Exhibit MPP-1T
Docket UE-070725
Witness: Michael P. Parvinen
REDACTED VERSION

BEFORE THE WASHINGTON STATE
UTILITIES AND TRANSPORTATION COMMISSION

WASHINGTON UTILITIES AND TRANSPORTATION COMMISSION, Complainant, v. PUGET SOUND ENERGY, INC., Respondent.	DOCKET UE-070725

TESTIMONY

OF

MICHAEL P. PARVINEN

STAFF OF WASHINGTON UTILITIES AND
TRANSPORTATION COMMISSION

January 28, 2010

HIGHLY CONFIDENTIAL PER PROTECTIVE ORDER

TABLE OF CONTENTS

I. INTRODUCTION

Q. Please state your name and business address.

A. My name is Michael P. Parvinen. My business address is The Richard Hemstad Building, 1300 S. Evergreen Park Dr. S.W., P.O. Box 47250, Olympia, Washington 98504-7250. My e-mail address is mparvine@utc.wa.gov.

Q. By whom are you employed and in what capacity?

A. I am employed by the Washington Utilities and Transportation Commission ("Commission") as the Assistant Director of Energy. In that capacity, I supervise the members of the Energy Section that analyze electricity and natural gas filings and issues. Before my current position, I was a Regulatory Analyst and later the Deputy Assistant Director in the Energy Section.

Q. How long have you been employed by the Commission?

A. I have been employed by the Commission since 1987.

Q. What are your educational and professional qualifications?

A. I graduated from Montana College of Mineral Science and Technology in May of 1986, and received a Bachelor of Science degree in business administration with a major in accounting.

I have testified before the Commission in the following proceedings:

Avista Corporation	Dockets UE-090134/UG-090135 Dockets UE-080416/UG-080417 Dockets UE-050482/UG-050483 Docket UG-021584 Docket UE-010395 Dockets UE-991606/UG-991607
Puget Sound Energy, Inc.	Dockets UE-090704/UG-090705 Dockets UE-072300/UG-072301 Dockets UG-040640/UE-040641 Dockets UE-011570/UG-011571 Docket U-89-2688
Cascade Natural Gas Corporation	Docket UG-060256 Docket UG-911246
Washington Natural Gas Company (now PSE)	Docket UG-931405 Docket UG-920840
The Washington Water Power Company (now Avista)	Docket UE-900093

I have also analyzed or assisted in the analyses of numerous other utility rate filings, and I have presented Staff's position on many such filings at Commission open public meetings. I have participated in utility-related rulemaking proceedings before the Commission. I attended the Seventh Annual Western Utility Rate Seminar in 1987, and the 1988 Annual Regulatory Studies Program, sponsored by the National Association of Regulatory Utility Commissioners.

II. SCOPE AND SUMMARY OF TESTIMONY

Q. What is this central issue in this docket?

A. The central issue in this docket is the appropriate regulatory accounting treatment for the money Puget Sound Energy, Inc. ("PSE" or "the Company") has obtained and will obtain from its sale of Renewable Energy Credits ("RECs") and Carbon Financial Instruments ("CFIs").

Q. What is the purpose of your testimony in this docket?

A. I provide Staff's recommendation regarding how the Commission should resolve that issue in this docket. I also respond to the three-part proposal PSE offers in its Amended Petition.

Q. How should the Commission resolve this docket?

A. The Commission should require PSE to book the net proceeds from the sale of RECs and CFIs in a regulatory liability account, which will reduce rate base. PSE will amortize the balance in the account over 10 years. We refer to this as the "regulatory liability" approach.

Using this approach, PSE would return REC/CFI proceeds to those customers who paid for the assets that generated those proceeds. All of PSE's retail customers paid for, and are paying for, the resources that generated the RECs/CFIs. Therefore, all retail customers should share the proceeds from the sale of these RECs/CFIs on the same basis as the Commission allocates these resources in the rate making process.

As an alternative, the Commission could require PSE to pass the REC/CFI benefits to customers on a yearly basis, with each year's actual amount of REC/CFI revenue allocated to each customer class using a generator-based allocator. We refer to this as the "direct refund" approach. This is the way PSE treats the Production Tax Credits (PTC) associated with its wind facilities. However, that treatment arose from a Commission-approved settlement,[1] so I am providing this example not as precedent, but to show that the direct refund approach can be implemented. I explain later why Staff prefers the regulatory liability approach.

The Commission should reject PSE's proposal. The Commission should not allow PSE to direct any REC or CFI proceeds exclusively to the benefit of any customer class or subset of customers, such as low income customers. The Commission also should not allow PSE to direct any REC or CFI proceeds to offset the California Receivable. Although Staff's regulatory liability approach is similar in concept to the third part of PSE's three-part proposal (PSE's Regulatory Asset proposal), Staff's approach more appropriately matches the allocation of benefits with the allocation of the costs of the resources generating those benefits.

