. Have you encountered any -- let me back up.
About how much generation do you have that runs on diesel fuel?
A. I believe that presently we're operating approximately 300 megawatts of combustion turbines on diesel fuel.
Q. Have you encountered any difficulties in procuring enough diesel fuel for that 300 megawatts of generation?
A. No.
Q. Has your procurement of diesel fuel for that generation caused a shortage, to your knowledge?
A. Well, not that I know of. And I think, in fact, it's reflected in the pricing. Because when we began acquiring this fuel back in early December, I think we were paying about $1.10 a gallon, and at last report, I think I was told we were paying about 85 or 90 cents. And so to the extent that the supply and demand relationship affects price, you could reasonably conclude that there's not a shortage.
Q. You mentioned the City of Tacoma obtaining generation. Do you have any more details on that?
A. Only that I have been told that the City utility has installed about 40 megawatts of internal

1504

combustion diesel generators in its tide flats area, and the reason, of course, is that it also is exposed to the wholesale market price of power, having in 1995 diversified a portion of its supply away from the low cost BPA power.

Q. Have you heard of other utilities using temporary diesel generation?

A. Yes, particularly in California that is happening. And, in fact, the independent system operator in California just within the last several months has conducted a request for proposals for temporary generation in California. Many of the bids it received were for internal combustion diesel. We saw the same thing happen in the mid continent area of the country in the summer of 1998 when there were very high wholesale power prices in that region.

Q. Under their contractual arrangements with Puget Sound Energy, do the Schedule 48 and Special Contract customers have the right to use this temporary generation?

A. Yes, so far as I know, there's no prohibition against self generation.

Q. If rather than installing temporary generation, the customers wanted to install a more permanent generation such as co-generation, do they have

1505

the right to do that?

A. Yes, I believe so.

Q. To your knowledge, do any of the customers have co-generation facilities?

A. If they do, it would only be a small amount and which I'm not aware of.

Q. Are there any other options available to the customers to deal with high power prices that we have not discussed yet?

A. Well, I think broadly we have discussed hedging and forward purchasing of power, and we have discussed self generation, both of which are alternatives available now. Others probably include efficiency improvements in their various industrial processes, which should be economically motivated by these higher prices.

Q. To your knowledge, is it true that in regions of the country where power prices have historically been higher than the Northwest that industrial customers have engaged in shifting of load to low cost time periods?

A. Yes, I'm sure that that has occurred, although most of my experience has been right here in the Northwest.

Q. Are you familiar, for instance, with pumping of water projects in California that has typically

1506

occurred in off-peak hours?

A. Yes, I'm familiar with the water system in California, California Department of Water Resources and its generation of load patterns where it does most of

its pumping at night with lower cost power and then releases the water during the day and actually even does some generation at its pumping facilities.
Q. Are you familiar with the term an interruptable load?
A. Yes.
Q. Is it correct that there are some industrial types of customers around the country who accept interruptable arrangements where they can cut their production when prices are high and increase production when prices are low, when electric prices are low, in order to make a -- to efficiently operate in a volatile power environment?
A. Yes, there are a wide variety of different interruptable arrangements, and even in this region, in notably the aluminum industry has operated that way for many years.
Q. We have heard at other points in this proceeding of the buy-sell option. Could you explain what the buy-sell option means?
A. The buy-sell option is a mechanism that the
1507
Company has been exploring with the customers which has the economic effect of taking the customers to market, providing them access to market.
Q. Would you say that the buy-sell arrangement gives open access to those customers who want it?
A. I would say that for all practical purposes, it is equivalent.
Q. Is it correct that Puget Sound Energy has, in fact, filed with this Commission a tariff that would allow buy-sell arrangements by the Schedule 48 and Special Contract customers?
A. Yes, we just recently have filed that.
Q. Let me shift gears again. Did you look at the revenue analyses and spreadsheets that were prepared by Mr. Schoenbeck and Mr. Lazar?
A. I did briefly as Mr. Schoenbeck was testifying, yes.
Q. Is the data on those analyses accurate and reliable as you see it?
A. No.
Q. Could you explain?
JUDGE MOSS: We have an objection.
MR. VAN CLEVE: Your Honor, I think we have a lack of foundation here where there's been no reference to which specific exhibits that Mr. Berman is referring
1508
to.
JUDGE MOSS: I think he referred specifically to the spreadsheet analyses performed by Mr. Schoenbeck and Mr. Lazar and that the witness testified he reviewed during their testimony, so that would be the exhibits in those witnesses' testimony.
MR. VAN CLEVE: Right, but there's a number of different spreadsheets that have different kinds of analyses that were presented by Mr. Schoenbeck.

CHAIRWOMAN SHOWALTER: I have to say in order to understand the answer, I want to know what document we're talking about.
JUDGE MOSS: It would be well to be specific to exhibit numbers, Mr. Berman. Would we want to look at 617, for example?
MR. BERMAN: I was thinking we could look at Exhibit 1302.
JUDGE MOSS: That would have been one of Mr. Lazar's?
MR. BERMAN: Yes.
BY MR. BERMAN:
Q. Do you have Exhibit 1302 in front of you?
A. I believe so, yes.
Q. Generally speaking, do you believe that the analysis performed by Mr. Lazar in that exhibit
1509
accurately reflects the cost of service for Puget Sound Energy?
A. No, I don't believe much of anything in this analysis. It's basically swiss cheese.
Q. Could you give a general explanation of why that analysis is swiss cheese?
A. Well, it's founded on a number of assumptions which are either out of date or wrong. It's founded on a load resource table snapshot as of June last year. There was an eyeballing, I'm told, of the Company's loads and resources in converting the graphs into numerical data. We have -- although we have a June snapshot of loads and resources, we have a December 20th forecast of forward market prices, which happens to be about the highest forward market price of any point in time for the year 2001. I think we have used NYMEX gas prices rather than SUMAS gas prices. I think we have double counted some of the resources. I can't rely on this at all.
Q. When you said we in your responses just now, are you referring to Mr. Lazar?
A. Yes.
Q. I would like you to take a look now at Exhibit 617 prepared by Mr. Schoenbeck, and I will get a copy of that in front of you.
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And this is a confidential exhibit, but I think we can talk about it without referring to specific numbers. The backup to that exhibit I think was premised on the Lazar analysis. Does it suffer from the same defects as the Lazar analysis you have just described?
A. Yes, it's my understanding that it's premised on that, and so therefore, it would have the same deficiencies.
Q. In Exhibit 617, there's purportedly an analysis of the incremental cost of serving these various Schedule 48 and Special Contract customers. Do you agree that that analysis accurately measures the costs that should be attributable to those customers?

A. No, not at all.
Q. Could you explain why?
A. There are several reasons. One is that the analysis is out of date. Another is that I'm not sure we have used the right per unit cost information. Another is that at least as I understand it, it is only variable costs and not the full cost of resources. There are just a variety of deficiencies.
Q. How about the general premise of both the Lazar and Schoenbeck exhibits, which is to look at the cost of the next incremental unit used to serve these

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customers; do you agree with that premise?
A. Well, I don't know what it has to do with Schedule 48 or the understandings that were reached in the merger rate order, because they don't have anything to do with the incremental cost of resources.
Q. Would you agree that it would be a fundamental change to the Schedule 48 pricing and Special Contract pricing to somehow link it to those incremental costs?
A. Certainly. Schedule 48 is not a tariff with prices based on incremental costs. It's a tariff with prices based on market indexes. The two are not related and never have been, were intended to be. So it would be a fundamental change, yes.
Q. Is Puget Sound Energy willing to accept a unilateral revision by the customers to the index used in Schedule 48 or the Special Contract?
A. No, it's not, and there's no provision for that.
Q. Is it reasonable to return the Schedule 48 or Special Contract customers to Schedule 49 rates or to some other preexisting rate schedule at this time?
A. No, that would be inconsistent with the merger rate plan.
Q. Is it consistent with the planning decisions

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that Puget Sound Energy has made over the past several years?
A. No. As I have indicated, we have taken certain actions and actually not taken certain other actions in reliance on our understanding of the pricing under Schedule 48, and as I indicated, many of those things can not be undone. And so it would be inconsistent with our planning actions and inconsistent with the merger rate plan.
JUDGE MOSS: Mr. Berman, we're up against the lunch hour, I wonder how much you have remaining?
MR. BERMAN: I'm very, very close to wrapping up. I would expect somewhere in the 5 to 15 minute range, probably closer to the 5, just a few final points to wrap up.
JUDGE MOSS: Let's press on then.
BY MR. BERMAN:
Q. Just a few final points to wrap up here. One, I would like to show you what has been marked as

Exhibit 1402, which was tabbed 72 in the documents that Puget provided previously.

A. Yes, I have that.

Q. These are two pages. Could you describe briefly what these two pages are?

A. Yes. We went back and plotted the

1513

Mid-Columbia Non-firm Index price for the year 2000 and continuing as far as we could into the year 2001, and this first page is a graph of that daily plot. The second page is a plot of the same thing but only over the period since the customers brought their complaint in this proceeding.

Q. Is it correct that generally speaking throughout this month that prices at the Mid-Columbia for the non-firm index have been in the $100 to $200 range?

A. Yes, that's right.

Q. I have to wrap up a point about the City of Anacortes. What voltage level is the City of Anacortes served at?

A. The City of Anacortes owns its own substation and therefore takes delivery at the 115,000 volt level on the high side of that substation.

Q. Is that high voltage?

A. It is.

Q. In your view, is the City of Anacortes eligible for service under Schedule 48?

A. Yes, absolutely.

Q. And why is that?

A. The schedule provides that any high voltage customer is eligible to take service under Schedule 48

1514

regardless of its load level.

Q. Let's switch gears to Air Liquide. Could you please take a look at Exhibit 1405, which appears at tab 75 in the materials previously distributed.

A. Yes, I have that.

Q. Could you explain what Exhibit 1405 is?

A. 1405 is a letter agreement between the Company and Air Liquide which appears to have been executed about the time that Air Liquide went onto Schedule 48 service.

Q. Going down the page to the part that has the handwritten bracket on the side, it says:

> Load may not be transferred from bank one to bank two to avoid high market rates or unavailability of energy.

Could you explain why such a provision would be included in the agreement with Air Liquide?

A. My understanding is that Air Liquide takes service from the Company under two different rate schedules, both under Schedule 48 and under another schedule, I believe 46, through two different transformer banks. And my understanding of this provision is a requirement that there not be load shifting between the two banks, and the purpose is to avoid gaming of the price.

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JUDGE MOSS: Mr. Berman, just a minute.

We don't have a question pending, Mr. Van Cleve.

MR. VAN CLEVE: Your Honor, I'm going to object to the relevance of this line of inquiry. I don't understand how the potential load shifting by Air Liquide relates to the issues in this case.

JUDGE MOSS: Well, the letter certainly relates to the relationship between the Company and Air Liquide, one of the Complainants in the case, and I think it's a fair game for examination, so I will overrule the objection.

BY MR. BERMAN:

Q. I would like to turn your attention now to Exhibit 1406, which doesn't say confidential on it, but pursuant to the discussion on Friday, the Company is designating as confidential because it has information concerning Air Liquide. I think we can discuss it here without actually repeating the numbers, so I don't think we have to go into confidential session to discuss it.

JUDGE MOSS: This is 1407?

MR. BERMAN: 1406.

JUDGE MOSS: I'm sorry, 1406.

MR. BERMAN: Which appears under tab 76.

JUDGE MOSS: That's right, I have 1406, so

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that will be marked confidential.

MR. BERMAN: So I guess that would be 1406-C.

JUDGE MOSS: Correct.

BY MR. BERMAN:

Q. Mr. Gaines, without describing any of the -- without disclosing any confidential information in this exhibit, can you please explain what this page represents?

A. This page shows the amount of load served at the Air Liquide facility under each of the schedules I mentioned, Schedule 48 and Schedule 46.

Q. Keeping in mind the sentence that we reviewed in the prior exhibit concerning load shifting between the different banks, what does this Exhibit 1406-C show to you?

A. It shows to me that in the last several months, Air Liquide has apparently been engaging in some self help by transferring load from the higher cost Schedule 48 bank to the lower cost Schedule 46 bank in apparent violation of the letter agreement that we just looked at.

Q. Has Puget Sound Energy authorized Air Liquide to switch load from Schedule 48 to Schedule 46?

A. No, we have not.

MR. BERMAN: Your Honor, I'm through with my

1517

direct examination. I would move the admission of Exhibits 1401, 1402, 1405, 1406-C and 1408, and the other exhibits that were previously marked I will not

move.
JUDGE MOSS: All right, Mr. Trotter, do you have an objection to one or more of those?
MR. TROTTER: No, I'm just standing for a more convenient viewpoint.
JUDGE MOSS: All right, then I take it there is no objection to any of these exhibits, and they will be admitted as marked.
This would be a convenient time to break for lunch. We will be in recess until 1:15 p.m.
(Luncheon recess taken at 12:05 p.m.)

A F T E R N O O N   S E S S I O N
(1:20 p.m.)

JUDGE MOSS: Counsel, if you're ready, I believe, Mr. Berman, that your witness is available for cross-examination.
MR. BERMAN: Yes, Your Honor.
JUDGE MOSS: All right, then I recollect, I don't have my notes here, but I think that the order we said the Complainants will go first on PSE's witnesses;
1518
is that correct? I don't care, tell me.
MR. TROTTER: I'm happy to go first and maintain the same order.
MR. VAN CLEVE: Doesn't matter to me.
JUDGE MOSS: All right, go ahead, Mr. Trotter.

C R O S S - E X A M I N A T I O N
BY MR. TROTTER:
Q. Mr. Gaines, I would like to start with the City of Anacortes situation, and could you refer to the tariff Schedule 48, which one copy at least is in tab 2 to the Company's brief attachments.
A. Yes, I have it.
Q. And you said that in your opinion, the City of Anacortes was eligible because they are a high voltage account; is that correct?
A. Yes, that's right.
Q. And so you interpreted the last phrase of paragraph Roman Numeral I, Arabic 1, that says, "with annual loads over 2.4 average megawatts," that that phrase does not modify high voltage accounts?
A. Yes, that's the way that the Company has consistently interpreted the activities.
Q. So I take it that the Roman Numeral I,
1519
paragraph 2, did not apply since the City of Anacortes does not have multiple primary voltage accounts on the same distribution feeder and that they were aggregating their accounts?
A. I believe that's right.
Q. I would like to refer you to Exhibit 101, which was one of Mayor Maxwell's exhibits. Do you have that?

A. Yes.
Q. And I believe Mr. Maxwell testified that this was a document prepared by Puget. Is that consistent with your knowledge, or have you ever seen this before?
A. No, I haven't seen this one before.
Q. I would like you to look at the first page, projected load, and it shows consistently in the historic kilowatt column a 2.451 average megawatt load. Do you see that?
A. Yes.
Q. And do you know how that was computed for the City of Anacortes?
A. No, I don't.
Q. Do you have an understanding of what occurs if a customer has, let's say a 2.4 megawatt condition applies to a customer, the customer has such a load, and then its load consistently on an actual basis is say 1

1520

average megawatt, what happens in that context with regard to their eligibility for Schedule 48?
A. No, I don't think I do have a perfect understanding of that. Obviously to determine eligibility in the first place, there would necessarily be a backwards look at historical loads. But on the question of whether a customer has to maintain that load for some period of time to remain eligible on the 2.4 megawatt standard, I'm just not sure.
Q. And can you discuss the hedging opportunities that Puget offered or discussed with the City of Anacortes?
A. Probably not all of them. I know that there was one hedge arrangement that was, I don't know if it was offered by the Company, but it was facilitated by the Company to Anacortes, and the counter party in the end determined that it did not want to make the hedge available to such a small load in that particular instance. I'm not sure though that there was an exhaustive search done of the market for alternative products.
Q. Is the size of a load a factor for these third parties, according to your experience, in order to offer a hedge?
A. It can be when the loads get very small,

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although, on the other hand, the loads could aggregate together and probably obtain hedges from just about anybody.
Q. Was Schedule 48 initially proposed with a condition that customers could aggregate their loads apart from being served on the same distribution feeder?
A. I don't know.
Q. The order in UE-960696 said that:

> Schedule 48 would be optional and available to all customers served at high voltage and primary voltage with aggregated loads over 2.4 average megawatts.

Do you know what aggregated loads means in that context?
A. I'm not sure I know which document you're looking at.
Q. It's tab 6 in that same addendum to the Company's brief, the Commission order approving Schedule 48 with conditions, page two, under availability.
A. It looks to be fairly parallel to the language that's in the tariff itself.
Q. So aggregated loads in that context would refer to multiple primary voltage accounts on the same distribution feeder?
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A. That's my impression, yes.
Q. Do you know any Puget customer served under Schedule 48 that received a hedge and had a load under 2 average megawatts?
A. We don't know about all the hedges that the customers have done.
Q. I'm just asking the ones you're aware of.
A. No, not that I'm aware of.
Q. Do you believe the spot market at the Mid-Columbia as measured by the indexes reported there is a competitive market?
A. Yes.
Q. Have you always believed that?
A. Yes.
Q. Do you believe there is no price at which it would be unreasonable to set at retail rates based on Mid-Columbia Indexes for the term of the Schedule 48 service agreements and the Special Contracts?
A. I believe that to the extent that the customers on Schedule 48 insisted on purchasing at market and subsequently on these indexes that the price level that the index reaches really doesn't have anything to do with fairness. I mean they have agreed to do that.
Q. Does your same answer go to the notion of
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unreasonableness?
A. Yes.
Q. So if the Mid-C Non-firm Index, and that's the index under which the Schedule 48 service agreements are priced?
A. Yes.
Q. If that index went to $3,000 an average megawatt today, that would result in a reasonable price in your opinion?
A. Yes, that's right. Keep in mind that what the customers wanted in the beginning was market access, and Schedule 48 was eventually developed as a reasonable alternative at that time to market access. And so had the customers had market access and had they chosen to continue to purchase at index, that's the price that they would be paying. It's the price that anyone else in that market pays.
Q. Is there anything inappropriate about using

the Mid-C Non-firm Index for purposes of Schedule 48 in your opinion?
A. Not that I can think of.
Q. Do you understand the complaint in this proceeding is a challenge to the fairness, justness, and reasonableness of the existing tariff structure in Schedule 48?

A. I understood that it was a request for some emergency relief.
Q. I would like -- you participated in UE-981410, did you not?
CHAIRWOMAN SHOWALTER: Can you identify these in addition to the number?
MR. TROTTER: Yes, it's the Air Liquide complaint against Puget Sound Energy regarding which index the Schedule 48 called for.
A. Yes, I believe I provided an affidavit in that proceeding. I don't recall being a witness.
BY MR. TROTTER:
Q. You don't recall --
A. I could be wrong.
Q. You don't recall filing direct testimony in that case dated March 24th of 1999?
A. I don't recall it, but I could be wrong. If you have it there, I'm sure I am wrong.
Q. Okay. I would like to quote you from the brief that the Company filed in that case, and this is from the brief in that docket dated June 8, 1999, and it indicates on page 18, line 3:

> That Complainants always have the right to seek Commission intervention if an inappropriate index is selected.

Would you accept that that's the correct quote?
A. Yes, there's a -- well, I will accept that it's a correct quote, yes, and there is a provision in the tariff that allows index substitution on mutual agreement.
Q. In addition to a complaint then?
A. Mm-hm.
Q. And would you accept subject to your check that the Commission's order in that case, the Commission's supplemental order on page 17 says:

> If the tariff is violated or becomes untenable, the customer's only recourse is to bring a complaint to enforce it or to ask us for relief from the tariff as PSE's own brief suggests.

A. I would accept that subject to check, yes.
Q. I would also like you to accept, subject to check, in the Company's opening brief in that case on page 56, the Company said:

> First, the tariff itself explicitly anticipates a reliable, credible index. The Mid-Columbia Non-firm electricity

Index's failure to meet that criteria makes it inappropriate to apply under

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the terms of the tariff.

Do you understand that that was Puget's position in that docket?

A. Yes, I think I pointed this out earlier, that it was one of the warnings that the Company gave the customers when they were insisting on using the non-firm index once Dow Jones had done the bifurcation of the indexes. But nonetheless, you know, the customers insisted on using that non-firm index, and ultimately the Commission agreed that that should be done.

Q. And did the Commission do that, in your understanding, because it was -- because the issue was whether the index was credible and reliable or because that's the index that was called for under their interpretation of the tariff as written?

A. I can't --

Q. And that --

A. -- be inside the Commission's minds. I don't know all the reasons that they might have done that.

Q. Based on your review of the order in that file.

A. I don't have it currently in my mind.

Q. Another thing Puget said, that same page of its brief, second, and I'm going to ignore citations to the record in that case just for ease of reference:

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Second, the customers themselves have cautioned against adopting an index that is subject to manipulation. If PSE were to purchase the entire Schedule 48 load at the Mid-Columbia Non-firm electricity Index, then PSE would control the index by virtue of the fact that it would control on average more than half the volume of the transactions reported.

Do you recall that as being one of Puget's positions in that docket also?

A. I recall that being an issue in the case, yes.

Q. And do you recall that Puget's witness, a Puget sponsored witness, Mr. Niman, N-I-M-A-N, testified to that effect?

A. I will accept that, yes.

Q. Has anything changed with respect to the Mid-C Non-firm Index since June of '99 that causes you to change the position that Puget took in that case?

A. No.

Q. Does Puget plan to serve its Schedule 48 loads at the lowest cost possible?

A. When Puget is making its dispatch decisions day by day or hour by hour, it follows the principal of

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economic dispatch, yes.

Q. Now there has been some discussion about

Mr. Schoenbeck's Exhibit 605, a comparison of PSE loads and resources. Do you have that; can you get that in front of you?
A. That's the resource bar graph?
Q. Yes.
A. Yes, I have that.
Q. Just turning to the second page of the exhibit, this is an exhibit prepared by Puget; is that right?
A. This is some illustrative information that we provided to the Commission's staff in an early data request before this proceeding actually began.
Q. Okay. And is the chart, such as the one on page two, is that typically prepared by Puget or not?
A. Yes.
Q. Are the two solid lines on that chart typically prepared by Puget?
A. Yes.
Q. And am I correct that the difference between those two solid lines, one with a triangle and one with a square, represent the Schedule 48 and Special Contract load?
A. Yes.

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Q. And this shows, does it not, that at least according to this chart and the assumptions on it, that in every month of the year 2001 under average water, those loads would be served by existing PSE resources?
A. Okay, we're on the average water version?
Q. Yes.
A. No, it doesn't really show that. What it shows is that there are some months, January, February, March, and December, where the Puget resources that would be available to serve the load are higher in cost than market, at least in this particular example. And so in that example, then rather than running the resources, the Company would be buying in the market to serve these loads.
Q. So if the CT's were "in the money", they would be used to serve these loads?
A. Yes.
Q. You mentioned today that FERC has imposed requirements on Puget to send power to California; do you recall that?
A. Yes, actually the Department of Energy.
Q. Okay. And must Puget send power to California before it provides any service to Schedule 48 or Special Contract customers?
A. The standard for service to the 48 customers

1530

and Special Contracts is laid out in the tariffs, and it basically is the availability of power in the daily spot market.
Q. Let me ask it this way. With reference to the type of analysis shown on page two of Exhibit 605, based on whatever the requirement is from the Department of Energy, would this chart more properly be depicted by

shifting the lines up and having underneath those lines placed energy or whatever you are selling to California?

A. I'm not sure how best to depict that on this graph, because the Department of Energy orders require sales to California of power in excess of retail load needs, whereas the 48 quality of service is based on availability of power in the market. So assuming that there's power available in the market, it's a fairly easy answer that it would be only power that's surplus to the total load of the Company that would be sold.

Q. You did use the word retail loads in your direct testimony. Did you intend to include or exclude Schedule 48 and Special Contracts from that terminology?

A. I don't remember exactly the context that I might have used it in.

Q. In what context would you characterize Schedule 48 and Special Contract loads as retail loads?

A. Well, I think they are retail loads.

1531

Q. One context in which you used it, I believe, you said that you do make discretionary wholesale transactions with resources surplused to retail loads. First of all, do you do that?

A. Yes.

Q. And in that context, do you consider Schedule 48 and Special Contract to be included in the term retail loads in that context?

A. Yes.

Q. In your direct testimony, you gave some scenarios under which the Company might make money in one month and not another. I think the month you would make the money, the assumption was you had lots of hydro available and temperatures were warm. And then in the other month, you had low hydro and temperatures were very cold. Do you recall that?

A. Yes.

Q. But on average, you recover your costs. Would that --

A. Well, assuming that the rates are set in a way that allows the Company to recover their cost and there's not regulatory lag and all of those things.

Q. So in the month that you did not "make money", you would not be fully recovering your prudently incurred wholesale power costs that month?

1532

A. I'm not sure that that's true. You know, there are a number of elements of power costs, fixed costs, variable costs, purchases, owned resources. And so, you know, whether or not the Company is recovering all of those costs in a particular period requires an examination of all of those things, not just its wholesale market transactions.

Q. Let me ask it in a different way. Let's assume that you have just had a rate case and your rates have been set. Do you have that assumption in mind?

A. Yes.

Q. And Puget's rates in that scenario are

typically made based on average water, correct?
A. Yes.
Q. And let's assume one month later, hydro diverges from normal and becomes less available than it was otherwise, and your wholesale power costs go up accordingly. Do you have that assumption in mind?
A. Yes.
Q. And assume that your wholesale power costs are higher than what was reflected in the rate case analysis.
A. Yes.
Q. Do you have that assumption in mind?
A. Yes.
1533
Q. How do you recover that increased wholesale power cost that you incurred one month later?
A. You don't.
Q. Is that --
A. You hope that it normalizes out over a period of time.
Q. And it's fair when it does that, and if it's not fair, you file for new rates; is that right?
A. Generally under normalized rate making, yes.
Q. Some of the customers that testified provided exhibits, and Exhibit 101 from the City of Anacortes is one of them, in which Puget made price estimates to the customer showing benefits of Schedule 48 over their preexisting schedule. Are you familiar with those presentations and that data generally?
A. I looked at them quickly, yes.
Q. Would it be fair to say that Puget did not anticipate the extreme spikes at the Mid-C that occurred late and mid 2000?
A. Oh, I don't think that at the inception of Schedule 48 the Company anticipated those spikes, no. I think that the information that are provided to the customers was for illustrative purposes.
MR. TROTTER: Let's go off the record for a moment.
1534
(Discussion off the record.)
BY MR. TROTTER:
Q. Do you have that exhibit?
A. These are the indicative pricing letters to the customers that we looked at earlier?
Q. Yes.
A. Yes.
Q. And just using the first page as an example, it says in the second sentence PSE has agreed to periodically provide to the customer:

> Indicative power market pricing so that BCS in this case can determine whether, when, and for what duration it may wish to hedge its electric supply costs.

Do you see that?
A. Yes.
Q. And it refers to the attached prices as

indicative of prices at which BCS could fix its supply costs and so on. Do you see that?
A. Yes.
Q. And just going to the third page of that exhibit, is it correct that the power price indications currently for the time period shown here are significantly higher than are shown here?
A. Yes, that's right.

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JUDGE MOSS: I didn't quite --
A. It tells me that they should have hedged back in October.
JUDGE MOSS: I'm not sure I quite got the question, Mr. Trotter. Was your question that the actual prices that have been experienced during time periods reflected here prospectively that are now historic, is that --
MR. TROTTER: Yes.
JUDGE MOSS: Okay, thank you.
BY MR. TROTTER:
Q. Is the non-firm market at the -- energy market at the Mid-C more thinly traded than it was in 1998 compared to today, or is it less thinly traded than it was at that time?
A. I'm trying to remember now when Dow Jones bifurcated the firm and non-firm indexes, because, of course, prior to that time there was not a separate non-firm index.
Q. I believe wasn't that the issue in UE-981410?
A. It was, and I'm just trying to remember the time frame for that.
Q. So do you have an opinion as to whether it's more or less thinly traded today than it was during the context of that case?

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A. Not really, no.
Q. You testified about a buy-sell tariff that the Company has just filed, correct?
A. Yes, Schedule 448.
Q. And that is going to be subject to Commission approval obviously?
A. Yes.
Q. If buy-sell is viewed by the Company as I think you said the economic equivalent to open access, why did it not propose that tariff earlier?
A. There are a number of legal and regulatory issues that the Company has been concerned about in offering open access or even in offering buy-sell service, and I don't know that I'm able to review them all in detail right now. But it's only been in the last few months that the Company has reasoned its way through a number of those and conceived of this Schedule 448 structure which it believes it can offer now to the customers.
Q. You referred to actions you took due to the existence of Schedule 48 and the Special Contracts, and I think you referred to one aspect of that as attrition,

meaning that some resources were not renewed and so forth.
A. Yes.
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Q. Some firm resources?
A. Yes.
Q. Do you include the sale of Centralia as an aspect of attrition?
A. I do, although the sale was not done for that purpose specifically.
Q. Do you consider the proposed sale of Colstrip as attrition in that context?
A. It would have fallen into that category had it been done.
Q. Do you consider Schedule 48 and Special Contract modes to be discretionary modes to Puget?
A. Discretionary as to service?
Q. Yes.
A. No, the service standard is set out in the tariff.
Q. Referring back to Exhibit 605 just for illustrative purposes, would not it have been the lowest risk to Puget to make a decision to market on the open market the load represented by the area between the solid lines on that exhibit and simply buy at the Mid-C the power to serve Schedule 48 and Special Contracts?
A. Yes, that would probably be low risk.
Q. And why was that not done?
A. We have tended to view sales to the Schedule
1538
48/Special Contract customers as essentially economically equivalent to sales into the wholesale spot market since the pricing is the same.
Q. If the pricing is the same, why didn't you take the lower risk option?
A. It's only lower risk to the extent that there's an upset of Schedule 48. I mean under Schedule 48 as it's been implemented historically, there's no risk that the Company will receive anything other than the Mid-C Index price from the Schedule 48 customers. It's only if somehow that pricing is upset that there's a risk introduced.
Q. I guess my question is, if the lowest risk to the Company would be to simply buy the power at Mid-C and then market and get whatever the market would bear for that 300 megawatt load served by the resources shown on Exhibit 605, why wouldn't it anxiously do that?
A. Oh, okay, I misunderstood your first question. Under Schedule 48 and the Special Contracts as they are presently implemented, economically it's the same for the customer to sell -- for the Company to sell to those loads or to sell to the spot market, the pricing is the same. The risk element gets introduced if somebody decides to change the pricing in Schedule 48, to somehow look back at the Company's costs, as has
1539
been advocated in this case. And so it would be lower

risk to the Company in that circumstance to actually create costs that are exactly equal to the Mid-Columbia price by entering into a purchase at that price.
Q. Is Puget currently serving Schedule 48 and Special Contract customers at the lowest possible cost?
A. Well, I believe so. As I indicated earlier, we always follow the principles of economic dispatch when we're running our resources.
Q. And has that been consistently less than the Mid-C Index in the last year?
A. No, not necessarily, because oftentimes the Company is purchasing in the market to serve the Schedule 48 and Special Contracts loads, and, you know, there are periods when its purchases are at prices that are higher than the index.
Q. And how often has that occurred in the last year?
A. I would have to go back and review the data. But keep in mind the index is an average of a range of prices, and the Company may not always be able to purchase at that average price or below it. And so I would have to go back and review the 3 million data points and determine how frequently that occurred.
Q. On average, has Puget served these loads at
1540
lower than the Mid-C Index?
A. Probably so on average, again looking just at the incremental costs of operation, short-term power purchase.
Q. You talked about risks of operation and unplanned outages such as at Colstrip; do you recall that?
A. Yes.
Q. In traditional rate making, would normal planned outages be taken into account in setting rates?
A. Taken into account in a normalized way, yes.
Q. And if the Company is able to operate its plants more efficiently than it has done in a normalized test year, it gets the benefit of that efficiency?
A. Yes.
Q. And is that a normal risk that the Company bears?
A. Yes, with respect to its embedded price loads.
Q. The same is true of average water versus critical water, you take the normal risk of variations in weather and water?
A. Absent the ability to come in for emergency rate relief should it become necessary.
Q. Have you ever participated in an emergency
1541
rate relief proceeding in which Puget Sound Energy or its predecessor were a party as the person seeking relief?
A. No, I haven't.
Q. Do you understand that in those cases, the Company does not produce rate case quality evidence in

order to obtain relief?
A. I just don't recall a proceeding like that.
Q. Is it true that Puget attempts to match its variable priced load with variable cost resources and likewise match its fixed cost load with fixed cost resources?
A. Generally, yes.
Q. And would Schedule 48 and Special Contracts be considered variable load, variable price load in that context?
A. Yes.
Q. You talked about converting variable cost resources into fixed cost resources as a strategy the Company undertakes from time to time?
A. Yes.
Q. And every day, you know how much variable cost resources you have converted to fixed cost resources, correct?
A. Yes.

Q. And so by definition, you know how much you did not convert; is that correct?
A. Yes.
Q. Is it fair to assume that the unconverted quantity is serving Schedule 48 and Special Contract load?
A. That's generally the way we think about it, yes.
Q. And likewise, is it fair each day you can measure how much variable cost resource you dispatch, correct?
A. Yes.
Q. Is it fair to assume that those resources are used in whole or in part to serve Special Contract and Schedule 48 load?
A. Generally.
Q. With respect to the Company's recent filing of Schedule 448, does Puget currently anticipate that all the customers under Schedule 48 and the Special Contracts will convert to that schedule?
A. Well, we hope so.
Q. My question is, do you have any indication that they all will?
A. Not right now, no.
Q. Do you have a sense as to the number that

will?
A. No, I haven't been working with the customers directly on this, so my information is at least third hand.
MR. TROTTER: That's all I have, thank you.
JUDGE MOSS: Thank you, Mr. Trotter.
Before we turn to you, Mr. Van Cleve, I have one question for the witness.

E X A M I N A T I O N

BY JUDGE MOSS:

Q. I want to get an exhibit clear in my mind before we move on. And, Mr. Gaines, you may or may not be able to help me with this. I think in terms of your general knowledge and experience, you will be able to even though you testified that you weren't personally familiar with Exhibit 101 and that you didn't create it. That's back at the beginning, it was one of Mr. Maxwell's exhibits.

I just wanted to know if you could briefly explain to me the relationship, if any, the mathematical relationship among the left most columns there, the kilowatt hour, actual demand, KVA, historic, kilowatt, could you tell me how I could relate those various figures mathematically?

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A. I think so. The first column is a kilowatt hour figure, and that would be the total consumption for that load for the period shown, and these are monthly periods. And so you could get an average monthly consumption by dividing that number by the number of hours in the month, get an average figure.

The next column, actual demand, is the highest recorded demand, probably the highest hourly demand for that load in that particular month, and it's in KVA, which is real and reactive power. And then the historic is analogous to that column we just mentioned measured in kilowatts instead.

E X A M I N A T I O N

BY CHAIRWOMAN SHOWALTER:

Q. Is that an average?

A. No, that would be, I think, an instantaneous hourly number. That's probably the highest hourly peak load that has occurred for that load.

Q. Historic?

A. Historic, yeah.

JUDGE MOSS: Thanks for clarifying that for me.

Mr. Van Cleve.

MR. VAN CLEVE: Thank you, Your Honor.

1545

C R O S S - E X A M I N A T I O N

BY MR. VAN CLEVE:

Q. Mr. Gaines, if you could refer to Exhibit 617, which is Mr. Schoenbeck's analysis of incremental costs.

A. Okay.

MR. BERMAN: I'm just concerned if we're going to be getting into confidential information or not.

MR. VAN CLEVE: I don't think we will be.

JUDGE MOSS: Okay, well, if the questions call for reference to specific numbers then, Mr. Gaines, I will ask you to hesitate before answering to give me an opportunity to jump in and see what we need to do, if anything, about handling the confidential information.

THE WITNESS: All right.

BY MR. VAN CLEVE:
Q. Mr. Gaines, could you restate what you mentioned earlier were the problems with the analysis performed by Mr. Schoenbeck?
A. I can try. I haven't done a thorough evaluation of this, and I'm not sure I can list all the problems, but I can list some of them. One problem that I noticed is that this is based on a load resource chart that dates back to June 12th of 2000, so it's
1546
significantly out of date. And as we have mentioned here in my testimony, there have been changes in the Company's underlying load resource position since then.
Also, as I understand it, somehow there was an eyeballing done. We looked at some graphical information, and we then turned that into numerical information through some process of eyeballing and some estimates, and that's not a technique that lends itself to great precision.
MR. BERMAN: If I could break in, I noticed that Mr. Gaines used we, and I think that confuses the record quite a bit. He did that during my examination as well.
THE WITNESS: I'm sorry.
JUDGE MOSS: Avoid pronouns, Mr. Gaines.
THE WITNESS: I will attribute all of this to Mr. Schoenbeck since it was his work.
CHAIRWOMAN SHOWALTER: Well, wasn't it really Mr. Lazar's work that Mr. Schoenbeck based his work on?
THE WITNESS: Yes, I guess that's right, so we'll get dual attribution.
A. I am not sure how long a list of defects we want here, but then we proceeded to use a forward price curve dated December 20th, about six months later than the date of the load resources. There's some
1547
inconsistency there. Also the price curve happens to be near the high point for the forward price curve for the Mid-C. We've got that. Then we use a NYMEX gas strip which I don't know what date that was chosen on, and that would be B material, because the power and gas prices tend to move together. But in any event, we used a NYMEX gas strip, I think, which is not necessarily representative of the points where the Company purchases gas for the turbines in question. So those are a few of the things that kind of struck me right off the bat.
BY MR. VAN CLEVE:
Q. Mr. Gaines, have you performed an analysis similar to this using what you believe to be accurate assumptions?
A. No, we haven't.
Q. The first problem that you identified was the fact that the analysis was based on the load resource information contained in Exhibit 605; is that correct?
A. Right.
Q. Can you turn to Exhibit 605.
A. Okay.

Q. Is Exhibit 605 a data response that the Company submitted in this proceeding?

A. It's a response to some data requests that the Staff issued before this proceeding actually began

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and then subsequently was submitted in this proceeding also.

Q. Now you mentioned earlier in your testimony that the top, let me focus on the chart on page two of Exhibit 605, and you mentioned earlier that the top portion of the bars would change as a result of updating market prices for gas and electricity; is that correct?

A. Yes, that's right.

Q. Can you explain how they would change?

A. Yes, it depends on the relative movement of gas prices versus power prices, and the wider that's spread, probably the more of the resource bar would be filled in with hatch marks.

Q. So the total height of the bar, would that be changed by the market prices?

A. No.

Q. Okay. Can you tell me what, still focusing on, well, let's turn to page three so that we're looking at the critical water assumption.

A. (Complies.)

Q. Can you tell me what factors have changed since June of 2000 that would materially impact the Company's load resource balance?

A. Well, I -- yes, I mentioned them earlier, I think, in my direct testimony. The hydro situation

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would be different, the availability of thermal plants and their maintenance outages likely has changed. The Company has been notified by Bonneville that it has obligations to deliver power to them in the first six months of the year. The Company may have continuing obligations to deliver power to California under emergency orders from the Energy Secretary. Those are a few. There are --

Q. Can you think of any others?

A. No, but I'm sure there are plenty of others.

Q. The hydro availability, would it be any lower than what was assumed on page three of Exhibit 605?

A. It's hard to know. It's likely that it would be distributed differently month by month.

Q. You mentioned the availability of thermal resources. Can you explain what has changed in that regard since last June?

A. We have an extended outage, maintenance outage plan for one of the Colstrip plants this spring that I don't think has been reflected in this chart that goes back to June.

Q. And when is that outage expected to begin?

A. I believe it begins in March, but I would have to confirm that.

Q. Which unit is that?

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A. I believe it's unit number three.
Q. And what's the Company's share of that unit?
A. It's 25%, plus the Company purchases power on a contract that's related to the output of the plant.
Q. So what's the total output available to the Company from that unit?
A. 225.
Q. And was that maintenance outage known last June?
A. I don't recall.
Q. The BPA contract that you mentioned that the Company may have to deliver power under, was that contract in place last June?
A. Yes.
Q. The power that the Company may have to deliver to California, can you tell me how much power the Company has delivered under the Secretary of Energy's order so far?
A. No, I can't.
Q. Do you know if it has delivered any?
A. I believe it has.
Q. Do you know when that occurred?
A. Not precisely, no.
Q. Was the power that was delivered surplus to the Company's total retail load?

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A. Yes, at the time.
Q. Would you agree that the information on page three of Exhibit 605 regarding loads may also be out of date?
A. Yes.
Q. Would you agree that the governor's request for a 10% reduction in electricity consumption could result in lower loads during 2001?
A. It could.
Q. Has that been factored into this chart?
A. No, I wouldn't know how to do that.
Q. Do you know whether this chart includes the BPA power that the Company is expected to receive under the residential exchange beginning on October 1st, 2001?
A. It does not, and it should not.
Q. And why is that?
A. Because the benefit of any power that the Company might receive from Bonneville is dedicated to the residential and small farm customers.
Q. Well, isn't the load of residential and small farm customers included in this chart?
A. It is.
Q. And wouldn't the availability of that power free up other resources for other customers?
A. Not really. If you think about it from an

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economic point of view, the value of the low cost power that the Company may receive from Bonneville is already dedicated to the residential and small farm customers and will be provided to them as a credit against their retail power bills. And so while on a physical basis it might increase the size of these bars, on an economic basis, it has nothing to do with the Company's resource economics and finances.

Q. Doesn't the BPA record of decision on the residential exchange power require that that physical power be delivered to the residential and small farm customers?

A. No.

Q. If the Company receives power from BPA under that program, does it intend to deliver it to anyone other than residential and small farm customers?

A. We don't color the megawatts, and so we're not able to track megawatts that we buy somewhere to deliveries that we make somewhere else. But notwithstanding that, there's no obligation to deliver the power to the customers. The obligation is to provide the economic value to the customers.

Q. Mr. Gaines, I'm looking at the BPA administrator's record of decision dated October 4, 2000, related to the residential exchange program

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settlement, and it states that firm power shall be delivered monthly and only to residential load.

A. That's interesting, but it's not too relevant. We've got contracts with Bonneville that talk about what's going to be done with the power and the value, and it doesn't say that.

Q. And is it your position that you're permitted to sell that power in the open market?

A. Sure.

Q. Could you look at page four of Exhibit 605?

A. That's the first of the annual bar graphs?

Q. Right. I was just curious why the relative size of the variable price load was growing over time?

A. There's an assumption here that the new Internet service provider load that has applied to the Company for service will be growing over time and will be served at market.

Q. Is it your position that those customers are not core customers?

A. It's our -- it's been our position that those loads should be served at market.

Q. Would those customers be core customers or non-core customers?

A. I don't know that it's helpful to try and distinguish them that way without some more definition

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of what is meant by core and non-core.

Q. Would the Company plan to serve those customers on a long-term basis?

A. I think the Company has taken the position that its obligation to serve should be commensurate with those customers' commitment to take power.

Q. Another criticism you had of Mr. Schoenbeck's analysis in Exhibit 617 was that it used a NYMEX gas strip price; is that correct?

A. I think that's what I saw on one of the line

headings, yes.
Q. And do you have any sense over the last year what the basis adjustment between the NYMEX price and the SUMAS price has been?
A. It's varied all over the map.
Q. Do you know what it has been on averages?
A. I don't know what it's been on average. I know that in the last several months, the SUMAS price has been several dollars higher.
Q. I believe you mentioned in your previous testimony that one of the problems with the analysis was that it didn't -- it only measured -- it didn't provide any contribution to fixed cost; is that correct?
A. I think I mentioned that, yeah.
Q. Have you looked at Mr. Schoenbeck's proposal,
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which I believe is memorialized in Exhibit 618?
CHAIRWOMAN SHOWALTER: Do you mean that, 618?
JUDGE MOSS: 618 is the direct testimony of Donald W. Schoenbeck, February 26, 1999, in Docket Number UE-981410.
MR. VAN CLEVE: Excuse me, it was Record Requisition Number 5.
JUDGE MOSS: That's Exhibit Number 22.
MR. VAN CLEVE: Thank you, Your Honor.
A. I do have that page here, but I have not looked at it.
BY MR. VAN CLEVE:
Q. Are you aware that Mr. Schoenbeck's proposal includes a 10 mil margin which would provide a contribution to fixed costs?
A. Well, I mean I have seen a lot of proposals in this case. I have seen a proposal that talks about some kind of a soft cap with a 25 mil margin, and I guess I have heard about some kind of a gas based cost based proposal, and I didn't realize that it had a 10 mil contribution to fixed price in it, no, I haven't looked at this sheet before.
Q. If you look at lines 14 and 15 of this sheet, they set out what the proposal is.
A. Okay.
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Q. Do you have any reason to believe that the proposal contained in lines 14 and 15 of Exhibit 22 would not cover the Company's cost of operating its simple cycle combustion turbines?
A. Well, I'm still trying to relate this proposal to Schedule 48. I mean my understanding of Schedule 48 is that it's a market priced tariff. And so then we had some kind of a soft cap proposal that's some kind of a hybrid of the lower of cost or market. And then this one here appears to be one that's just cost. And how any of that relates to Schedule 48, I just don't know.
Q. Mr. Gaines, my question was whether the proposal on lines 14 and 15 would cover the Company's cost of operating its simple cycle combustion turbines?

A. Of operating them? I would have to know on line 15 where the delivery point would be for the natural gas. It says here Canadian border. Does that mean SUMAS? So that would be one question. And I think your question went to operating costs, but did you mean the full costs or what?
Q. Well, why don't you answer both questions.
A. I think it might cover the operating costs. I don't know that it would cover the full costs.
Q. You're not aware of whether $10 a megawatt
1557
hour as a margin would cover the fixed costs of those facilities?
A. I just don't know.
Q. Would you agree that this proposal would be relatively simple to implement?
A. I guess so.
Q. Have you calculated the financial impact of this proposal on PSE?
A. No.
Q. Do you know if anyone at the Company has?
A. No, I don't think so.
Q. Do you know whether the Company's results of operations for the month of December have been finalized?
A. I don't think so.
Q. Do you know when the Company intends to file its December financial reporting package?
A. No, I don't.
Q. You testified earlier that the Schedule 48 customers insisted on buying at index prices; is that correct?
A. Yes.
Q. And when did that occur?
A. At the time the Schedule 48 was implemented.
Q. Were you present when they insisted on it?
1558
A. No.
Q. Are you aware that the industrial customers wanted cost based direct access in 1996?
A. Yes, with cost based applied to the transportation component of their rate, which they ultimately received in Schedule 48 as well.
Q. Wouldn't you agree, Mr. Gaines, that it was PSE that proposed Schedule 48?
A. I'm not sure who proposed it. My understanding is it was jointly developed.
Q. Were you involved in the negotiations with Georgia-Pacific and Bellingham Cold Storage?
A. Yes, some latter ones, yes.
Q. Isn't it true that the index mechanism in Schedule 48 came from those contracts?
A. It may be.
Q. You don't know whether it is or not?
A. How could anyone say where it came from. Someone has proposed a schedule, and my understanding is that the schedule was jointly developed by the Company

and the customers, and it contained an index pricing mechanism. So to say where it came from, I'm not quite sure.

Q. Well, let's be a little more precise here. Do you think that the index pricing component of

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Schedule 48 was jointly developed during the Schedule 48 negotiations?

A. I believe so.

Q. Did the Georgia-Pacific and Bellingham Cold Storage contracts come before Schedule 48?

A. I think they did, the original ones, yes.

Q. You weren't involved in the negotiation of Schedule 48, were you?

A. No.

Q. How about the drafting of Schedule 48, were you involved in that?

A. No.

Q. Is there anyone still employed by PSE who was involved in those negotiations?

A. I don't know that anybody that was a part of the direct negotiating group still is employed by the Company. I'm just not sure.

JUDGE MOSS: Why don't you tell us what you're handing up.

MR. VAN CLEVE: We're handing up DWS-23 and 24 so everybody may have it.

JUDGE MOSS: Do you want to have these marked?

MR. VAN CLEVE: Yes, Your Honor.

JUDGE MOSS: All right, these will be, DWS-23

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will be marked as 1409, and DWS-24 will be marked as 1410.

BY MR. VAN CLEVE:

Q. Mr. Gaines, if you could refer to Exhibit 1409, was this data response prepared under your direction?

A. It was prepared by some people who are on my staff, yes.

Q. And were there some errors in this data response?

A. Yes, I understand that there were.

Q. Can you identify Exhibit 1410?

A. Yes, I think this was a correction to that original data response legend.

JUDGE MOSS: Does that remain confidential, Mr. Van Cleve?

MR. BERMAN: Your Honor, it was designated confidential by PSE, and the reason is that it specifically names some counter parties to transactions, and so I think that those specific names of counter parties are confidential, but if we can avoid discussing those specific names of counter parties, I think there's -- I don't see any problem discussing the exhibit.

JUDGE MOSS: All right, but I need to mark it as 1410-C.

1561

BY MR. VAN CLEVE:

Q. Was the data response to Complainants' Data Request 1.003 with this supplement made accurate?

A. I believe so.

Q. Do you know if there's anything missing from this response?

A. Well, again, this response is a legend or a key, if you will, to the electronic data that we provided on all of the Company's hourly energy transactions in the wholesale market in the year 2000. So the purpose of this was to annotate that electronic data response.

Q. So in other words, the problems with the data that were identified in the original response to 1.03 have been cured by the supplement?

A. Well, the problems were not with the data. The problems were with the original legend, with Exhibit 1409, and so we now have corrected those legend errors in Exhibit 1410-C.

Q. Is the data itself that was provided to the best of your knowledge accurate?

A. Yes.

Q. I would like to ask you a couple of questions about the Company's complaint that it filed at FERC. I noticed in the complaint that it states that all

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correspondence and communications and pleadings related to the complaint should be sent to you. Is that correct?

A. I don't have it in front of me, but I believe that's right, yes.

Q. Does that mean that you're the officer responsible for this proceeding for the Company?

A. Yes.

Q. Do you agree with FERC's conclusion that the wholesale market structure in California is seriously flawed?

A. Well, FERC made a lot of findings in that order, and it found some things in the California market that it thought were flawed and set out to repair those.

Q. Do you believe that FERC should impose a price cap on Northwest wholesale prices?

A. We advocated in the pleading that you're referring to that FERC do that on a temporary interim basis, and we advocated that several months ago.

Q. How do the think the price of the cap should be determined?

A. We didn't talk about that in our pleading. What we suggested was that if FERC determined to put a price cap in place in a particular market, in California for example, that it should be evenhandedly applied

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across all the western markets. We didn't suggest a particular cap level or methodology.

Q. Do you think a price cap in the Northwest is necessary?

A. Well, I think it's necessary, particularly if it's going to be imposed somewhere in the market. We do feel that if there's going to be an imposition of a price cap that it should be done evenhandedly.

Q. Can you explain why you think a price cap in the Northwest is necessary?

A. I didn't say I thought it was.

Q. Well, you asked for it in your filing, didn't you?

A. To the extent that one is imposed in California, yes.

Q. Well, explain why a cap in California necessitates a cap in the Northwest.

A. Oh, because the markets tend to work together, as has been observed a number of times in this case already. One market influences the other one.

Q. So what would be the impact on Northwest markets if a price cap is imposed in California but not in the Northwest?

A. If a price cap -- if an effective price cap were imposed in California, our sales prices to

1564

California would be limited, but our cost of purchasing power might be unlimited.

Q. Does that mean that it would tend to drive prices up in the Northwest?

A. It might.

Q. Do you agree with the comment made by Mr. Lazar on Friday that the Mid-Columbia Indexes represent the market clearing price for a relatively small increment of power?

A. There seems to be quite a bit of confusion about what the indexes represent and don't and what the markets are or aren't, and most of these opinions are coming from people that don't have any practical experience in the markets themselves at all. And what I found is that there are not multiple spot markets, there is one, at any particular point. And what I found is that the Dow Jones Mid-Columbia Indexes do a reasonable job of representing the price levels in that spot market.

JUDGE MOSS: Is this something you want marked, Mr. Van Cleve?

MR. VAN CLEVE: Yes, Your Honor.

JUDGE MOSS: All right, what has been handed out is the direct testimony of William A. Gaines on behalf of Respondent, dated March 24, 1999, in Docket

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Number UE-981410, and I will mark it as number 1411.

BY MR. VAN CLEVE:

Q. Mr. Gaines, Exhibit 1411 is the direct testimony that Mr. Trotter referred to a few minutes ago that you provided in Docket Number UE-981410; is that correct?

A. I thought I had blocked it from my mind successfully until you now returned me to it, but yes.

Q. If you could turn to page three of your

testimony.
A. (Complies.)
Q. On line 16, you state that:
There are serious questions whether the Mid-C Non-firm Index accurately reflects commodity electric prices in the region.
Does that statement continue to be true?
A. Yeah, it's one of the warnings that we provided to the customers in this proceeding.
Q. You also state at the beginning of line 17 that:
On many days, the volume of energy traded at the Mid-C Non-firm Index is only a fraction of the total Schedule 48 volume.
Does that statement continue to be true
1566
today?
A. I think it is. It's what I find ironic about all of this is that we provided these warnings, the customers insisted they wanted to be priced on this index, and now they're coming back with the same complaints themselves.
Q. When did the customers insist that they be on this index?
A. During this earlier proceeding.
Q. Isn't it true that the purpose of this earlier proceeding was to determine whether the Company had a unilateral right to change the index specified in the tariff?
A. You can characterize it any way you like, but what they were trying to do was get on the non-firm index because they thought it would be cheaper.
Q. Isn't it true that the tariff referred to the non-firm index?
A. That was one of the issues in the case, yes.
Q. If you could look at page 4 at lines 13 through 15, you state that -- the question asks -- at line 7 asks about the Company's intent in proposing the index, and you state at line 14 that:
The Company attempted to select those that reflected as closely as possible
1567
the Company's actual cost of buying energy in the market.
Was that a correct statement when you made it?
A. I'm sorry, I was on the wrong page. I think I now have it right, it's page 4?
Q. Page 4, line 14.
A. And the question was, was that our objective?
Q. Was the Company's objective in selecting the non-firm index to reflect as closely as possible the Company's actual cost of buying energy in the market?
A. That was one of the objectives, yes.
Q. And if you could turn to page eight of Exhibit 1411. On lines one and two, you state:

We have serious doubts about whether the Mid-C Non-firm Index accurately reflects the market for commodity electricity in the region. Do you still have serious doubts?

A. This was a warning that we provided to the customers in this earlier case, that the index was thinly traded compared to the other firm index.

Q. And my question is, do you have the same doubts today?

A. I think that this index reflects the

1568

transactions that it's composed of, which are short-term hour-to-hour transactions.

Q. Well, when you say here that you have a doubt whether the index reflects the market for commodity electricity in the region, what market were you referring to?

A. I was referring to the day ahead market. Keep in mind that the way Puget operates, we do most of our short term purchases and sales in the day ahead market, the prescheduled market, if you will, that is done today for tomorrow. And so when they were making these statements, we were talking about the cost that Puget incurs in that day ahead market, which is the market that's reflected in the firm Mid-Columbia Index. Here now we're talking about the non-firm Mid-Columbia Index, which is the hour-to-hour market within a particular day, and we do relatively fewer of our transactions in that market.

MR. VAN CLEVE: Can we also have this exhibit marked, Your Honor.

JUDGE MOSS: What I have been handed is characterized the direct testimony of Stanley R Niman, March 24, 1999, in the UE-981410 proceeding. I will mark it as 1412.

BY MR. VAN CLEVE:

1569

Q. Mr. Gaines, was Stanley Niman an expert witness for the Company in the prior complaint case, the 1410 proceeding?

A. Yes, he was.

Q. If you could turn to page 8 of Mr. Niman's testimony, which has been marked as Exhibit 1412, and I would like you to focus on lines 7 through 14.

A. Yes.

Q. And Mr. Niman is identifying some problems that he sees with the Mid-Columbia Non-firm Index, and the first problem is that, according to Mr. Niman, is that:

It suffers from the lack of liquidity and true price discovery in terms of small reported volumes and small numbers of participants.

Would you agree that this concern remains today?

A. I think he was talking about this relative to the other index, relative to the firm index, but generally.

Q. The second point that Mr. Niman raises is that:

The reported transactions are potentially subject to manipulation by a

1570

large player such as PSE at the Mid-Columbia.

Is that a true statement?

A. Focusing particularly on the word potentially, yes.

Q. The third comment that Mr. Niman makes is that:

The index is an index for which it is difficult to obtain competitive market quotes for fixed and variable price swaps, given the very low volume and resulting illiquidity of the non-firm index.

Is that statement correct?

A. This was actually one of the biggest worries that I had when the customers were insisting in the prior case on this index, because the hedge products are all built off the other index, the firm index. So to the extent that any of the customers wanted to hedge their Schedule 48 service, they would have an imperfect hedge because of the non-firm index. I thought it was fairly short sighted. And again, I think their objective was simply to get an index that they believed would be lower in price at the time by a mil or two.

Q. So your answer was yes?

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A. My answer is a whole answer.

Q. Well, let me ask you again then. Is it difficult to obtain competitive market quotes for fixed and variable price swaps for the non-firm index?

A. Yes.

Q. If you could now refer to page nine of Exhibit 1412, if you could read for the record the first question and answer on the top of page nine.

A. This is from Mr. Niman's testimony. The question is:

How could the index be manipulated?

And the answer is:

The ability of a single participant to manipulate the index may be the most compelling reason that the non-firm index is not an appropriate pricing mechanism. PSE is by far the largest non-federal Mid-Columbia participant in terms of Mid-C generating capacity. This capacity combined with effective Mid-Columbia control area presence gives PSE the capability to easily effect significant changes in reported non-firm transaction prices.

Q. Is there anything inaccurate about

1572

Mr. Niman's statement that you just read?

A. I don't know that there's anything inaccurate here about the potential for that. I have to tell you though that in this proceeding and in the prior one, the insinuation and the implication that there is manipulation by Puget is offensive and ridiculous.

Q. Did you state earlier in your testimony that the Company had about 1400 megawatts under its control at the Mid-Columbia?

A. Yes.

Q. I would like you to look at Exhibit 508, which is the statement from Mr. Davis.

JUDGE MOSS: I lost you momentarily. Where are we?

MR. VAN CLEVE: 508.

A. I have two different pieces of testimony here from Mr. Davis.

BY MR. VAN CLEVE:

Q. It's a three page statement signed by Mr. Davis that has been marked or has been admitted Exhibit 508; do you have that?

A. Yes.

Q. And if you could refer to paragraph 12.

A. Yes.

Q. Mr. Davis sets out a test for what a credible

1573

index is, and my question for you is whether you believe that the Mid-Columbia Non-firm Index satisfies Mr. Davis's test?

A. The non-firm index is not the index that we were advocating for the customers in the prior proceeding, and there's not too much that has changed about that now.

Q. So what's the answer to the question?

A. Mr. Davis has laid out a test here. Whether it's the appropriate test, I'm not sure.

Q. Do you think that the Mid-Columbia Non-firm Index satisfies that test laid out by Mr. Davis?

A. Well, I think it certainly satisfies A, and is it subject to movement, maybe; has it been moved by us, no.

Q. When you say it satisfies A, what market do you think the index reflects?

A. It's primarily the hour ahead market, the so-called real time market that's traded hour to hour within a day.

Q. Can you give us a description of why people enter into that market and what real time transactions are used for?

A. Sure. It's about the shortest term market available, and it's the market the utilities and

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marketers use to balance their real time surpluses from hour to hour. So that if your loads in a day, for example, are different than what you predicted the day before or if your stream flows are higher or lower or you've got a generator outage different than what you planned when you set up your operation the day before, this is the market you would use to balance those things.

Q. I would like to ask you a few questions about hedging. Has the Company ever directly provided optional price stability to Schedule 48 customers?

A. When you say directly, I assume you mean has the Company taken the risk into its own portfolio.

Q. That's correct.

A. No, we haven't.

Q. Are you aware of whether hedging for the Mid-Columbia was available at the time Schedule 48 was created?

A. I believe that it was.

Q. Even before there was a Mid-Columbia Index?

A. No, I think people were hedging off the COB Index at the time, although I think there were people who would sell fixed price power at the Mid-Columbia at that time as well and who could have constructed a hedge had someone asked.

Q. So the hedging that was available was for COB?

A. Generally. That was the market index that evolved first in this area.

Q. Has hedging ever been available for, and let me be more precise, has a fixed or floating price swap ever been available for the Mid-C Non-firm Index?

A. I'm not sure.

MR. VAN CLEVE: I would like to refer now to the Complainants' response to Bench Request D-1, which, I'm sorry, Your Honor, did you give that an exhibit number?

JUDGE MOSS: 28.

MR. VAN CLEVE: 28.

BY MR. VAN CLEVE:

Q. Mr. Gaines, do you have Exhibit 28 in front of you?

A. Yes.

Q. This is an E-mail to Alan Warman, who is in the energy department at Boeing, and as you can see from the bottom of the document, it's from Jason Thackston, who is a wholesale energy marketer from Avista Corporation. And I would like to refer you to the last two full paragraphs of the document where it says that:

Regarding the NYMEX futures contract for

the Mid-Columbia and COB, there has been little activity.

And it also says that:

There is no open interest on the COB contract at this time, and this illiquidity makes hedging very difficult on the NYMEX.

Would you agree that the NYMEX, Mid-Columbia, and COB contracts are illiquid?

A. Well, when we, as I mentioned earlier, we don't use the NYMEX exchange, so I don't have any real current information about the liquidity there. We tend to use the over-the-counter market and the brokers, which is where most of the activity is.

Q. You stated earlier in your testimony that the Mid-Columbia formed the basis for indexes upon which futures prices and swaps and options were based, and I'm trying to understand whether there's a futures market for the Mid-Columbia?

A. There's a very active futures market for the Mid-Columbia, swaps and options both.

Q. But is it your testimony that that market is not on the NYMEX?

A. Right, the exchange traded swaps and options, that market tends to be fairly thin, and most of the

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actual market activity is done on an over-the-counter basis directly with the market makers in these derivative instruments, and it often is done through brokers. A couple of them are mentioned at the end of the first paragraph in this E-mail.

Q. Let me refer you to the last paragraph of the E-mail in the last sentence where it says:

> As a result of illiquidity, options contracts are not a reasonable vehicle for hedging.

Do you think that's true?

A. Absolutely not. I don't know who Alan Thackston is, but he's obviously not plugged into the market very well.

Q. The first sentence of that last paragraph in Exhibit 28 where he says that:

> Volatility in the electricity markets has drastically decreased trading of electricity options over the last ten months.

Is that statement incorrect?

A. I don't know that that's correct or incorrect. I know that we have done a number of options transactions in the last several months for the Company.

Q. Can you describe those for us?

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A. Yes. I mentioned one earlier where we had bought some call options on supply for the November to February period. We have also executed some put options for the third quarter of 2001. We have done call options on gas. We have done a number of things.

Q. Can you describe the call options for the November through February period?

A. Yes, we were trying to supplement our peaking supplies for that winter period, and so we entered into call options to derive purchase power at a given price.

Q. What is the size of the option?

A. Varied month to month, but they were several hundred megawatts each month.

Q. Are those options still in place?
A. Yes.
Q. And what's the price of exercising the option?
MR. BERMAN: If we're going to get into actual pricing of specific transactions, I would ask that we go into confidential session.
JUDGE MOSS: I think that does sound appropriate. Is that what we need to do?
MR. VAN CLEVE: Yes, Your Honor, but maybe we should save that until the end and see if there's any other confidential questions that come up.
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JUDGE MOSS: Let's do that.
BY MR. VAN CLEVE:
Q. Mr. Gaines, if you look at the section on Exhibit 28 right below the table that says notes, do you see that there?
A. Yes.
Q. And the third sentence down that begins with:
Products with volumes below 25 megawatts are not liquid on the OTC market.
Now I'm assuming that OTC refers to over the counter. Do you agree with that statement?
A. I agree with it except for the 10% number. I think the 10% is probably a guess, and whether it's right or not, I have no idea.
COMMISSIONER HEMSTAD: In view of the reference to the 10%, perhaps you should read into the record that second sentence so we know what it refers to.
MR. VAN CLEVE: Let me read the whole thing.
Products with volumes below 25 megawatts are not liquid on the OTC market. Historical indications suggest a purchaser may pay as much as 10% above quoted prices for odd lot volumes.
BY MR. VAN CLEVE:
1580
Q. Mr. Gaines, I would like you to take a look at the exhibits that were associated with your direct testimony, and the first exhibit that I would like you to look at is one that wasn't admitted, and it's marked as PSE-74. I think it's Exhibit 1404.
A. Yes.
Q. Can you explain what this document is?
A. This is a snapshot of the forward price curve that we took from our own forward price marks as of the date that's shown, January the 3rd of 2001.
Q. Now one of your criticisms of the analyses performed by Mr. Lazar and Mr. Schoenbeck was that they were based on an outdated forward price curve. Is this forward price curve more accurate?
A. Well, it's more recent, but as we have learned through this proceeding, the forward prices are moving around quite a lot.
Q. Well, in that regard, I would like to ask you

to take a look at Exhibit 1408, and if you can turn to
what's marked at the bottom as page 27 of Exhibit 1408.
     A.   Okay.
     Q.   Is this the Company's November 1st, 2000,
forward price curve?
     A.   Yes.
     Q.   And on that day if you wanted to purchase a
1581
flat product for the month of January 2001, it indicates
that the price would be 82.14 mils; is that correct?
     A.   I have 82.65, but okay.
     Q.   For November 1st?
     A.   Yeah.
     Q.   Oh, that's the cumulative.
     A.   Oh, for the month?
     Q.   For the month, yeah.
     A.   Pardon me, 82.14, you're right.
     Q.   And now if you could look at page 51 of that
exhibit, I'm sorry, yes, page 51, and is that the
December 6, 2000 forward price curve?
     A.   Yes.
     Q.   And the price on that day for the same flat
January product was 613.57 mils; is that correct?
     A.   Yes, it makes the earlier number look pretty
good.
     Q.   So in the course of a little over a month,
the price went from $83 a megawatt hour to $613 a
megawatt hour for the same time period; is that correct?
     A.   The forward market price, yes.
     Q.   Right.
     A.   Not necessarily the spot price that the
customers would pay, but the forward market price did.
     Q.   Would you agree that that is an extraordinary
1582
level of volatility in the power market?
     A.   Very large move, yes.
     Q.   In all of your years of experience in the
power industry, have you ever seen volatility
approaching that?
     A.   No.
     Q.   Do you think that this level of volatility
has an impact on the price and availability of hedges?
     A.   It has a -- it has an impact on the
availability and price of options, because volatility is
an explicit element in options pricing.
     Q.   I believe that on the first day of this
hearing, Mayor Maxwell from the City of Anacortes
testified that employees of the Company had advised him
not to buy a hedge because it was too expensive. Are
you aware of employees of the Company having
conversations like that with customers?
     A.   It would surprise me very much if any of the
employees of the Company had done that. The Company is
not in the business of giving advice about particular
levels of price in hedging.
     Q.   Would you agree that the market for hedging
gas is more liquid than for electricity?

A.   Generally that's true, particularly at the big national trading hub in Louisiana. It's less true
1583
in the local markets out here.
Q.   You testified regarding what the "deal" was in the rate plan, and I would like to ask you a couple of questions about that. I believe it is attached as Appendix A to Exhibit 1563.
Mr. Gaines, I believe that you testified that the Company bears the risk of the cost of serving its fixed price loads under the rate plan; is that correct?
A.   Yes.
Q.   If you could look on page ten of the stipulation, which is Exhibit 1563, and referring to section six, which is entitled interim rate relief, my question is, isn't it true under the interim rate relief provision that if the Company was unable to pay its debts as a result of load growth or an increase in its costs that it could seek rate relief under the rate plan?
A.   I think I'm in the wrong place. You said page ten?
CHAIRWOMAN SHOWALTER: I think the issue is there is a stipulation attached to the order.
THE WITNESS: Oh, I'm sorry.
CHAIRWOMAN SHOWALTER: There is an attachment.
MR. VAN CLEVE: Appendix A to the merger
1584
order.
COMMISSIONER HEMSTAD: What page of the exhibit?
CHAIRWOMAN SHOWALTER: Page 61.
JUDGE MOSS: What page of the exhibit is it?
CHAIRWOMAN SHOWALTER: Page 61. Is everybody on the same page, okay.
THE WITNESS: I have it now, thank you.
BY MR. VAN CLEVE:
Q.   You're there, the interim rate relief provision?
A.   Yes.
Q.   And I guess to restate my question, does this provision allow the Company to obtain rate relief if it's in financial distress?
A.   I'm not familiar with exactly what the PNB standard is, but generally yes.
Q.   So when you stated that the Company bore the risk of serving its fixed price loads --
A.   Subject to this.
Q.   -- that was subject to obtaining rate relief if it became distressed?
A.   That's right.
Q.   And on the next page beginning at line three, it explains the process for seeking interim rate relief.
1585
Do you see that?
A.   Yes.

Q. And down at line seven, it says that:
PSE would propose to spread the requested interim rate relief among customer classes based on an equal percentage of margin and on an equal percentage of revenues.
Do you see that?
A. Yes.
Q. And do you think that the customer classes referred to there in line eight includes the Schedule 48 and Special Contract customers?
A. I really haven't thought about it.
Q. You don't have an opinion on that issue?
A. I really don't.
Q. You don't know what the intent of this provision was?
A. Not with respect to that, no.
Q. If you could look at the provision entitled storm damage on page 59 of Exhibit 1563. Do you have that?
A. Yes.
Q. Do you see where it says in the second sentence that:

1586

Current policy authorizing deferral of extraordinary property losses related to storms will continue.
A. Yes.
Q. Does that mean that the Company can defer extraordinary storm damage cost despite the rate freeze?
A. If they exceed a certain level, and I'm not sure exactly whether they're deferred beyond the rate freeze period or not.
Q. Well, let's assume for the sake of argument that those deferred amounts can be recovered after the rate plan. Can you explain why extraordinary storm damages are treated differently?
A. Than what?
Q. Than the other costs the Company might incur during the rate plan.
A. No, I really can't. I think it's an artifact of historical regulation of the Company.
Q. Do you know why the Company doesn't just obtain insurance for extraordinary storm damage?
A. No, I don't. I don't know that it's available.
Q. Is it fair to say that the Company didn't take the risk of extraordinary storm damages in the rate plan?

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A. Over some threshold.
Q. Do you think the Schedule 48 and Special Contract customers assumed the risk of a fundamentally flawed wholesale power market?
A. Yes.
Q. Did you say in the beginning of your testimony that you were responsible for the Company's

gas procurement?
A. Yes, I am.
Q. Did the Company recently seek a rate increase for its retail gas rates?
A. Yes, under its purchase gas adjustment rates.
Q. And was that request granted?
A. Yes, it was.
Q. And did the Company incur significantly higher gas costs in the month of December than it anticipated?
A. The index prices for gas were higher than anticipated, yes.
Q. And did the Company hedge its gas supply risk for the month of December?
A. Not for the core gas operation, no.
Q. One last area on this question of the risk that the Company assumed in the rate plan. Do you think the Company assumed the risk in the rate plan of low
1588
growth among the core customer class?
A. Generally.
Q. Can you explain why that risk doesn't include the data center customers?
A. It was load that was not anticipated, a class of load that was not anticipated.
Q. So you think it's okay for the Company to be relieved of the risk it assumed if the risk turns out to be something that was unanticipated?
A. There are risks associated with that load, primarily that it might not really be a load, but rather that it might go away. That could cause the Company to incur costs including capital costs that would burdon future rate payers. The Company would prefer not to do that.
Q. Is it the Company's position that those customers can't take service under Schedule 49 or Schedule 31?
A. I'm not involved in that. I can't tell you.
Q. Mr. Gaines, if you could look at Exhibit 601. Do you have Exhibit 601, Mr. Gaines?
A. Yes, I do, thank you.
Q. Is this a list of the current Schedule 48 customers?
A. That's what it says. I'm not personally
1589
familiar with each of the customers.
MR. VAN CLEVE: Your Honor, does this exhibit remain confidential?
JUDGE MOSS: Perhaps we need to clarify. I have the front page marked as confidentiality waived, but now I just noticed that it's stamped on the second page as part of the protective order, so I'm not sure.
MR. BERMAN: We have indicated several times on the record that we waive confidentiality on Exhibit 601.
JUDGE MOSS: Well, I'm trying my best to remember these things, but there are limits to human

endeavor. It's not confidential then.
BY MR. VAN CLEVE:
Q.   Mr. Gaines, I am informed by Mr. Schoenbeck that the on-peak price for the non-firm index on the 17th of November in the year 2000 was $250 per megawatt hour, and I just wonder whether you could explain why a Company like Qwest would sign up for Schedule 48 at those kind of prices?
A.   I have no idea who this customer is or why they would sign up.
Q.   Can you tell us what tariffs the Company has that are generally available for large industrial customers?
1590
A.   I'm not an expert on this, but generally I believe it's tariffs 46, 48, and 49.
Q.   And is Schedule 49 available for any new customer except a data center?
A.   I'm not familiar with what's available or not for data centers.
Q.   Is it available for other new large customers?
A.   So far as I know.
Q.   I wanted to ask you a little bit about the diesel generators that you talked about earlier, and the first question has to do with the generators that the Company is operating on diesel. Can you describe that in a little more detail?
A.   Yes, they're the combustion turbine generators that the Company has had in place since the early 1980's.
Q.   And those are simple cycle facilities?
A.   They are.
Q.   And are all of those facilities capable of running on diesel?
A.   Yes.
Q.   And when did the Company -- when has the Company in the past year run those facilities on diesel?
A.   I believe that we began that kind of an operation early in December of last year.
1591
Q.   And what was the reason that you began to run those facilities on diesel?
A.   It was economics. It was because the per btu price of diesel was lower than that of natural gas.
Q.   And was December the first time in the year that it became more economic to run on diesel compared to natural gas?
A.   At least on a continuous basis. We may have run some on diesel earlier in the year 2000 for peaking purposes. I just don't recall.
Q.   You mentioned a diesel price of I think it was 85 to 90 cents; is that correct?
A.   Per gallon, yes.
Q.   Can you tell me what the incremental operating cost of one of the combustion turbines is assuming that price for diesel?

A. I would have to go do some math to be precise about it.
Q. Can you give me a rough estimate?
A. I will give you a very rough estimate. I would guess it's in the neighborhood of 100 to 150 mils per kilowatt hour, just the fuel portion.
CHAIRWOMAN SHOWALTER: Did you say 150 what?
THE WITNESS: Between 100 and 150 mils per

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kilowatt hour.
BY MR. VAN CLEVE:
Q. Can you tell me how you would calculate that?
A. I would multiply the heat content of a gallon of diesel oil times the heat rate of the combustion turbine unit and the price.
Q. And what's the average heat rate for the Company's simple cycle combustion turbines?
A. They vary a little bit depending on which fuel you're using, but generally in the range of 12,000 to 13,000 btu per kilowatt hour.
Q. And what's the peak capacity of the Company's simple cycle combustion turbines?
A. Added together, it's approximately 550 megawatts.
Q. You referred to I believe it's called selective catalytic reduction.
A. Yes.
Q. Can you tell us what that is?
A. Its a technology that's used for reducing nitrous oxide emissions from power plants and other things.
Q. There's been quite a bit of testimony in this proceeding about temporary diesel generators. Do you know what the capacity of a temporary diesel generator

1593

is?
A. I think generally they're fairly small, in the range of say less than two megawatts.
Q. Do you know how the process works for a selective catalytic reduction device?
A. Not in great detail, but generally the exhaust stream from the machine is passed across the catalyst, which removes the emissions.
Q. Now you testified earlier that it was like a catalytic converter on a car.
A. That's my understanding generally.
Q. Have you ever seen one of these devices?
A. Not for a small portable generator, no.
Q. Do you know who makes them?
A. Caterpillar, among others.
JUDGE MOSS: Mr. Van Cleve, how much more do you have?
MR. VAN CLEVE: Maybe 20 minutes.
JUDGE MOSS: I think we need to take a break. Let's break until a quarter before the hour.
(Brief recess.)
BY MR. VAN CLEVE:

Q. Mr. Gaines, is the Company's position that the Complainants have given up any claim that they may have to a share of the generating assets of PSE?
1594
A. Yes.
Q. Can you refer to Exhibit 504?
A. Yes.
Q. Mr. Canon previously testified that this was one of the clarification letters that the Company sent to the Commission during the approval process for Schedule 48. If you can turn to page four of Exhibit 504.
A. Okay.
Q. Would you agree that the two lines at the top of page four provide that the Schedule 48 customers could pay a, quote, appropriate surcharge and return to the core class?
A. Yes.
Q. Do you think that the option of returning to the core class was included because Schedule 48 or open access might not work out?
A. It could be.
MR. VAN CLEVE: Can I have this document marked, Your Honor.
JUDGE MOSS: All right, what's been handed out as original sheet number 104, Schedule 104, Puget Sound Energy, and it will be marked as 1413.
BY MR. VAN CLEVE:
Q. Were you a witness in the proceeding related
1595
to the sale of Centralia?
A. Yes.
Q. Does Exhibit 1413 indicate that the Schedule 48 customers, the high voltage Schedule 48 customers, were given the same share of the Centralia gain as Schedule 49 customers?
A. It looks that way, yes.
Q. Can you explain how this is consistent with your position that the Complainants have given up any claim to a share of the generating assets of PSE?
A. No, I have no idea how the two are related, if at all.
Q. Do you know whether customers that purchase under Schedule 49 are required to sign a service agreement?
A. I don't know.
Q. I would like to ask you a couple of questions about the buy-sell tariff, Schedule 448. Are you aware of any retail buy-sell tariffs that have been implemented in the WSCC?
A. I can't think of any that I'm aware of, no.
Q. Was it the Company's position prior to this Fall that a buy-sell arrangement was prohibited by law?
A. We had concerns about our ability to implement a buy-sell tariff consistent with law and
1596
consistent with regulation at the state and federal

level.
Q. Was the Company asked by Georgia-Pacific last summer to provide a buy-sell type arrangement?
A. We had had requests like that from Georgia-Pacific, yes.
Q. And did the Company refuse to provide such service?
A. Company indicated to Georgia-Pacific the issues that it had with that construct and offered Georgia-Pacific alternatives which we believed were economically equivalent.
Q. Would you agree that Schedule 448 is not an acceptable alternative for the Schedule 48 and Special Contract customers if it's not acceptable to sellers in the marketplace?
A. Are you suggesting that it's not acceptable to any seller in the marketplace?
Q. Yes.
A. If that were the case, it probably wouldn't be very workable. I don't know that to be the case though.
Q. Do you know that it is acceptable to sellers in the marketplace?
A. We have talked to some marketing companies

1597

about it, and they have raised no objection that I'm aware of.
Q. Which ones have you talked to?
A. We have talked to PG&E, we have talked to Morgan Stanley, that I'm aware of, probably others.
Q. And those two companies said that they would be willing to provide service to retail customers under a buy-sell arrangement?
A. We described generally the concepts behind the tariff, and they didn't indicate any problem with it.
Q. Did you solicit comments from potential sellers before you filed Schedule 448?
A. I don't know that we did.
Q. Is it the Company's position that Schedule 48 should be extended beyond its current expiration date?
CHAIRWOMAN SHOWALTER: What expiration date do you mean?
Q. I believe it expires at the end of the year.
A. I think that the Company's preference would be to design a buy-sell tariff that would be acceptable to the customers and use that going forward.
Q. Has the Company attempted to determine what an appropriate surcharge would be as that's used in the letter that's marked as Exhibit 504 on page four?

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A. No, I don't believe so.
Q. Why not?
A. Haven't needed to.
Q. Would the Company be willing to do that if Schedule 48 customers wanted to return to core service?
A. Yes. I think we might find that economically

it's the same thing as going to market, but we could determine that, yes.
Q. I think before the break we were exploring selective catalytic reduction technology. Do you recall that?
A. Yes.
Q. And you referred to Caterpillar as being a manufacturer of that equipment?
A. Yes, so I'm told.
Q. And do you believe that that equipment is at this time readily available from Caterpillar for temporary diesel generators?
A. I don't know that it's available from Caterpillar today. I'm told it's available from a number of manufacturers, and Caterpillar was mentioned as one.
Q. Are you aware of whether selective catalytic reduction technology for temporary diesel generators is readily available from any manufacturer currently?
1599
A. I am told that it is.
Q. Who told you that?
A. We put together a team of people inside the Company for the purpose of aiding the industrials in setting up their temporary generation installations, and one of the members of that internal team was providing me some information about that.
Q. And what information did that person provide you?
A. Generally that this technology was available for small diesel generation.
Q. And is the technology that's available, can it be retrofited on existing diesel generators?
A. I'm not sure about that. I suppose it probably depends on the manufacturer.
Q. Do you know what the cost of this equipment is?
A. No.
Q. Do you know how long it would take to get this kind of equipment?
A. No, although I suppose someone could have ordered the machines with the equipment on it in the first place.
Q. If the Schedule 48 and Special Contract customers self generate, do they contribute anything to
1600
the fixed costs of the company's distribution and transmission system?
A. No, not under the current tariff, assuming that the generation operates continuously anyway.
MR. VAN CLEVE: Your Honor, I think all I have left is the one confidential area that we identified earlier.
JUDGE MOSS: All right. Anybody who is not a signatory to the appropriate certificate under the protective order in this proceeding for the review of confidential information, I will have to ask you to

leave the room, and we will be off the record momentarily while I turn the teleconference bridge off.

(Discussion off the record.)

(The following testimony designated confidential.)

CONFIDENTIAL SESSION CONCLUDED

(Discussion off the record.)

JUDGE MOSS: Mr. Berman.

MR. VAN CLEVE: Your Honor, before we get to Mr. Berman, I did intend to offer 1404, 1409, through 1412.

JUDGE MOSS: Any objection?

(Discussion on the Bench.)

JUDGE MOSS: I have lost track of the order here, but the first matter of business I need to take care of is these exhibits, and we've got 1404?

MR. VAN CLEVE: 1404 and 1409 through 1413.

JUDGE MOSS: And the question was whether there is an objection to any of these.

MR. BERMAN: No objection, Your Honor.

JUDGE MOSS: Then those will be admitted as marked.

And in terms of our order, I'm just neglecting things, I apologize, but the Bench has questions that should precede the redirect, so let's do that.

E X A M I N A T I O N

BY CHAIRWOMAN SHOWALTER:

Q. Mr. Gaines, I have a number of specific

questions that will track questions that arose during your cross, but I have a more general one first. And that is supposing within the four corners of Schedule 48 and the rate plan exists all the risks and specifics that you testified to, that say clearly lay out those different responsibilities. If this Commission finds that even taking into account all of those explicit risks and responsibilities, the net effect now is not fair, just, or reasonable, and maybe I should say now meaning at the end of this proceeding, not necessarily this emergency hearing, do you agree that the Commission in that instance would have the right to modify the tariff?

MR. BERMAN: I object to the extent you're asking a legal conclusion.

CHAIRWOMAN SHOWALTER: That's okay to object to my questions, I don't mind. Sometimes our experts up here are also experts in regulatory policy, and we allow the questions, and I will defer to the administrative law judge on that question.

JUDGE MOSS: I will overrule the objection.

CHAIRWOMAN SHOWALTER: I really don't mind if you object, because I need to hear the objection, so don't worry about it.

JUDGE MOSS: I was a little glib, I shouldn't

1611

be. We do have witnesses who frequently appear who have sufficient experience in regulatory matters. We had Ms. Linnenbrink the other night, for example, who demonstrated her expertise in the area, and so we allow witnesses to answer those questions, understanding that their lawyers may ultimately disagree with their conclusions as a matter of law.

A. Well, I think with those objections and clarifications, I should say that you're right, oftentimes the witnesses are adept in regulatory matters. I'm not sure I'm particularly adept on that question, but I will venture an opinion.

And that is that we think we have a deal, that Mr. Berman has called this a deal throughout the hearing, and we think that the terms of that deal should be inviolate. Now whether the Commission can reopen the deal, I don't know that I'm qualified to speak to. But it does seem to me that if it can, then maybe everything is fair game, and maybe there are other elements of the deal that would need to be readjusted also.

BY CHAIRWOMAN SHOWALTER:

Q. And I think I am getting at the should versus must question, that is, or maybe it's the should versus can't. And by that I mean one argument would be that this Commission has no right to change the terms of the

1612

deal. The other might be that, well, it may have the right, because after all, all of these are tariffs, not contracts in the sense that people understand that sometimes, but nevertheless, we shouldn't because a deal's a deal, and that's a different level of discretion on our part. But I take it you don't want to turn yourself into a lawyer and say we may not?

A. I just don't think I'm qualified to do that.

Q. All right, that's all right.

Maybe we could turn to Exhibit 605, and I am using this for my questions simply for illustrative purposes, which I understand is how it was offered anyway. But let's say you purchased in November of last year an option to buy power during the months of January and February this year. First of all, once you do that, once you exercise that option to purchase but yet you have not yet purchased, would that change how this graph would look if you redid the graph on the day that you purchased the option?

A. Well, it could, and it would depend on whether or not on the day that I redid the graph that

option in January and February was in the money. That is if the market price in January and February was higher than the strike price of the option that I purchased, then I would show the power that's related to
1613
that option in my resource graph.
Q. Okay.
A. That's what I would do.
Q. Then let's say you buy those options November 1st, and on November 1st you redraw your graph, and at that point, you would just simply make a determination of whether the power you could purchase would be in the money; is that right?
A. Yeah, exactly, and I can tell you that on November the 1st those options were not in the money, so they would not have then altered the graph.
Q. All right, so they were not in the money that day. Now if you redrew the graph on November 15th, and I don't mean to pin you down on that day, but let's just say it's a day when it would show that that power was in the money. Then some of the white boxes would turn into patched boxes; is that right, part of the white boxes?
A. Well, more likely the solid part of the bar on the bottom would get larger, because I know the price at which the option could be struck, so it would look more like a fixed price resource at that point.
Q. All right. Now I want to jump a little, but bearing this example in mind, to how the Staff's soft cap proposal would work. I'm trying to understand the mechanics of it.
1614
A. Me too.
Q. And first of all, can you describe generally how you would see Puget first determining its costs and then determining whether or not to make a claim, I guess, that its costs had gone above the cap?
A. It's a good question, and we started to get into it in some of the cross-examination earlier when someone was asking about the time period over which this cap computation would be done, and there was one suggestion that it would be either an hourly or a daily computation, and then there was another suggestion that it would be a monthly computation, and it matters a lot which one of those things it is as to whether and how and how frequently we would make the claim, as you called it.
Q. Well, let's just take one or the other. Let's take a monthly claim. If January has been completed, and for the moment let's skip over the process you use, but supposing you say we were above the cap on seven days, and therefore we should be paid, how would you go about demonstrating that?
A. I'm not real sure, to be honest with you, because I'm not quite clear yet on just exactly which costs the Staff thinks would qualify as sort of incremental or marginal costs that would be a part of
1615

this soft cap proposal. Is it just the power that I purchased in that day for that day, or is it power that I purchased three months ago at some price for that day in question. I'm fuzzy about that.

Q. Well, that actually was one of my questions. Supposing instead of buying an option in November, you had simply bought power.

A. Right. Would that be included in the computation, I guess I don't know.

Q. Okay. But if you had bought an option only in November, then if you had exercised it on, let's say for a whole month just to make it easy, then I guess the question I have, does the cost of that power also include, would it or should it include the cost of the option, the premium paid?

A. The premium, well, it's a good question. I mean is the Company supposed to bear the premium cost of the insurance, and then the customers get the benefit under the soft cap proposal, or does the premium cost get recovered always, or does it get recovered pro rata when the option is struck. I mean we just don't know.

Q. Well, but do you have an opinion as to whether it should be? Supposing you are making the claim that the costs have gone above a cap, would you propose to include the premiums that you had paid at

some earlier time for the time period for which you are making the claim?

A. Well, honestly I haven't thought about it very much, because I wouldn't like to see that proposal implemented. But it does seem to me that if someone is going to enjoy the benefit, for example, of an option that is purchased, that they should bear the premium cost that's associated with the option.

Q. Well, then take the example where you buy the premium or pay the premium in November but never exercise it. It's simply a sunk cost that wasn't used for the months in 2001.

A. Right.

Q. How would you propose to treat that cost?

A. Well --

Q. Would you build it into the financial bars, I realize these are power bars, not financial bars, but would you pro rate it over January, February, et cetera?

A. Two answers I guess. First, I haven't thought very much about how you would do that. It does seem to me that if a premium cost is incurred, whether the option is struck or not, someone who is enjoying the benefit of the option whether its struck or not should bear the cost.

But this question in my mind illustrates the

broader point, that why have the Company make these hedging decisions for the customers. I mean this is the whole beauty of an index based tariff is it decouples the supply decisions from the pricing decisions, and it allows customers individually and in their own discretion and at various points in time to make the very hedging decisions that we're talking about rather than relying on the Company to do it. And the Company may do it in a way that isn't related to the customers' underlying costs or in a way that the customers wouldn't agree with, but yet they would have to bear the cost.

And so it seems to me that we have a very fortunate decoupling of this pricing aspect from the delivery aspect, and the customers should be happier, it would seem to me, to make these pricing and hedging decisions on their own individually.

Q. So you're saying if these premiums are not included in your costs, then you're not fairly treated. But if they are included, there are going to be disputes over whether you should have done it?

A. Was it a wise hedging strategy, was it one that each individual customer would agree with, and we could never be sure that it would be.

Q. Okay. I would like to ask some questions about the future with the variables being what happens

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if there is a West wide price cap versus not, and then what happens if California makes some long-term purchases in the market? I'm trying to get a sense of what might happen to the wholesale market. And then third, how the soft cap proposal versus the status quo would affect Puget in that wholesale market.

So let me begin let's take the simplest case. If FERC should impose a West side wholesale price cap, would you agree there that neither you nor the customers could or would have to go above that cap?

A. Yes, assuming that we could get a price cap in place broadly in the West that was applicable to all the market participants, yes.

Q. So if under the status quo with no changes in Schedule 48, you would not be affected, but other than the price that you collected from the customers, but the customers' own vulnerability would be limited to whatever that price cap was?

A. Well, no, we would be affected too on the cost side.

Q. Okay.

A. As you say, the revenue side would be limited by the price cap, but our costs of procuring power on the market would be similarly limited.

Q. Okay.

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A. So it works on both sides of the income statement.

Q. And I suppose also the price that you could get if you sold on the market would also be limited?

A. Yes.

Q. All right. Now if there is a soft cap and there's a West wide price cap, let's assume that the price cap is -- that the West wide price cap is at $150 and the proposed price cap is at $125. And frankly, I'm not sure how to work in the $25 premium.

A. Okay.
Q. So I would like to explore an example where the West wide price cap is higher than the net effect of the Staff proposed price cap. Now what happens there? I'm just trying to think this through.
A. Well, I will have to think this through out loud.
Q. All right.
A. Because I haven't thought about it myself. So we have a West wide price cap of $150, we have a so-called soft price cap with respect to these customers at $125.
Q. Right.
A. Well, we can explore some scenarios. We could explore one where the Company's costs are less
1620
than $125. I guess in that case, we recover costs, say they're $100, we recover costs. If we have a case where the Company's costs are $135, I guess we recover $125 in that case. We have a $10 loss versus cost loosely defined. But presumably our exposure never exceeds the difference between $150 and 125, the gap in between the two caps.
Q. And then I assume that the Mid-C Index would never go above $150 if there was a West wide price cap?
A. Presumably.
Q. So that's what I will call a ceiling under there, there's a cap and a ceiling maybe under the Staff proposal?
A. Yes.
Q. So what happens if your costs --
A. Theoretically we should not have costs above $150. It depends though a lot on how the cap is applied. Is it applied just to the daily spot market, or is it applied to the forward market. If it's not applied to the forward market, we could have bought power previously at prices that exceed both the caps, and we could be incurring those costs as a result of decisions that had been made previously. So it would depend a lot on the things to which the caps applied.
Q. All right. Now supposing though that we
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don't have a West wide price cap, and on this point let's pause for a minute about the FERC filing. As I understand it, your position before FERC is that there should not be a selective price cap that is subject on part of the market to a price cap but not others in the market; is that right?
A. Yes, that's right.
Q. So the current status is there is a soft FERC price cap in California of $150, or there will be in April; is that right?
A. Well, there is, and I hesitate to call it a cap even. I view it more as a trigger for a reporting requirement. It's phrased in a way that when the price exceeds the cap, if you will, that triggers an obligation on the selling utility to report the cost of

the power underlying the sale. And whether or not ultimately the selling price is limited to cost or some function of cost is to be determined by FERC.

Q. All right.

A. So it's really not a cap in my mind. It's more a trigger for a reporting obligation.

Q. Can you comment at all on what the effect is if we have a soft cap of $125 and FERC has imposed a soft cap of $150 in the California market, is there a way to relate those two things?

A. You mean if it were imposed only in the California market?

Q. Yes.

A. Presumably if it were imposed only in the California market, it might not have much effect in the market up here. But anything like that, anything that subjects the Company on the expense side to uncapped prices or prices that are capped at some high level, and on the revenue side to the sort of a soft cap that's proposed in this proceeding at a lower level, it introduces risk to the Company. It's what my boss calls the shock absorber position. It's a place where we would like not to be.

Q. And what does that mean by the shock absorber position, that you're feeling the collision of two forces?

A. Absorbing the difference between the wholesale market price and whatever retail power price is. It's directly analogous to the situation of the two large investor owned utilities in California right now. It is exactly what has led to the financial situation of those companies.

Q. I'm wondering about that one, because there it seems you have a hard cap on what the retail customers can pay that's below --

A. That's right.

Q. -- the actual price that the utilities have to pay, and therefore they just can't make up the difference.

A. That's right.

Q. But here there's a proposal for a soft cap, which should allow you to make up that difference.

A. Well, it's a matter of --

Q. Perhaps with some difficulty procedurally, but that conceptually, isn't it supposed to allow you to make up the difference?

A. I think it's just a matter of degree. I think what's being proposed here is not so extreme as the situation in California, but conceptually it's the same.

Q. Now assume that FERC takes no further action, but assume that the state of California backs large long-term contracts for the utilities there.

A. Mm-hm.

Q. What do you see as the effect on the Mid-C market or the rest of the wholesale market as a result of that?

A. Well, the expectation, of course, is that that will reduce the prices and the volatility in the spot market in California, which presumably then would

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be reflected up into the Northwest market as well. However, we are in uncharted territory, and we have a situation over the last several weeks where the California spot market has been trading at prices much higher than the Mid-C because of these credit concerns. And so if the State of California steps in to provide credit support, it should at least bring those two markets back closer together and may hopefully have the effect of depressing both the markets.

Q. I guess the reason I'm wondering, I sure don't know what it will do to the wholesale market, but it seems like if you had some very, very large purchases, it would remove a lot of supply from the market, it also removes some buyers. And I don't have a way of knowing which has a greater effect, the loss of supply or the loss of the buyers, or maybe it's equal on the spot market.

A. It is hard to know. It's all the same generators, and it's all the same loads, of course, physically in either case. And it's just a question of from day to day how much of the necessary supply is flowing through and being priced in a spot market mechanism, all of it or just some top fraction, as has been done historically.

Q. Well, I note that I have a question on

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Exhibit 25, so maybe we can turn to it, and I will try to remember what it is. That's the Bench request.

JUDGE MOSS: It's the Records Requisition Number 8 response. It's the charts where it's got a chart Mid-C flat forward prices for 2001.

A. Okay.

BY CHAIRWOMAN SHOWALTER:

Q. And you may have answered this in a couple of ways, but I just want to be sure I understand. Is this a forecast of what prices will be then or -- and by then I mean these for 2001, or is this the amount that someone could buy a one year contract for 2001?

A. It's the latter.

Q. Okay.

A. It's what the forward market was telling us on each of these days during 2000 would be the forward price as of that day for 2001.

Q. All right. So on January 10th of this year, someone could buy power for the whole year of 2001 on something around $220 a megawatt hour?

A. Yes, that's right.

Q. All right. I wanted to ask you a little bit about Schedule 48 and what happens if and when it terminates. There were a few questions on this. And do you agree that under Schedule 48 itself, it says that if

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Schedule 48 terminates, the customers have a right to return to a tariff, a regular tariff, but only if they pay long run incremental costs?

A. Yes.

Q. And can you outline for me essentially what that means. I don't mean an elaborate answer, but if we were to terminate Schedule 48 next month, let's set aside the question of whether we can do that, I'm just trying to say if we were to, how would you go about determining what the long run incremental costs are if the customers said -- if they declared, I want to go back onto Schedule 49?

A. Well, we have not given that a lot of deep thought in the Company. But generally, I think in order to determine that, we would need to know the duration of the commitment that the customer would make to continue to take power from the Company. And then the resource acquisition actions that we would take would then take that commitment period into account. So that would help us determine the specific power supplies that we would aggregate up in order to serve the customers going forward.

And so if it were a short commitment, it would probably be something reflective of the market prices that we have been looking at in this proceeding.

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If it were a very long commitment, you could either do that, or you might be able to do some resource development and reflect those costs back to the customer. But it would be -- it would be a function of a number of things, but including particularly the duration of the commitment.

Q. So if the customer said, yes, I want to get back on Schedule 49 for the next year, you're saying it would, the cost, the long-term incremental cost or the one year cost would be something like Exhibit 25?

A. Well, I think so. I don't know what else the Company could do to aggregate supply in that time frame.

Q. But if it were for a five year period, would you go out and buy a five year contract, or would you maybe buy a one or two year contract and then determine that you might build?

A. We might do that, but building, of course, or any form of long term resource ownership, you know, implies long-term, very long-term commitments, and we would need to have that, I think, from the customers to actually do that.

Q. So to actually build, you would want a 15 to 20 year contract?

A. Yes.

Q. I see. Then I wanted to ask you a little bit

1628

about the other proposal having to do with gas, a gas index.

A. Mm-hm.

Q. Are you fairly familiar with gas, wholesale gas prices?

A. Fairly much, yes.

Q. Can you make any observations about the reliability, I guess, of the SUMAS gas prices at this time?

A. Well, the SUMAS point where gas enters the U.S. from British Columbia is known in the gas industry as a relatively more thinly traded index, and so as a result of that, you know, there's some reluctance of major market players to trade at that point, although some do. Enron and Ngage Energy particularly make markets at that point.

Q. Well, I think I heard some presentation which suggested that the very high electricity prices in California were first of all in general causing gas prices to go up and that gas prices generally follow or have been following electricity prices, not vice versa. But that in particular because of the constraint of pipelines into California or out of California and because capacity had been bought up by various people, that the only available or non-contracted for capacity

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was in Canada and that this was causing the price of that gas to go up, because it was the only way to get it to California.

A. Yes, that's our understanding, at least, you know, during the fourth quarter of 2000 and particularly in the month of December that the SUMAS price essentially was the swing supply of gas for California. As a result, we had a tremendous run in the price of gas at SUMAS.

Q. Okay. Small questions. At one point you were asked about risks, and you said that now the Company bears the risks of costs that are above embedded costs, I think, for the core customers, I think. Did you say that?

A. Yes, I probably did.

Q. And what did you mean, how does it go, how do your costs for the core go above embedded costs?

A. Well, we have implicit, I guess, in the rates that the embedded cost customers are presently paying some power costs that were set in a rate case way back when, sometime prior to the merger. And so if the Company's resource costs have changed since that time, and they have, because of say escalation in PURPA contract costs, because of the expiration of certain long-term supply contracts which expose the Company to

1630

increased market purchases to serve the core, any number of things have caused the Company's resource costs to be greater than what is presently implicit in the embedded retail rates.

Q. Okay. Another question, and it's also looking at Exhibit 605, people can turn to it or not, I think we're pretty familiar with that exhibit by now, but can you explain to me if there's any difference between a financial hedge and a physical hedge that

Puget might buy? That is, as I understand it, you could pay a premium for the right to buy power at a future date. And if you do, I don't know how you think of that power in the future, as a fixed or variable priced?

A. The question was whether there is a difference between doing that with a physical transaction or with a financial transaction?

Q. Right.

A. And the answer is that from a financial economic dollar point of view, there is no difference. The only difference is whether in the one case if I buy an option that provides for physical delivery, the counter party delivers me the power when I ask for it. If I buy one that's just a financial option, then I go out and aggregate power at index, and he pays me the difference between index and whatever the fixed strike

1631

price is. So the only difference is do I get physical power delivery from the counter party or not. Economically and financially it's equivalent.

Q. Under the soft cap proposal, do you see that those two situations would be treated differently or not differently?

A. I hadn't thought much about the application of the soft cap proposal in connection with options, so I would need to think about that a little bit more. But generally no, I wouldn't see it making any difference under the soft cap proposal whether it's a physical arrangement or whether it's a financial one.

Q. Another question about hedges, this was in reference to your saying that periodically you use hedges on a kind of a careful planning basis.

A. Mm-hm.

Q. Is the goal to minimize the day ahead or short-term activity, or is that not a particular goal?

A. It's not necessarily a goal, but it's usually an outcome. The two primary objectives of our activity are, number one, hedging to limit the Company's financial risk, and number two, optimization. So to the extent that the Company has surplus supply or surplus transmission capacity or something like that, to optimize the value of that. And really we think about

1632

it in that order, hedging and then optimization.

Q. All right. Then you mentioned a number of contingencies that could worsen your situation, like Colstrip going out and having to supply Bonneville with power. But the question I have is, how would those contingencies affect calculations under the soft cap? Would it mean that you simply might go above the cap more easily because you had to allocate the power somewhere else, but nevertheless you would get paid for your expenses above the cap?

A. That's my sense, yes. I mean as I understand it, the soft cap would be calculated on an after the fact actual basis and would be reflective of whatever contingencies did occur and affected the resources.

Q. And I just remembered another question I have, but I think it's not written down anywhere. In one of your requests, did you supply, one of our Bench requests, did you supply a picture of the Mid-C Index over the last year?
A. Yes, we did.
Q. What is that?
A. Actually, it also shows up in one of Mr. Schoenbeck's exhibits, I think.
MR. BERMAN: Your Honor, Exhibit 1402 is an exhibit that Mr. Gaines had looked through.
1633
CHAIRWOMAN SHOWALTER: I think that was it.
MR. BERMAN: That's not a Schoenbeck exhibit. That was a Gaines exhibit.
THE WITNESS: I don't know if I have it here or not. Okay, right here.
MR. BERMAN: That was at tab 72 in the materials that we originally provided.
CHAIRWOMAN SHOWALTER: Right, okay.
BY CHAIRWOMAN SHOWALTER:
Q. Do you have Exhibit 1402?
A. Yes.
Q. Do you have a way to tell me, perhaps not eyeballing this, but going back and finding out the data, since July 1, how many days was the non-firm index above $125?
A. We could find that out, sure.
Q. Okay and then --
MR. TROTTER: Chairwoman, that's shown --
CHAIRWOMAN SHOWALTER: Is that somewhere?
MR. TROTTER: That's shown on Exhibit 1003, which was entered through Mr. Buckley. The same table has the data points listed.
CHAIRWOMAN SHOWALTER: In 1003?
MR. TROTTER: Yes.
JUDGE MOSS: We make those who bring cookies
1634
share, Mr. Berman.
MR. BERMAN: Would the Bench like some cookies?
JUDGE MOSS: We'll save it for the break.
BY CHAIRWOMAN SHOWALTER:
Q. I will tell you what I'm looking for, and maybe you can point out somewhere where I can find this information, which is on how many days last year or since July 1 did the index go above $125 and how many days above $150. And if you can tell me a column where I will be able to find that out, I will be happy. It must be the second column; is that right?
A. I'm not familiar with their exhibit, but we could certainly do a sort on this data and count the number of occurrences.
Q. Are you looking at Exhibit 1003?
A. No, I haven't found it yet.
Q. Okay, I think that Mr. Trotter has --
MR. TROTTER: If you go to the very last page

of the exhibit, page six, and the last three columns, it starts on the very last entry is the first day of the year, 2000. Okay, do you see that?
CHAIRWOMAN SHOWALTER: No.
MR. TROTTER: Page six, fourth column, it says date.
1635
CHAIRWOMAN SHOWALTER: Nope.
MR. TROTTER: Page six, in the bottom right-hand corner.
CHAIRWOMAN SHOWALTER: All right.
MR. TROTTER: There's actually two series of data going on this page, but just look at the fourth column has date, and at the very bottom is 1-1-2000.
CHAIRWOMAN SHOWALTER: Yes.
MR. TROTTER: On that day, the reported index of 15.53, okay, and the volume is shown.
CHAIRWOMAN SHOWALTER: The Mid-C Index was 51.53?
MR. TROTTER: Yes.
CHAIRWOMAN SHOWALTER: The non-firm?
MR. TROTTER: That would be the Mid-C Non-firm On-peak Index, okay?
CHAIRWOMAN SHOWALTER: All right.
MR. TROTTER: Then you can go straight up that column, and that gets you to February 8. Then you go to the same type of data for the first three columns, and you start at the bottom on February 9th, okay.
CHAIRWOMAN SHOWALTER: I see.
MR. TROTTER: So it kind of winds its way through the exhibit that way. So you haven't gotten to $125 yet. You go all the way to the top of the page.
1636
So through March 30th of 2000, we haven't reached $125 yet. Okay, it's all less than $125 in that dollars per megawatt hour column.
CHAIRWOMAN SHOWALTER: I see.
MR. TROTTER: So then you go to page five and start at the bottom, second to last column, that's March 31. And you go up, and then you go back down to the middle column of the page for July 1st, and then I guess July 19th, 2000, you see $201.85.
CHAIRWOMAN SHOWALTER: Yes.
MR. TROTTER: That appears to be the first day of the year that exceeded $125.
CHAIRWOMAN SHOWALTER: So --
MR. TROTTER: Continue up, and there's another one on July 26 and so on.
CHAIRWOMAN SHOWALTER: Right.
MR. TROTTER: So then you can see the data points that way. So the exhibit is actually, like on that page, it has three sets of three columns, and the dates kind of wind their way through it.
CHAIRWOMAN SHOWALTER: Right.
MR. TROTTER: It's sequential, but it's instead of listing them from top to bottom, they kind of go back up and down.

CHAIRWOMAN SHOWALTER: And it goes backwards

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in time.

MR. TROTTER: And it goes backwards, right. So it could be reorganized, but that's how it is organized. And this was taken, as I understand it, right from the newspaper as reported in the Wall Street Journal, by Staff.

CHAIRWOMAN SHOWALTER: We can obviously do our own counting if we want to, but if you want to help out tomorrow and bring a sort. And the question would be, beginning January 1, 2000, but also beginning July 1, 2000, how many days were above $125, and how many were above $150.

MR. BERMAN: We'll get that information, Your Honor.

JUDGE MOSS: I suppose we better make that Records Requisition Number 13.

MR. BERMAN: I would note that the Company, because it's a holiday, finding people today might be difficult, but we should be able to get the information sometime tomorrow morning, I would expect.

CHAIRWOMAN SHOWALTER: That's fine.

BY CHAIRWOMAN SHOWALTER:

Q. You were asked some questions about buy-sell agreements and 448, and I know this is not today a proceeding on 448, but can you outline extremely briefly

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what kinds of terms 448 allows that you have proposed in 448, in particular the length of the terms of possible contracts?

A. I have not looked at the latest several drafts of the tariff, nor the one that was finally submitted, but I don't know that we put any limitation on the term of the contracts that the customers could enter into.

Q. And then another question, are the kinds of contracts or agreements that could be entered into under 448 also allowable under Schedule 48 if both the Company and the customers agree?

A. I believe so. We spent a lot of time in the summer of 2000 illustrating for the customers and particularly for Georgia-Pacific how they could enter into forward physical power purchases even under the present Schedule 48 construct, so I believe so, yes.

Q. So as you see it, under Schedule 48 right now, a customer and the Company could enter into a buy-sell agreement for a specified period of time?

A. We --

Q. At least through next October, I guess.

A. I believe that we have shown the customers some deal structures like that, yes.

Q. You were asked if size is a factor in the

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ability to hedge, and I think you said it could be a factor.

A. I think so, when the loads get very small.

Q. And my question there is again about financial hedges versus physical hedges. Is size also a factor in getting a financial hedge?
A. Yes, I think so, when the loads get small. Generally I think it would result in some kind of a premium being paid over the open market price of the product.
Q. And on the question of size, would it be likely that a small customer could not get as good a deal on a buy-sell agreement as a bigger customer?
A. It's hard to say.
Q. All other things being equal, say, meaning they use the power in the same way, say flat?
A. I would say it could be, but not necessarily. You know, there are a number of energy marketing companies that -- in fact, many of them are stumbling over one another trying to woo customers. And so to the extent that someone was trying to build a customer list, it might not necessarily result in a small load paying a premium, but it could.
Q. Would it be possible for one or two or three smaller customers or maybe not so small customers, 48

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customers, to aggregate themselves and you would conduct -- you would arrange a buy-sell agreement for a collection of customers?
A. Well, at least conceptually, yes. I don't know what we have said in the proposed tariff about aggregation, whether that's something that the Company does or not or whether the customers can do it under the tariff or not or whether some energy marketer completely outside of the tariff structure could do it, but conceptually, yes.
Q. And under a buy-sell, whether it's under 48 or under 448, who is on the hook for the payment to the seller? If the seller wants to get paid, is the seller collecting from Puget, or is the seller collecting from the customer?
A. I'm not sure mechanically where we finally shook down on that in the final version of 448. But the concept is that the seller of power looks through Puget to the customer for payment and credit and all of those things.
Q. So the financial viability of the customer would be an issue that the seller would look at, they wouldn't just stop with PSE?
A. Yes, exactly. And if that were questionable, the Company -- the customer might need to put up some

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sort of credit support letter or something.
Q. I wanted to clarify something on the questions about the residential exchange. I think I heard you say that if PSE gets physical power under that arrangement, it can sell that power on the market, but it must pass through the value of that power to the residential and small farm users.
A. That's what I had in my mind, yes.

Q. And would that be in the form of a credit on the bill?
A. Yes.
Q. I think you talked a little bit about ISP's, that you didn't think that they should be part of the core, that at least they should -- well, let's stay away from core and non-core, that they should pay market prices. This Commission hasn't decided what to do about new ISP customers.
A. Yes.
Q. Supposing we decide that they should be able to be treated like any other new arrival in the community.
A. Yes.
Q. And should be able to get on Schedule 49 rates or perhaps a term that they commit to, but in any event, not a market price.

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A. Mm-hm.
Q. What would that do to the calculation of who is core versus who is non-core? I mean where would they fit in the Staff's proposal of those bars? Where would they fit on the bus, to use the metaphor; would they be on the bus before or after?
A. Well, I think they would be the second to the last on the bus, if I understand the Staff's proposal right. In your hypothetical, you suggested that they would be not priced at market, but rather something more approximating a fixed price. If that were the case, I would think they would be I guess second to last on the bus. I think we would need some more definition around it to know exactly, but it would tee up all the same financial risk issues that are being discussed in this proceeding for the Company.
Q. With the difference that these new customers haven't entered into prior agreements?
A. Yes.
CHAIRWOMAN SHOWALTER: I think that's all the questions I have, thank you.

E X A M I N A T I O N

COMMISSIONER HEMSTAD:
Q. Back in your direct testimony, I wasn't

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entirely clear in understanding. You may have been quite clear, and my problem may be grasping the point in your discussion about discretionary wholesale transactions. And I thought I heard you to say that there was no duty to serve 48 customers ahead of any discretionary transactions that you would be undertaking in the market. Is that a fair understanding of your testimony?
A. That isn't what I meant to say. What I meant to say was that, you know, the Company's obligation to serve the Schedule 48 customers is spelled out in the tariff, and generally the obligation is to the extent that power is available in the spot markets, those

customers will be served. And it's only then after that is done that the Company might have surpluses to sell on a discretionary basis in the wholesale markets.
Q. Well, I don't want to repeat some of the questions that Chairwoman Showalter asked. There is some overlap here and with the others too. If we end up with California having a capped price, and I understand that you're a bit uncomfortable with the term cap here, but using that term, but FERC doesn't cap the Northwest, I wasn't quite clear as to what you thought would be the consequence of that circumstance.
A. I was dancing a little, because I'm not sure
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I know what might happen. Clearly the expectation is that that will moderate prices, but I -- you can't be sure.
CHAIRWOMAN SHOWALTER: If there's no cap in the Northwest, but there is a cap in California, that was your question?
COMMISSIONER HEMSTAD: That's my question, yeah.
CHAIRWOMAN SHOWALTER: It wasn't the purchases, it's the cap.
BY COMMISSIONER HEMSTAD:
Q. A cap in California but no cap in the Northwest.
A. I'm not sure I know what would happen in that circumstance either, but I think the tendency would be for power to want to be sold in the highest value market, which would be the uncapped market, I think, in the Northwest.
Q. Well, we would at least be at risk of having a two tiered market, one at capped price in California. I suppose in different scenarios one could be a higher price or a lower price, I suppose, under some scenarios in the Northwest.
A. Yes.
Q. But the Northwest wouldn't inherently track
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the capped California price?
A. No, that's right, and there would be a lack of evenhandedness, you know, as between the two regions in their ability to collect revenues from surplus power sales and offset other costs.
Q. Now would you consider that scenario to create, well, broadly defined, a flawed market?
A. Broadly, yes.
Q. In turn, would that support an argument that that kind of a market would not be a fair, just, and reasonable price?
A. Well, I don't know that, because the Company does most of its transactions in the Northwest spot markets at the Mid-Columbia, and we have heard, you know, a lot of discussion in this proceeding about the indexes and do they reflect the market or is the market itself somehow flawed or broken. But the reality is that the market is what it is. It's the water that we

all swim in, the Company and the customers alike. And so, you know, to the extent that the Company is bearing the cost of power purchases in those markets, they are what they are despite any flaws.
Q. Okay. Mr. Van Cleve had pointed you to Exhibit 1563. I believe that was the settlement agreement. And I don't think you need to get it out at

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this point unless you want to look at it again, and that talks about call it the safety valve available to the Company if it finds itself in economic distress.
A. Yes.
Q. I think that's the term used. And in which situation, if there is a requirement for rate or if the Commission concluded the Company was in such distress there would be rate adjustments, that would be spread equally among the various classes of customers?
A. Yes.
Q. And then presumably that would include the Schedule 48 customers. I think you said you weren't sure what that meant, but at least the language was such that it would apply to all categories of customers?
A. Yes, I don't have it in front of me, but I think it said all customers, and whether that meant all customers or all embedded cost customers, I just don't know.
Q. I see. And you also referenced the matter of storm damage, and I assume the reason for it, sort of an escape valve for storm damage, is there because that can under certain circumstances be a catastrophic event of very substantial costs unanticipated.
A. Yes, and the fact, I think, that that category of cost has historically been treated that way.

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Q. Do you find it at all troubling that the bargained for arrangements here in the settlement provide escape valves for the Company in the event it finds itself in economic distress but no such equivalent escape valve for the Schedule 48 customers if they find themselves in call it economic distress?
A. Well, honestly I don't. I don't find it troubling at all. I mean I think the merger rate order fairly well spells out the deal that was struck between the Company and the customers and the Commission. And if there had wanted to be an escape valve for the customers, I suppose one could have been put there. But I also think that the customers have had over the course of their experience so far under 48 the ability to control their costs. So for those reasons, it really doesn't trouble me.
Q. All right. Under the conceptual soft cap proposal, and I realize that there has been discussion here about certain significant practical problems and the like, but conceptually, I believe you stated in response to the question from the Chair that it's conceptually the same as California. Well, isn't it conceptually quite different from California, I mean

there the hard cap, but here the soft cap with the Company allowed to recover its costs if it's above the

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cap?

A. Well, the only reason I said what I did earlier is because even the soft cap introduces the potential for a mismatch between the Company's costs and the Company's revenues. That's all I meant.

Q. And what do you mean a mismatch?

A. It depends a lot on the accounting period over which the soft cap is computed, whether it's a daily computation or a monthly computation. You would get very different results, I think, under the soft cap proposal depending on which of those were chosen. And it would create different incentives for the Company in the way it would manage its supply, I think.

Q. Well, skipping over those not minor issues, but assuming for the purpose of discussion that with a soft cap the Company over time, well, over I suppose the remaining period of time in Schedule 48, earned substantial margins on the Schedule 48 sales. Would that still be a mismatch?

A. Well, in the strict sense I think yes. Schedule 48 is not a cost based tariff, and so could the revenues be quite different than the cost, yes.

Q. But if the revenues were substantially above the costs but still less than what would have been the case with no modification of the tariff, the Company

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would not be put in a position of having concern about any substantial economic risk, would it?

A. Well, only to the extent that it hastened the day when emergency rate relief would be required.

Q. And is that because the other categories of customers over the several years here have not been earning an adequate return?

A. I don't know for certain that that's the case. I was thinking more of the contingencies that we talked about earlier, the things that may occur during the year 2001 that are likely to create, you know, financial hardship on the Company.

Q. Well, in your opinion, can a market based price ever be unfair, unjust, or unreasonable?

A. Well, I suppose to the extent that -- I suppose it's possible, yes.

Q. I assume at some point, say the price spiked to $10,000 a megawatt, at some point, the price becomes intolerable, doesn't it?

A. That's right, and I think though that the fix -- the approach to that should be to fix the factors that are causing that to occur rather than putting the utility company in the position where it's squeezed between the wholesale market price and whatever its retail rates are. I really think the better solution is

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to solve the problem at its source at the wholesale level.

Q. Just so it's on the record, I asked this question of the other witnesses, do you believe there are grounds on this record to conclude there is an emergency?
A. No.
Q. Does the Company have a policy to seek to shed its large customers as core customers?
A. I don't know that it necessarily has a policy to shed the customers, no. The Company's view is that the customers have already made the decision not to be core customers, that that decision is sunk, and it was made at the time that they chose to go to Schedule 48. So by definition, they're not core customers at this point.
And so, you know, they face a couple of choices going forward. One is to, you know, engage in a buy-sell transaction that is the economic equivalent of market access and go forward and aggregate their own supply or to return to some kind of a tariff that the Company would administer but which would be reflective of the costs of supply going forward. So our view is that that decision has already been made.
Q. Well, how about customers, large customers,
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who have not elected in Schedule 48?
A. That would be different.
Q. I take it you have large customers who would have been eligible for 48 but have not elected that option?
A. I'm not sure that we do, or if we do, I'm not sure that they're very large.
Q. Finally, you were asked questions about how the Company manages its risks, and I understood your testimony to be that a major way of doing that is that either you or your day traders then make telephone contacts, over the counter, and with brokers on a daily or a weekly basis or whatever?
A. Yes, they execute the transactions that are called for as a part of broader hedging strategies that are developed and approved.
Q. And that you don't look to the NYMEX futures market as a way to really manage that risk?
A. No, we haven't used the NYMEX markets really. We tend to use the over the counter markets, because they're much more active and robust.
Q. Well, if the 48 customers are expected to manage their risk, they don't really have that sophistication, do they?
A. Some do to varying degrees. I think the
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larger energy intensive companies such as the refineries and to some degree the pulp and paper industry are experienced in commodity trading. In other companies where energy is not such a large portion of their cost, probably not. So for those who are not, they would probably need to get some assistance in doing that, either from us or from third parties.

Q. All right. So the smaller ones almost certainly wouldn't have the skills to do it themselves?

A. Probably not.

COMMISSIONER HEMSTAD: That's all I have, thank you.

E X A M I N A T I O N

BY JUDGE MOSS:

Q. Mr. Gaines, getting back to this question of the West wide price cap, you mentioned that you're familiar and you named a number of the big marketers, the big players, Enron and so forth, names we're familiar with. Can these marketers take their deals elsewhere if there's a West wide price cap?

A. Certainly the asset based company can. They own generation in the region. The generation needs to be run and sold. And so to the extent you're a generator or an asset operator, you really can't. If

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you're a peer trading company, I suppose you can stop trading in the West, or you can at least wind down whatever book of business you've got on over time and step out of western trading if you believe that price caps would so distort the market that you no longer desired to participate.

Q. How far ahead does PSE typically plan for its gas supply portfolio enough to satisfy all of its customers needs? Are you out six months ahead, four months ahead?

A. This now is on the core gas side, the LDC side?

Q. I'm sorry, I didn't mean gas, I meant on the electric side. On the electric side, how far out do you plan to meet your customers' needs? You mentioned, for example, that you entered into some hedging arrangements back in November for the November through February period. That was adequate along with your other supplies to meet the needs of all your customers, I take it?

A. Yes.

Q. And do you typically have plans like that in place out two months, three months, six months, whatever?

A. Yes. The Company is still developing its

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capability in this area, but as you know, we've got this underlying long-term resource portfolio that goes out many, many years in the future. We saw it in the bar graphs. And then the hedging and short term acquisition that is done around that core portfolio is done many months into the future, maybe a year into the future. But again, we're still developing that capability more.

Q. And I will divert back to the line of questions that Commissioner Hemstad was getting into, because that point does get back to it. I think that you said that your company has a number of executives, and I assume you're one of them, working on developing

these hedging strategies going forward?
A. We have a committee that reviews and approves recommendations for hedging, yes.
Q. And did you testify earlier that the Company is still finding that to be challenging, that you're still developing those programs and plans?
A. Yes.
Q. And so again, you wouldn't really expect the City of Anacortes and the CNC Container, companies of that size, to have the expertise or ability to do that sort of thing on their own, would you?
A. No, I think they would have to get some help with that.

Q. Do you think it's realistic to believe that the sorts of hedging opportunities that might be available generally in the market or under Schedule 48 or whatnot are something that these customers can take intelligent advantage of under the circumstances?
A. Well, I do. It happens in every state where the retail market has been deregulated, and it's the same large energy companies that are providing the services in the other states, so yes.
Q. Now getting back to the main line that I was pursuing there, if you looked at the PSE's resource situation today, could you look out say 90 days into the future and know what the maximum financial risk, if you will, facing the Company was with respect to supplies adequate to meet its full potential load at peak?
A. No, I couldn't, but there's a tremendous amount of volatility and optionality in our portfolio, and those sorts of forecasts, while you can make forecasts of that, there is always a significant degree of uncertainty around them.
Q. Even 30 days out?
A. Even 30 days out.
Q. What part of your service obligation, for lack of a better word, would that significant volatility affect? I mean I assume that you have some fairly

significant part of your obligation taken care of with longer term forward contracts based on the resource staff that we're looking at or your own resources really?
A. Well, we do, but resources break, power plants break, and so that's a source of volatility and uncertainty. And even still about 40% of our supply portfolio on an annual average basis is hydroelectric. So if we have a poor hydro year, that will affect that. We sit down stream from Grand Coulee with most of our generation. So to the extent that Bonneville likes to shape water differently month by month than what was anticipated, that would affect our production in a given period. And there are numerous other things that can occur as time goes by. So there's just a lot of volatility around it.
And as I mentioned earlier, it's much easier

to hedge price risk in a portfolio than it is to hedge volume risk. So we still have quite a lot of work to do, I think, in that area, learning to hedge that sort of risk.

Q. And you're doing that, you're undertaking that effort to make the forward look a bit more predictable; is that the object of the exercise?

A. Yes, and to put on hedging strategies that

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give us better certainty and better predictability.

Q. Do you have a goal about how far out you want to be able to reliably predict, subject to Grand Coulee Dam breaking and falling in two, that sort of thing, I mean putting aside the kind of disasters that we all hope to avoid, do you have a goal; does the corporation have a goal in terms of being able to sort of reliably plan, if you will, its financial situation 30 days in the future, 60 days, 90 days?

A. No, it doesn't have a specific time frame goal like that, although I would say generally a longer period than what you just suggested.

Q. There were some questions asked earlier about, and I think it was Mr. Van Cleve was asking you about the idea of FERC imposing a wholesale price cap, and I don't think we ever got to the underlying question. Do you think it's a good idea for FERC to impose a West wide price cap right now today?

A. We would support that on a temporary interim basis, and there's an increasing number of market participants, particularly in the Northwest here, that would support that.

Q. And what is the underlying reason that you think FERC should intervene in the market in that fashion?

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A. Because of -- probably the biggest underlying reason is because of the uncertainty of the squid hunt in California and what that's introduced in the market and broadly in the West, and so at least until that situation is brought a little bit more under control.

Q. So you're not just sort of a laissez faire economist type, let the market do what it will?

A. Well, I am actually, and I'm torn about this, and the Company is torn about it. I indicated earlier as a broad matter of policy, we're not supportive of price caps, because they tend to depress economic activity and resource development, which is exactly what is needed in the long run to solve the problems in the market. And that's why we have tried to be very clear whenever we suggested price caps that they should be done only on a short term interim temporary basis and that they should be evenhandedly applied. But in terms of broad policy, no, we don't think that's the right way to go.

Q. You, in connection with discussions regarding Schedule 448, and this was in some cross-examination by Mr. Trotter, and I think you made the comment on another

occasion as well, that it's PSE's hope that all of the current 48 customers will decide that your buy-sell tariff is a great idea and go to the schedule 448; is
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that basically it?
A. That's the hope, yes.
Q. Would you hold that hope forth for customers like the City of Anacortes based on what you have seen and heard in the course of this hearing?
A. I think that they can aggregate their supply and hedge their prices just as well with the Company or without. I think there are enough participants in the energy market that could provide that service to them that they could do just as well either way.
Q. Despite the fact that they take less than, what is it, two megawatts, two average megawatts, or whatever?
A. I think so. I think if they established a relationship with one of the large energy companies and it looked like it might be a long-term relationship that those companies would provide them the assistance that they need. We see a lot of this in the deregulated states happening with all kinds of customers.
Q. With loads of that size?
A. I don't have any specific experience in deregulated states, but someone is serving those customers in the states where the utility is no longer the default supplier at some fixed price.
Q. Now when PSE, and I'm going backwards through
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your testimony, you have probably picked up on it, when PSE entered into the Schedule 48 and Special Contracts and the whole merger, that whole period, all of those events were taking place in '95 and '96, that time frame, right?
A. Yes.
Q. Now I would think that the Company had some long-term financial goals in mind when it agreed to a five year merger rate plan that included, I don't want to call it a rate freeze, because it does have some escalators in it and one thing or another, but the Company had some long-term financial goals at the time it entered into that?
A. Yes, the Company had a goal to complete its merger with Washington Natural Gas and to achieve a level of earnings that was reasonable in light of the financial structure of the combined company. And again, as I indicated earlier, the retail rates under the freeze, if you like, were set at a level that were not thought to be generally representative of the company's then current costs. And so the challenge to the Company was to control and reduce its costs so that it could live within the revenues that were produced by these then existing rate levels. And so really its objective was just to produce a reasonable level of earnings for
1661
the new merged company.

Q. And this would be through the restructuring of the supply portfolio in part?
A. Yes, in part, and other cost reductions and efficiencies that the Company would realize.
Q. Certain so-called merger synergies?
A. Yes, exactly.
Q. That sort of thing. And has the Company been pretty successful over the last four years in achieving its goals in that regards, of moving steadily towards achieving those goals?
A. We have restructured two of the PURPA contracts, and we have brought costs down some as a result of that. We have had some synergies in the T&D side of the business. I'm not sure I could tell you in the aggregate how that all stacks up relative to what was hoped for at the time of the merger.
Q. Now we have had a fair amount of evidence, financial evidence and so forth, and I recognize that the Company has raised some questions about the quality of that information, but I'm wondering if it does not at least demonstrate that fortuitously by virtue of what has happened in the wholesale markets and the way Schedule 48 and the Special Contracts are priced, if the Company's margins have not improved beyond what anyone
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could reasonably have anticipated say a year ago before all these market price spikes and so forth?
A. No, I don't think you can necessarily conclude that. I think you need to look at it over a longer period of time. For example, if this same snapshot were taken in April of 2000, you would find on a cumulative basis the company's recovery from these customers was tens of millions of dollars less than what it might have otherwise collected. And now we have gone through a period where rates have been higher and there have been collections higher than the embedded cost rate schedules.
But there's absolutely no telling what might happen going forward or how the Company's revenues from these customers or its overall finances might fare over the course of this next year. There's nothing that's been introduced in this case that would give us really any solid evidence or information about that.
Q. And one part of the Schedule 48 approval tariff that was approved included some transition charges; you're familiar with that?
A. Yes.
Q. And those transition charges, as I understand it at least, were in part to compensate for the fact that PSE had a supply portfolio that considered the
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customers to be core customers, and it was going to have to adjust that through I think you used the word attrition over time. And that in the meantime because those were long-term obligations, some of those anyway, the transition charge, wasn't that supposed to compensate PSE at least in part for the fact that it had

taken the risk and gone out and gotten this power for the core customers?

A. Well, I have been told that, although I really don't know how the transition charges were calculated or whether they were calculated at all or whether they weren't just stipulated and agreed upon numbers. I'm just not very familiar with that.

Q. Okay. I'm afraid my notes aren't very clear on the point, but there was some cross-examination again by Mr. Trotter having to do with whether PSE anticipated the sort of spikes that we have observed in the Mid-C. And I think your testimony, at least in part, was no, you certainly didn't anticipate that sort of thing whatever happened at the outset. And perhaps even more recently, that wasn't anticipated. I was curious though, there was a price spike in the Midwest markets, I believe it was back in about June of 1998, that sort of got everyone's attention, if you will.

A. That's right.

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Q. And I'm wondering if the Company took notice of that in the sense of making any plans for hedging or financial or physical hedging and so forth going forward out of concern over what that might implicate?

A. We did take note of it. It was hard to help noting it really, and it did have adverse financial consequences on some of the trading partners that we dealt with. So yes, that was one of the factors that went into the Company's efforts to develop its own hedging capability.

Q. And has that affected your ongoing plans for this financial hedging project that you described? In other words, was that one of the things that spurred the Company to begin working more intensely, I should say?

A. It's one of the things, yes, among many. And, of course, what's happened here in the last many months has just reinforced our recognition of the need for that capability.

Q. I think this must have been back in Mr. Berman's direct, he pointed us to an exhibit that I believe either he or you described as representing some self help by Air Liquide in terms of shifting load from one rate schedule to another by means of having separate buses or meters or I'm not sure how the engineering worked. But I gathered from your testimony that you

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were inferring simply from the numbers, the change in the amount of load that was running on Schedule 46 versus Schedule 48, that this sort of self help was taking place contrary to your letter agreement. Was that the basis for that?

A. Well, that was part of it, but there was also some communication and correspondence between the Company and Air Liquide where Air Liquide sort of informed the Company that it was going to be making some changes internally in its plant and that this load transfer would be taking place, and it was really long after the load transfer actually had begun, and so it was, I think, that communication that really brought it to the Company's attention.

Q. I don't think we need to look at the exhibit, probably you and I have it well enough in mind, I noticed that the load on Schedule 46 changed pretty significantly from the earlier period to the more recent period.

A. Yes.

Q. But is that still within their rights under Schedule 46, do they have a service agreement with you under that schedule?

A. Well, yes, they still have the right to take service under Schedule 46 for that one complement of

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their load. What they don't have is the right to transfer load from the Schedule 48 service bank over to the keeper Schedule 46 service bank. That's where the issue rises.

Q. I guess my question was were they taking more than they're entitled to take under 46?

A. I don't know without looking at the service agreements if there's a limit on how much they can take under 46. The limit was on the transference.

CHAIRWOMAN SHOWALTER: Just for the record, I want to mention it's Exhibit 1405 so that if we're looking back at this conversation we'll know.

Q. I have heard reference to, on several occasions, I don't think it's come up in your testimony directly, but to people who were called I think key accounts executives?

A. Yes, key account representatives.

Q. And those are the people who are primarily responsible to be the contact people, if you will, between PSE and the industrial customers, say, who are key accounts?

A. Yes.

Q. And what are their responsibilities; are they essentially sales people, or what is their function?

A. Well, their function has been evolving a

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little bit lately. But generally during most of the period in question here, they're really it's a liaison function and to some degree it's a customer advocacy function within the Company. They see themselves as advocates for the customers' interest back at the Company. They do some of that. They maintain an ongoing liaison with the customers. They present new tariffs and things to the customers that they're eligible for, help them with all sorts of service issues, including transformation and T&D type service issues as well as the power itself.

Q. Are they under your supervision?

A. No, they're not.

Q. I will ask you anyway, perhaps you know, perhaps you don't, does the Company give them an affirmative responsibility to keep the customers informed regarding the customers' options to purchase under various rate schedules and that sort of thing, or are they more independent in terms of what communications they have with the key account people?

A. I'm not sure I can answer that very well, but my expectation is that part of their role is to make the customers aware of all the service options that are available to them.

Q. I guess what I'm getting back to is that it

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struck me that when Mr. Franz was on the stand and he testified that he was surprised to have learned recently that there was an interruptable rate schedule for which his company is qualified and that all of his other facilities throughout the country are on interruptables, and had he known about that, he would have probably signed up for that rate Schedule 46 instead of rate Schedule 48. And it puzzled me at the time why he would not have known about that, because they're a pretty big customer, I think, about 8 megs or something like that.

A. Well, it puzzled me too. I was surprised that he was surprised, because it seems to me that if he were in the business of purchasing power on an interruptable basis elsewhere that he would likely have inquired about it here also.

Q. I guess in part my concern over this issue, and I will use that word, do you believe that the Company as a public service company has some affirmative obligation to keep its customers informed of that sort of thing?

A. Yes, oh, sure.

Q. You described at one point in your direct testimony the relationship between the firm and the non-firm spot market as you used the word, interesting, and I wondered if you meant that in the sense of it has

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performed in a manner that is not what you would expect based on your experience in this field?

A. It's performed recently in a manner that's different from its historical performance. As we all learned in the complaint case, for the first several years of the indexes, there was a relatively stable difference or delta between the two indexes. And then recently in the latter part of this year, there have been wide divergences going both ways between the firm index and the non-firm index. And if you think about the transactions that comprise those two different indexes, that maybe shouldn't be too surprising. It's just that the divergence in the last six or eight months has been much greater and bidirectional as opposed to the historical differences.

Q. In terms of the testimony that Mr. Berman elicited from you with respect to earnings, and you were I would call it somewhat critical of the idea that you should take -- that anyone would take a look at daily earnings and draw very much from that, and you talked about the difficulty of comparing apples and oranges and coconuts and further said, the market is very dynamic and that in order to get a realistic picture, it would be important to look at the financial situation over longer periods of time. I just wanted to ask you what

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sort of time frame do you think is reasonable?

A. Well, I don't have a specific one, but a year or a series of years.

Q. Oh, you will be relieved to know I'm getting near the top. You described Exhibit 605, the PSE resource stack, as being a snapshot and said it's quite different today. I wonder, is that something the Company prepares on an ongoing basis, or was that prepared just to respond to a data request, or what's the story on that exhibit?

A. It's something that we prepare occasionally, and part of our effort in the risk management area is to prepare that much more regularly. But we're not yet at a point with our system of information that we can do that, and so it's more of a sporadic snapshot that we have been doing.

Q. Is there a more recent snapshot available?

A. We're working on one for 2001, but it's not final.

Q. And has there been one in the meantime since June?

A. Not that I'm aware of.

Q. Okay.

A. We were focused mostly on the latter part of 2000 and trying to manage that, and so we didn't put a

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lot of effort into 2001.

Q. You testified in response to a question from Mr. Berman that the Company has no obligation to plan for the Schedule 48 customers in terms of least cost planning or otherwise. But the question that came to my mind was, you do have an obligation to your shareholders to plan in that regard, don't you?

A. For Schedule 48 customers?

Q. Right.

A. I don't believe so. The way I think about it, I distinguish long-term resource planning and least cost planning and so forth, distinguish that from the shorter term operational planning that we do to serve them. But I'm not sure sitting here today that we've got a long-term obligation to plan resources for those loads.

Q. Maybe we're hung up on terminology here. I guess my thought was that the Company would have an obligation to its shareholders always to seek to make the necessary arrangements, be they financial, physical, or otherwise, to minimize its cost and maximize its sales and thereby maximize its profits.

A. Yes, I'm sorry, that's right, that's what I would characterize as operational planning for serving these loads, yes.

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Q. And you would agree the Company has that as a continuing obligation, probably the one that everybody has a motto on their wall about?
A. Yes.
JUDGE MOSS: Okay, well, that does complete my questions, and I thank you for helping me with your testimony.
CHAIRWOMAN SHOWALTER: I have a few follow ups to those questions.
JUDGE MOSS: I always do that.

E X A M I N A T I O N

BY CHAIRWOMAN SHOWALTER:
Q. One is you said that Schedule 48 customers if they want to get into buy-sell arrangements may need help in doing that. I think most of us have a sense of going to a lawyer for legal issues or a real estate agent for real estate issues or a financial advisor for financial issues, both on an individual and company basis. My question is, where does one go to get help in arranging a buy-sell agreement?
A. Well, there are a variety of places actually that you can go. You can come to your friendly neighborhood utility, and we would be glad to help. You could go to one of the energy companies that's active in
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the wholesale market and who might actually be a supplier of power to you and get help from them in designing a supply arrangement. Or you could go to the consulting community or the legal community and find individuals who are experienced in that area and get help.
Q. And in the last category of say independent advisors, can you give me any examples of either firms or individuals who fall into that category?
A. Sure, I think Mr. Schoenbeck's firm might be an example, or ESI in Vancouver might be an example. I could provide a longer list, but there are several.
Q. All right. Another question, when you said that you support at this time a temporary price cap, in your view, how long is temporary, at least for purposes of your recommendation to FERC at the moment?
A. I don't know that I have a view on that actually.
Q. You don't have a particular recommendation as to how long a cap should be imposed by FERC?
A. No, I don't.
Q. Is your position just that whatever it is, whatever the cap is that FERC may impose, if it imposes any one at all, it ought to be West wide?
A. Well, that's been the thrust of our
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recommendation so far, yes.
Q. You mentioned that if you took a snapshot in April, then the Company would be in a negative position vis-a-vis Schedule 48, but the snapshot in December shows it substantially ahead.

A. On the revenue side, yes.
Q. And that there's no telling what will happen in the future?
A. Looking only at the revenues, yes.
Q. Well, my question is, might it not be to the Company's advantage to quit while you're ahead. That is, if relief is granted now or some form of relief or some new 48 or 448, if we more or less ended this arrangement sometime in the near future, wouldn't the Company be ahead of the game?
A. I think that the Company would be supportive of an early implementation of 448, yes.
Q. Okay. And just to clarify one more time on least cost planning versus operational planning, I understand your testimony to say you have no obligation for least cost planning in the sense of planning long-term on a least cost basis for 48 customers, but that you do have a responsibility at least to your shareholders for operational planning that's on a basis where your costs are minimized and your profits are

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maximized?
A. That's right, I'm not sure that I have used the best terms to describe all of that, but generally yes.
CHAIRWOMAN SHOWALTER: All right, that's all my questions, thanks.
JUDGE MOSS: That would appear to be completion of the questions from the Bench, and I get the sense that the reporter would appreciate a break.
(Dinner recess taken at 6:10 p.m.)

E V E N I N G S E S S I O N
(7:15 p.m.)

JUDGE MOSS: I believe we're to the redirect.

R E D I R E C T E X A M I N A T I O N
BY MR. BERMAN:
Q. Mr. Gaines, I have a series of questions, kind of cover the field of different things we have heard. One point that was made during the examination related to purchasing of gas supply for your core gas customers. Do you recall that questioning?
A. Yes.
Q. And I think a question was asked about

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whether Puget Sound Energy hedges when it buys gas supply for its core LDC gas customers. Why doesn't Puget Sound Energy hedge when it buys gas for its retail gas customers?
A. Well, the Company never has done that. It's always been the understanding that we would pass through the direct cost of our gas purchases and that there would be some diversity in the purchases because it's made from different supply basins. But more importantly than that, we have had only the most brief discussion

with Commission staff about the prospect of hedging on behalf of core load, and we would only do that in the context of a much fuller discussion and understanding about whether and how that should be done.
Q. Would you expect that those discussions will continue, the discussions with the Commission staff?
A. Yes.
Q. Switching to another topic, there were some questions relating to whether hedges are available against the non-firm index as compared to against the firm index; do you recall those questions?
A. Yes, I do.
Q. And do I understand, is it correct that in general marketers and brokers base their hedges on the Mid-Columbia Firm Index?
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A. Yes.
Q. Does that mean that if someone has power pricing based on the non-firm index that they're just out of luck?
A. No, not really. You could probably find a counter party who would design a hedge around that index, or you could just hedge against the firm index, and you would be bearing then the differential between the two indexes, I believe.
Q. So, for instance, if we discuss a fixed for floating swap in relation to the firm index, do you know what I'm referring to there?
A. Yes.
Q. So you could cut a deal that says that, or the customers could cut a deal saying that they will pay a fixed price to a marketer, and the marketer will pay the firm index price back to the customer; is that correct?
A. That's right.
Q. And then if there's any difference between the firm and the non-firm price, the customer would have to deal with that level of risk?
A. That's exactly right.
Q. There were quite a few questions relating to your testimony in the 981410 complaint proceeding where
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you and other company witnesses discussed which index was most appropriate. Do you recall that questioning?
A. Yes, I do.
Q. And it was your position in that case that the non-firm index was not the best index to use; is that correct?
A. That's right.
Q. What were you recommending to be used instead?
A. Well, we were recommending a continuation of the blended index that we had been using all along.
Q. And the blended index is what?
A. It's the weighted average combination of the firm index and the non-firm index together.
Q. And so was it your view that taken together,

the firm and the non-firm fairly reflected the market?
A. Yes.
Q. Some concerns were expressed about whether the non-firm index matched the market. Was it your view then that the non-firm index overstated the market price?
A. No, no, it was never our position that it overstated, neither of the indexes.
Q. Is it your view now that the non-firm index overstates the market price?
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A. No.
Q. Do you think the non-firm index is, in fact, a pretty good match to that type of transaction?
A. I do, I think it's -- I think it's the best one available.
Q. And what type of transaction is that?
A. It's mostly the hour-to-hour transactions within a day, the so-called real time power market.
Q. Switching topics a little bit, you have discussed an obligation to sell power to Bonneville under some contract; do you recall that testimony?
A. Yes.
Q. And you told counsel for Complainants that that obligation preexisted your June 2000 resource graph; is that correct?
A. Yes.
Q. Why didn't you reflect that obligation in that resource graph?
A. Well, even though that has been a longstanding obligation that the Company has had to Bonneville, Bonneville has never exercised its right to receive power from the Company under that contract, and it was only late in December that they first informed us of their intent to do that.
Q. There were quite a few questions that went to
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the sophistication that would be required to be involved in the hedging markets. Do you recall that you submitted an affidavit in the Bellingham Cold Storage/Georgia-Pacific complaint case in the summer of 2000?
A. Yes.
Q. And do you recall that in that affidavit, you described a five year, $20 per megawatt hour hedge that Georgia-Pacific could have obtained to lock in $20 power for the entirety of its term?
A. Yes, I recall that.
Q. If a customer locked in a long-term deal like that, would they have to engage in numerous complex transactions?
A. No, they wouldn't have to. They could lock their price for say the entire five year period and be finished with it.
Q. So would you agree that it's just a question of how much risk the customer decides to bear?
A. That's right, and how they elect to do their

hedging consistent with their own cost. I think it's notable that one of the historically most vociferous Complainants in all of this is not present in the case today, Bellingham Cold Storage, and that's because, as we understand it, they now have obtained a long-term
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hedge and haven't found it necessary to engage in this activity.

Q. There were a number of questions about West wide price caps. To your knowledge, has Puget Sound Energy submitted any additional pleadings recently in its complaint proceeding at FERC?

A. I don't know that we have submitted anything, but we're preparing a pleading which would be an appeal to the FERC ruling of December 15.

Q. Is that a request for rehearing of their December 15th ruling?

A. Probably it is.

Q. And in that request, you reiterate your request for comparable price caps throughout the region?

A. I haven't read all the drafts, but that's the general theme of it, yes.

Q. A number of times in your testimony, you were asked about variable cost resources; do you recall that?

A. Yes.

Q. Could you tell me what type of resources fit within your view of variable cost resources?

A. Well, the way that I'm using the term here is that it's any resource whose operating cost vary with market, and so it would, of course, include the Company's combustion turbine resources that are exposed
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to the variability of the gas market, and I think that's well understood. But it would also include the spot market power purchases that the Company makes from time to time to serve either its core loads or Schedule 48 loads or both. So those market purchase costs would also be a variable cost resource under this construct.

Q. And so when you refer to the resources of the Company, you view wholesale power purchases as one of those resources?

A. Yes, that's right.

Q. I think we made this one clear on the record, but I just want to get it nailed down. When you were asked about Exhibit 617, even after I raised the concern about the use of we, you said we a few more times. Were you involved in preparing the analysis that went into Exhibit 617?

A. No, I was not.

Q. So when you said we, that was just a manner of speaking?

A. I think I used we a little loosely, and I will be a little bit more careful about that going forward.

Q. You were asked some questions about whether a buy-sell transaction could be done under Schedule 48; do you recall that?

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A. Yes.

Q. And I think you may have said that a buy-sell transaction could be done under Schedule 48. Could you explain that a bit more?

A. Well, what I meant to say was that we have shown the customers transactions, deal structures that could be done under Schedule 48 which we believe are the economic equivalent of a buy-sell although structurally not the same.

Q. So this relates back to the notion that there are financial deals and there are physical deals, and sometimes a financial can be economically identical to a physical?

A. Yes.

Q. On cross-examination, there were a few more questions that went to the potential ability of PSE to manipulate the market at the Mid-Columbia. Would you agree that any such manipulation would require a counter party?

A. Well, I think it would. I haven't spent a lot of time thinking about how to manipulate the market, but I suppose in order for there to be a transaction that would get reported to Dow Jones, there would have to be a counter party, yes. And I'm not sure how you would convince that counter party to engage in that kind

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of activity.

Q. And just to repeat, has Puget Sound Energy worked with any counter parties to create sham transactions at other than market prices to manipulate the market?

A. Puget has never done anything for the purpose of manipulating the market.

Q. There was a bit of questioning about hedges and derivative products that Puget Sound Energy has acquired for its own risk management purposes; do you recall that?

A. Yes.

Q. Did Puget Sound Energy win on those deals?

A. Win is an interesting question where hedges are concerned, because our view is that once you put a hedge on, you don't look backwards to determine whether it was in the money or not to determine a win. You look at whether it achieved its objective of managing or limiting price risk. And to the extent that it did that, you are successful regardless of whether or not the instrument that you chose ultimately was in the money.

Q. And in that respect, would you say it's something like car insurance or fire insurance?

A. It's an awful lot like that, particularly

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option type products where you pay a premium, and you don't necessarily have to collect on the insurance to "win", but rather you have limited your risk, and that's the objective.

Q. Would you agree that an entity that compares
what it paid for the hedge to what it, well, would have
happened if it took no hedge, is looking at it in a
wrong or unsophisticated way?
A. Yes, it's not the way that a true hedger
would look at it. Rather he would look to see whether
his hedging strategy achieved his objective of limiting
price or limiting the volatility of price.
Q. There were a number of references to the
surcharge or cost that would be imposed on customers if
they returned to cost based rate schedules; do you
recall that questioning?
A. Yes.
Q. Just to tighten that up, I would like you to
turn to do you have the prehearing brief that Puget
submitted with you?
A. I will find out.
Q. If you could turn to tab 2, which has the
Schedule 48 there, and this probably appears as an
exhibit in several places, but we have often referred to
the one in the prehearing brief. Do you have that in
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front of you?
A. Yes.
Q. I would like you to turn to I think it's the
eighth page, it bears the number sheet number 48-G at
the top.
A. Okay.
Q. Do you see paragraph two there, risk of
availability of power?
A. Yes.
Q. Midway through that paragraph or actually the
last sentence of that paragraph, could you read that
sentence into the record?
A. The last sentence?
Q. Yes, starting at the expiration.
A. Yes.

> At the expiration of the term of the
> service agreement, customer may commence
> taking service under any retail tariff
> providing firm service, however, the
> customer understands and acknowledges
> that such service may be subject to
> payment by such customer of any long run
> resource cost and any incremental
> capacity cost, which costs are not
> intended by the Company and customer to
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> constitute an exit fee incurred by the
> Company to provide such service.

Q. When you have referred to the cost that would
be charged to the customer, were you referring to what's
referenced there, that is the sum of any long run
resource costs plus any incremental capacity cost?
A. Yes.
Q. Is that just redundant, those two different
terms, long run resource costs and incremental capacity

costs?
A. Well, I don't think so. The way I have
interpreted those is that the long run resource costs,
you know, relate more to the full costs, you know, the
energy related costs of the new resource, and
incremental capacity costs are another category that's
additive to the resource cost.
Q. And again, you haven't worked out exactly how
those would work in a specific instance; is that
correct?
A. No, we haven't.
Q. I guess finally I want to bring you back to
some of the questioning that related to the merger rate
plan and Schedule 48 and how this all fit together. At
the initial prehearing conference in this matter,
Chairwoman Showalter essentially referred to a

three-legged stool that this all balanced on, a set of
risks that were assumed by the Company, by the
industrial customers, and by the other customer classes.
Do you think that's a fair way of looking at the set of
agreements entered into in 1996?
A. Yes.
Q. Is it correct that if the revenues are
disrupted with respect to the -- between the Company and
the industrial customers that that can affect the
balance between the Company and the other customer
classes?
A. Well, sure. For example, if the revenues
from the industrial customers are reduced in some way,
and if other events, poor hydro for example, cause the
Company to have poor financial performance, it will
increase the likelihood that the Company will need to
request emergency rate relief and recover costs from the
embedded cost customers.
Q. So I guess comparing to the situation of the
California utilities, there was some back and forth
about whether Puget Sound Energy is or is not in similar
straits as the California utilities. Would you agree
that with respect to the residential and small customer
classes that you have fixed your rates in the merger
rate plan?

A. Yes, that's right.
Q. And so if you now have to limit your revenues
from the Schedule 48 and Special Contract classes but
are still exposed to market, you really could find
yourself in the same position as the California
utilities?
A. Well, sure, we may not be buying all of our
power on the wholesale market like the California
utilities are, but we're buying some. And to the extent
we get caught between variable wholesale prices and
fixed retail prices, there will be a squeeze. We'll
need to recover those costs some way.
Q. So those deals just basically all fit
together?

A. That was the idea, yes.

MR. BERMAN: No further questions.

MR. VAN CLEVE: Your Honor, I neglected to also offer the deposition of Mr. Gaines, which I think was previously distributed. I'm not sure whether it has been given an exhibit number or not.

JUDGE MOSS: It has not, but I will give it one now. It will be 1414. And it's been offered, is there any objection?

Hearing none, it will be admitted.

CHAIRWOMAN SHOWALTER: Oh, I don't have a

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question, but I feel we should probably clarify the record after Mr. Gaines's testimony on a FERC filing. PSE has filed something before FERC, and the UTC has sent an overnight mail, a motion to intervene at FERC in support of PSE's motion. And both motions would seek a rehearing on the issue of whether there ought to be a West wide cap, and more particularly PSE says that if there is any cap, then it ought to be West wide. And the UTC for the State of Washington, not just the agency, has endorsed that view.

JUDGE MOSS: I had just a couple of points that I wanted to raise.

E X A M I N A T I O N

BY JUDGE MOSS:

Q. Mr. Gaines, very quickly I hope, in terms of PSE's actual activity at Mid-Columbia in terms of the spot market that is reflected through the indexes that these customers rates are based in part on, I thought I understood you to say earlier in your testimony that PSE only enters that market to balance its load on a real time basis. Did I get that wrong?

A. If I said that, I probably misled you. We do do transactions in the real time market, the one that underlies the non-firm index. We also do transactions

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in the day ahead or the daily prescheduled market, the one that underlies the firm index. So we're active in those markets, and, of course, as we have talked about in connection with hedging transactions, we're also active in the forward market at the Mid-Columbia, so all three of those really.

Q. And there are quite a few transactions that take place at Mid-Columbia that are not included and therefore not at least directly reflected by those indexes, right?

A. Yes, you're probably referring to the electronic data, the 3 million points that we submitted. And yes, that's right, a number of the transactions in that electronic data record are not reported. And many of those are forward market transactions, transactions that don't have anything at all to do with the hour-to-hour or day-to-day spot market, but rather are transactions for months into the future.

Q. You talked about some of the interesting characteristics at the non-firm and firm daily market or real time basically market has taken on over the past months. Is it generally true or always true that the forward market prices in the market there are lower than those reflected in the real time market, or does that relationship not hold either?

A. It doesn't hold. The forward prices can be either higher or lower than present spot market prices, and you will also find that forward market prices are not necessarily a good predictor of what future spot market prices will be.

Q. And I hope this doesn't require too big of an answer, but I was wondering, what would be required to work out the long run resource costs and incremental capacity costs that are referred to in the tariff; what would be involved in doing that?

A. Well, just thinking off the cuff, I mean I think we would have to have some idea about what the duration of the power purchase commitment from the customers would be, and then there would need to be some kind of a least cost planning process or something like that to determine what the most economic source of service would be over that commitment period, and it might be a combination of things. It might be a purchase for the first few years and then a resource in the case of a long-term commitment, or it might just be the market price in the case of a short-term commitment.

And so we would go through that process, I suppose, and determine what that least cost supply package would be. And then -- and the quality of it, of course, would have to match the nature of the commitment

to the customers. And then based on all those things, we would determine a rate.

Q. If the Commission were to task you with the project of establishing what those costs would be under a variety of scenarios, say one year duration, or let's go back, six months, one year, two year, how long do you think it would take to put together I will call it a menu or set of offers or whatever? I mean are we talking about something that would take you a few hours and a few days or a few months?

A. Oh, well, I think for shorter term commitments it would be fairly easy, because we would just look to the forward market. But for longer term commitments that involved, you know, selection among different resources and then actually the construction or contracting for a future resource, it would take us much longer to do the planning around that and the math, I think.

JUDGE MOSS: Okay, that gives me a sense of this, thanks.

CHAIRWOMAN SHOWALTER: I always have one follow-up question after Judge Moss.

E X A M I N A T I O N

BY CHAIRWOMAN SHOWALTER:

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Q. But I had been meaning to ask, you mentioned this word quality of service or electricity, could you just expand on what quality means?

A. Yes.

Q. Or what factors go into it?

A. Well, the way I was thinking of it just a minute ago is that, for example, in the case of the Schedule 48 customers, that quality of service is spelled out in the tariff. It talks about interruptability when power is not available to be aggregated in the spot markets. And so that's one quality. And then there's another quality that's for service to most of the embedded cost customers, which generally is a higher quality. And then there's, for example --

Q. Higher quality because it's not interruptable?

A. It's not interruptable just for lack of availability in the spot market. And then there's interruptable tariffs, of course, that the Company has which specify yet another level of service quality. And you could imagine or construct several others, I think.

Q. So by and large, you're talking about the ability to interrupt or fail to provide the power?

A. Yes, I mean our approach in constructing this

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sort of new resource cost for follow on service would be to match the character and quality of the supply purchase as nearly as possible to the character and quality and all of the other terms and conditions of the commitment made by the customer. We try to match those things as best we could.

Q. Now you introduced the term character, is character different than quality?

A. There are, if you look at power purchase and sales contracts, there are a number of attributes of the service that usually are specified. There's the term, there's the rate of delivery, there's the quantity of energy, there's the point of delivery, the interruption rights, all of those things are various attributes of a power supply arrangement. And all I mean to say is that we would try to match those things as nearly as possible as between the supply source and then the delivery commitments that we would make to the customer.

CHAIRWOMAN SHOWALTER: Thank you.

JUDGE MOSS: Okay, I believe then that brings us to the conclusion of our examination of Mr. Gaines, and we thank you very much. I'm sure you will be staying with us having been here for the duration.

THE WITNESS: Wouldn't miss it.

JUDGE MOSS: Mr. Berman, you have something

1696

before we move on?

MR. BERMAN: Well, I think it's in the nature of moving on, but before the Company closes its case, we have a number of exhibits not sponsored by a witness, and I wanted to move those in. I can very generally describe those right now for the record. Exhibits --

JUDGE MOSS: Give me half a minute.

(Discussion off the record.)

MR. BERMAN: Judge Moss, just for the record, the exhibits that are in our list of exhibits not sponsored by any witness fall into several categories.

1501 through 1514 were the exhibits to the various depositions that were used by -- that were taken by Puget Sound Energy in this case. So they support the various depositions that I believe have all been admitted in the case.

Exhibits 1515 through 1525 I will call generally the Pohndorf letter, that is a letter was sent to the Commission on December 12th of this year generally describing Puget Sound Energy's positions in relation to these matters with various supporting exhibits, and that letter and the supporting exhibits are Exhibits 1515 through 1525. And they were also produced as discovery in response to Staff Data Request 1.

Exhibits 1526 through 1561 is Puget Sound Energy's prehearing brief and all the exhibits that were appended to the prehearing brief, and everyone has had a copy of those exhibits, and we wanted to be sure that those exhibits were made part of the record.

Exhibit 1562 is an ICNU brief that was submitted back in the merger docket. We feel that's relevant to the proceeding because it describes the relationship between the merger case and Schedule 48 and how it all fits together.

Exhibit 1563 is the merger rate plan order, and I believe you already admitted that.

Then exhibits 1564 through 1569 are the depositions. You have already admitted those depositions, and so I don't think they have to be moved again. Exhibit 1570 is the least cost plan, the most recent least cost plan of Puget Sound Energy, which shows the fact that Puget Sound Energy does not account for the Schedule 48 and Special Contract load in its least cost planning.

JUDGE MOSS: Well, actually, I'm glad you did that, because it strikes me that we can then not have to worry about 1564 through 69 since they're already in the record, nor do we need to worry about 1501 through 14, since they are attached to those various depositions and

therefore part of the record. And I believe, let's see, the Pohndorf letter is not part, attachments not part. And the, well, the prehearing brief exhibits I guess we need to give them exhibit numbers, so yeah, the balance of it is offered then I think appropriately. 1515 through 1563 and 1570 are pending admission are there any objections to any of those exhibits?

Hearing no objection, they will be admitted as marked.

MR. BERMAN: Thank you, Your Honor. I would note that we do not necessarily refer during the examination in this hearing room to all of the deposition exhibits, but it's my understanding that you have admitted all of the deposition exhibits even if they weren't specifically referred to in this hearing room.

JUDGE MOSS: That's correct, what I am trying to do is save paper. We don't need to have them in the record twice. Parties can refer to them as deposition exhibit number whatever, and we will understand.

All right, so that takes care of your direct case, I take it, Mr. Berman.

MR. BERMAN: That is it for our direct case, Your Honor, in phase one. We, of course, reserve our right to submit any additional information if there are

additional phases of this case.

JUDGE MOSS: I need to make one amendment to what I said before. 1525 is already in the record as 605, so we don't really need it twice.

MR. BERMAN: And for that matter, Your Honor, 1561 is a duplicate of that exact same document, which seemed to arise everywhere. That's the resource graph.

JUDGE MOSS: So we won't have that one either. I'm just going to mark those as not offered for the sake of reference. It will take me just a minute here.

All right, then I believe we are ready for our rebuttal. Let me just make sure we've got all the players. You're going to have two witnesses on rebuttal?

MR. VAN CLEVE: Yes, Your Honor. The first witness is going to be Russell Crawford. We're going to call him first because we expect that Mr. Schoenbeck's testimony will again be confidential, so I think it would be better to get that witness out of the way first, and I think it should be pretty brief.

JUDGE MOSS: And is staff going to have anything in rebuttal?

MR. CEDARBAUM: I don't see any staff witnesses in here.

JUDGE MOSS: You can go out and drum some up, Mr. Cedarbaum, the night is young.

MR. CEDARBAUM: My guess is not, but I will have to double check with Mr. Trotter. I think the answer is no.

JUDGE MOSS: Okay, because I think the Complainants have the opportunity to go last, so I would really like to know.

MR. CEDARBAUM: Well, I think the only subject matter would have been on Mr. Gaines's testimony on the Staff rate plan, so. And the fact that there is no Staff person in the hearing room, I would say that we don't have a rebuttal case.

JUDGE MOSS: All right.
Then let's have Mr. Crawford back on the stand, and, Mr. Crawford, I will remind you that you remain under oath.
THE WITNESS: Yes.

Whereupon,
RUSSELL CRAWFORD,
having been previously duly sworn, was called as a witness herein and was examined and testified as follows:

1701

D I R E C T   E X A M I N A T I O N

BY MR. VAN CLEVE:
Q. Mr. Crawford, could you refresh our memory on who your employer is and what your position is.
A. Yes, I work for Tesoro Northwest Company in Anacortes, Washington. And what was the other question?
Q. What your position is.
A. Position is manager of process engineering.
Q. And you have previously testified in this case; is that correct?
A. Yes, I have.
Q. Have you heard the testimony during this case related to selective catalytic reduction?
A. Yes, I have, and I might be able to shed some light on that. It's not as simple, catalytic converter, as you might think. We have inquired from all three of our potential temporary emergency generator suppliers, and basically that pollution control equipment is not available to us from any of the suppliers.
Q. Can you tell us how big a temporary diesel generator is?
A. The 12 units that we ordered were one and a half megawatts, and they're from NC Machines, which is a division of Caterpillar.

1702

Q. And were those new machines?
A. I think they are fairly new machines, yes. They may have been used briefly, but I think they're fairly new machines.
Q. What type of emission concerns are there with this type of temporary diesel generator?
A. Basically the primary concern for us is NOX emissions, and we have inquired about what's been in the works, and I think there's some study underway, and there actually is some experimentation and development going on. But it's not available right now to just install on the generators. I mean they did not come with a pollution control device.
Q. Have you had an opportunity to review the California Air Resource Board document that was offered as a cross-examination exhibit, and I believe it's marked Exhibit 904?
A. Yes, I did, and I just briefly went through

some of this. It looks like it pertains mostly to particulate emissions, and there's also a disclaimer on the front page. But most of these items don't -- there's no NOX treatment at all with some of these summaries, and the others are again experimental and in the development phase.
Q. Have you found any of the technologies

identified in Exhibit 904 would be available for the temporary diesel generators that you have ordered for your facility?
A. No, my understanding is that they are not available.
Q. And in your investigation, have you found any selective catalytic reduction system that would be currently available for the diesel generators that you plan to use at your facility?
A. No, we have not.
MR. VAN CLEVE: That's all the questions I have, Your Honor.
JUDGE MOSS: Any cross from Staff?
MR. CEDARBAUM: No questions.
JUDGE MOSS: Company?
MR. BERMAN: Give me one minute, Your Honor.
JUDGE MOSS: All right.
MR. BERMAN: No questions, Your Honor.
JUDGE MOSS: Thank you, Mr. Berman.
Bench?
CHAIRWOMAN SHOWALTER: Yes.

E X A M I N A T I O N

BY CHAIRWOMAN SHOWALTER:
Q. What does not available mean? Was it NC

Machines that you talked to?
A. Correct, yes.
Q. And what were you told as to about availability?
A. Presently there's really no equipment that you can just purchase and buy and install for pollution control equipment.
Q. So your understanding is that it's not that the equipment is being used somewhere else or has been bought up, it just isn't available to anyone anywhere at the present time?
A. My understanding it's being invented. It's under development and really hasn't hit the marketplace yet.
CHAIRWOMAN SHOWALTER: I see, thank you.
JUDGE MOSS: Anything else from the Bench?
All right, well, with the market opportunity identified for all the inventors out there, I guess we can release you from the stand, Mr. Crawford.
THE WITNESS: Thank you.
JUDGE MOSS: Thank you very much.
Mr. Schoenbeck, welcome back, and remind you that you remain under oath.

THE WITNESS: Very good.

1705

Whereupon,

DONALD SCHOENBECK,

having been previously duly sworn, was called as a witness herein and was examined and testified as follows:

JUDGE MOSS: All right, I have been handed something that calls itself a water supply forecast, and I'm going to mark that as 623. And I have also been handed something that calls itself a spring run off comparison forecast versus actual, and I will mark that as 624.

D I R E C T   E X A M I N A T I O N

BY MR. VAN CLEVE:

Q. Mr. Schoenbeck, did you hear Mr. Gaines's earlier testimony regarding the hydroelectric water forecast for this year?

A. Yes, I did.

Q. And can you explain to us what Exhibit 623 is and how it relates to that testimony?

A. Certainly. Mr. Gaines had a very similar exhibit also from the Northwest River Forecast Center that was the January 1 early bird. This is simply an

1706

update of that exhibit but based on the final January forecast of the spring run off.

This is an exhibit that is prepared, the final version at least, is prepared for the six months January through June. I would like to point out a couple of things about it. First of all, while the focusing, on The Dalles, Oregon line where it shows the forecast as of January 1 final indicates a 76% of normal run off. The exhibit also shows a maximum and minimum possibilities. The maximum would be 104% of average, and this forecast center looks at excedentcies. And in this case, there would only be a 10% probability of getting a forecast in excess of the maximum level, a run off in excess of the maximum level. Similarly, the excedentcy with respect to the minimum run off is 90%. So there is at least a 90% probability already that there will be a run off of 48% of normal.

There is one other important aspect that I would like to clarify because we have been relatively loose in our terms throughout this entire proceeding, and one of them has to do with the critical water, the assumption that 2001 would be a critical water year.

In regional hydro planning, the critical water year is the one year period that is based on the 1937 water condition. The run off under that water

1707

condition is just barely under 70,000 acre feet.

So if, again focusing on The Dalles line, if you would see under the 76% forecast, that has a value of 80,400, so it's slightly over 10,000 acre feet greater than the critical water year. If you go over two more columns to the maximum line, you can see the maximum that's indicated of 110,000 acre feet corresponds to 104%. So if you do the math, you would find out an average spring run off is approximately 106 million, 106 thousand acre feet. If you do the simple interpolation between the non-firm energy that on average would be available between the 69,000 value and the 80.4 value, you would see that's somewhere in the range of 900 to 1,000 megawatts of surplus available above the critical assumption, critical water assumption.

Q. If you could turn now to Exhibit 624, is this a document that you prepared?

A. Yes, it is.

Q. Can you explain the document to us?

A. Certainly. The intent of the document is to show with respect to the first half that the January final forecast is not all that great of a predictor of what the future actual spring run off would hold. We have the water records of what the final predictions or

forecasts have been for the water years 1929 through 1994. The top portion of this exhibit shows the ten greatest deviations from the January forecast to what the actual was. You can see, for example, that using the 1985 water year, while the January final forecast has indicated a run off of 131,000 acre feet, the actual was only 87.8. Similarly, line five, which was the 1953 water year, had a value for January that was lower than the current value from the January 2001 forecast, and yet it ended up being for all practical purposes an average water year. So again, the January 1 final forecast is a 50/50 expectancy, and like all forecasts, it can be off.

The bottom portion of the table is just looking at the five years, the five water years on either side of the January 1, 2000, final forecasts of the 79.9. And again, it shows the same thing. For some water years, the run off actually decayed from the current value. And in other water years, it actually went up to an average water year value. What's shown by the final line of this sheet is just the average deviation between what the -- going from the January average versus final to the June average versus final. As you might expect, the deviation about the actual gets narrower and narrower as the jaws of uncertainty as you

move through time and you get the better impression of the snow that's been accumulated in the basin plus the precipitation.

So it's just simply to not put too much weight on the fact of we are looking at a or staring in the face of a critical water year based on 2001, and also that taken together, yes, it at a 76%, 77% level it

does not look great at this time, that's still above -- there's a significant amount of surplus power that would still be generated at that run off level.
Q. Thank you, Mr. Schoenbeck. I would like to turn now to documents which have been marked confidential, and I think we may have to refer to some of the confidential numbers in them. And I'm not sure, these are documents DWS-20, 21, and 22. I'm not sure whether they have been given exhibit numbers, but I think they have been previously distributed.
JUDGE MOSS: Those were the ones that were supplemental to the prior exhibits, weren't they?
MR. VAN CLEVE: That's correct.
JUDGE MOSS: All right, well, here's what I did with them. DWS-20 is a supplement to DWS-10, supplements and corrects that exhibit, and they are both marked as 612-C. And then DWS-21 supplements and corrects what was in DWS-11, so they both bear the mark
1710
613-C. And then DWS-22 supplements and corrects DWS-13, and they both together bear the number 615-C.
And is this, as we have been handling things, of course, we have been trying to go into confidential session at a point in the examination when we could most conveniently have people leave and turn off the phone and so on and so forth. Are we at that point, or I don't want to have to do a jack in the box routine.
MR. VAN CLEVE: Well, let me ask Mr. Schoenbeck.
BY MR. VAN CLEVE:
Q. Mr. Schoenbeck, do you believe that it would be necessary to specifically refer to the confidential data in these exhibits in explaining what you have done in the exhibits?
A. I was certainly planning on doing that. I could try and talk around that and not refer to specific values.
JUDGE MOSS: Well, can you just point us to the specific values, and we can see what they are, or do you need to say them out loud, keeping in mind that we all have the exhibit?
THE WITNESS: Right, I was thinking for comparative purposes, it may have been a lot faster just to speak to that as opposed to getting two pieces of
1711
paper -- I was just thinking timewise it would have gone faster just to state the values. I guess we can struggle through the comparison.
CHAIRWOMAN SHOWALTER: I would rather shut it down. It gets so difficult to say looking halfway across the page on line whatever, and you're never quite sure you're actually --
JUDGE MOSS: All right. Those of you who aren't signatories, apologize, but we need to clear the room again.
MR. BERMAN: Your Honor, if I might suggest, I have just a couple of questions of cross in relation

to the exhibits we just saw. I could wrap those up now so that we could just close out in confidential session.

JUDGE MOSS: Will this be the last area you go into?

MR. VAN CLEVE: Yes, it will, Your Honor.

JUDGE MOSS: All right, well, why don't we do that, and then those of you who have come to observe the hearing, what I would anticipate happening is we will have this non-confidential cross-examination, then we will go into confidential session. And as I understand the lay of the land, that will wrap up the evidentiary portion of the proceeding.

MR. VAN CLEVE: That's correct.

JUDGE MOSS: And so you all could go have some dinner or do something else that normal human beings do. And the rest of the hearing will be simply procedural. We will talk about the plans for the argument tomorrow and a few housekeeping matters and that sort of thing, which probably other than myself will bore everybody to tears. It's my job, so I can't acknowledge that it might bore me to tears.

So why don't we proceed as Mr. Berman suggested. I appreciate your suggestion. Go ahead with the non-confidential cross.

CHAIRWOMAN SHOWALTER: Well, let me just say, we will open it up again after the confidential session, so if you're here, you're welcome.

JUDGE MOSS: Sure, thank you, appreciate that.

C R O S S - E X A M I N A T I O N

BY MR. BERMAN:

Q. With respect to Exhibits 623 and 624, I guess first looking at 623, there's a final column on 623 that seems not to have copied well. Do I understand correctly that that reflects the average run off, that's the far right-hand column of 623, that's the average run off at the various points on the Columbia River?

A. Yes, that's correct.

Q. And do you know what the average run off was at The Dalles?

A. I did not look at it specifically. The guide I normally use is it would be 106,400.

Q. Which seems to correspond more or less to what it reports there about the maximum of 110 being 104% of the average?

A. Right, we could do the math by just taking the 110 and dividing by 104, and you would get a pretty significant digit number.

Q. If we just use for rough purposes that 106,000 is the average run off, if you could turn over to Exhibit 624 and look at this set of 11 years that are referenced down at the bottom group of the page?

A. Yes, I see that.

Q. In how many of those years did the actual

turn out to make it back up to the average water year?
A. The closest would be 1990 at 99.9 million acre feet.
Q. Would you agree that in none of those years did it actually make it back up to the average?
A. Yes, but if you also look at the top half of the table, 1953, it was actually less than where we currently are, and yet it made it back up, for all

practical purposes, made it back up to the average. There are a couple of other years like that as well that within the water records of record I had that they simply do not fall within what I was calling my top ten list for the greatest deviations in -- the ten deviations about the current value of 79.9.
MR. BERMAN: No further questions.
JUDGE MOSS: Thank you Mr. Berman.
All right, then I suppose we will move into our confidential portion, and as Chairwoman Showalter pointed out, we will announce for anyone who would wish to remain, if you want to come back in then we can do that, and I will go turn the telephone off, so we will be in recess briefly while I do that.
(Brief recess.)
(The following testimony is designated confidential.)

(Discussion off the record.)
JUDGE MOSS: We have had a brief recess and discussed the way in which we will proceed tomorrow for the close of our evidentiary phase and argument. What we have agreed is that, well, at 10:00 there will be a hopefully very brief open session, and then immediately following that, we have allocated 20 minutes to the Complainants to argue, 20 minutes to Staff and Public Counsel to divide up as they see fit, and, of course, you two counsel can split up your time as you see fit as well, 20 minutes for PSE, and then we have scheduled one hour which will be open discussion directed from the Bench, and then we will bring our proceedings to a close after that.
Now the commissioners will be leaving immediately after the argument, but you all might be prepared to stay for another half an hour or so, because there will probably be some housekeeping at the end to complete, and we will take care of any of that that needs to be done.
So are there any questions concerning our procedures tomorrow?

Then I appreciate you all being here and staying late yet again, and I look forward to seeing and hearing from you at 10:00 tomorrow morning, and we will

be in recess until then.

I apologize, there's one thing I neglected, and that is I had an inquiry from Mr. Prochaska who is representing the Union, and I have thought about it and decided that given the limited amount of time we have available for oral argument and given the fact that only the parties here have participated actively, other parties, that is to say interveners, will not be permitted to participate in the oral argument session. However, they may if they choose to do so submit a brief written statement of ten pages or less stating their argument and position in the case, and that needs to be filed by 9:00 tomorrow morning so that all parties can have an opportunity to review that in advance of the arguments.

And with that, we will be in recess.

(Hearing recessed at 9:30 p.m.)