III. BACKGROUND

Q. What are Renewable Energy Credits, or "RECs"?

[1] *Utilities & Transp. Comm'n v. Puget Sound Energy, Inc.,* Docket UE-050870, Order 04 at 9-10, ¶ 18 (October 20, 2005).

A. Renewable Energy Credits, or "RECs", represent the monetary value of the environmental attributes of the electricity PSE generates from its renewable energy facilities, such as a wind farm.

Q. How are RECs created?

A. RECs are created when PSE generates electricity from its renewable energy facilities: The Hopkins Ridge, Wild Horse, and Klondike wind facilities. PSE owns these facilities or has them under contract, and PSE operates these facilities. In my testimony, I refer to these resources as PSE's renewable resources, or as the resources or assets that give rise to the REC proceeds that are at issue in this case.

Q. How does PSE realize revenues from RECs?

A. PSE sells to other utilities the attributes associated with the output of PSE's renewable resources, and receives cash in return.

Q. In what markets is PSE able to sell RECs?

A. As I understand it, there are two distinct markets; a "compliance market" and a "non-compliance market."

"Compliance market" describes a market in which the utility purchasing RECs must acquire certain amounts of renewable energy. These sorts of requirements are often called "renewable portfolio standards", and they are contained in a statute. Typically, a utility subject to such standards complies by buying or building the renewable resource, acquiring its output, or purchasing RECs.

States without statutory renewable portfolio standards are called "non-compliance markets". In these states, a utility may purchase RECs if it wishes to add renewable resources to its portfolio, but no law requires it to do so.

Q. What are Carbon Financial Instruments, or "CFIs"?

A. CFIs are similar to RECs in that the CFIs typically are derived from any reduction in greenhouse gas emissions, as measured from a baseline. PSE's participation in the Chicago Climate Exchange ("CCX") created an opportunity and a market for PSE. As PSE has been acquiring renewable and lower emissions resources, PSE has sold CFIs to gain additional benefits for its customers.

Q. How are CFIs generated?

A. To the extent PSE has lowered its production of greenhouse gases below a baseline, it has been able to bank and sell excess CFIs to participating companies which are unable to physically meet emission targets.

Q. How does PSE realize revenues for CFI?

A. CCX has created a market where CFIs can be bought and sold. PSE has been a seller in this market, and receives cash from such sales.

Q. For rate making purposes, how does the Commission treat the resources that generate these RECs and CFIs?

A. Each of these resources are owned or under contract by PSE, and operated by PSE.

The Commission includes the corresponding investment amounts for these projects in PSE's rate base and power supply calculations for ratemaking purposes. The Commission sets PSE's rates to allow PSE an opportunity to recover the operating costs, taxes, and depreciation associated with these resources, as well as a return on the money PSE invested to acquire the resources. The Commission allocates the cost of these resources to the customer classes using a generation-based allocation factor.

Q. What is the current balance of RECs and CFIs on PSE's books?

A. As of November 30, 2009, PSE had the following balances of net cash proceeds from PSE's sale of RECs and CFIs:[2]

RECs: [redacted]

CFIs: [redacted]

Q. What is the estimated amount of PSE's contracted future proceeds from the sales of RECs?

A. Based on PSE's contracts, PSE estimates that future REC sales from 2009 to 2015 will be in the amount of [redacted].[3]

[2] The source of the REC balance is PSE's response to Public Counsel Data Request 30, Part C (CONFIDENTIAL). The source of the CFI balance is PSE's response to Public Counsel Data Request 31, Attachment A (CONFIDENTIAL).
[3] This source of this figure is PSE's first revised response to Public Counsel Data Request 37, Attachment A (HIGHLY CONFIDENTIAL).

IV. STAFF'S RECOMMENDATION

Q. How should the Commission treat the REC and CFI revenues PSE has received related to certain renewable resources PSE has in its rate base?

A. The Commission should distribute these revenues in an equitable manner to the ratepayers who have supported the assets that give rise to the REC and CFI revenues. As I have explained, these ratepayers are paying rates based on the costs of these assets, which includes a return on PSE's investment, plus all related operating expenses, and taxes. It is entirely proper for those ratepayers to receive the benefits generated by these assets on the same basis that their rates are set. This is the conceptual basis for Staff's Regulatory Liability approach.

A. Staff's Regulatory Liability Approach

Q. Please describe Staff's Regulatory Liability approach.

A. Under the Regulatory Liability approach, PSE will book the proceeds from its sales of RECs and CFIs in a regulatory liability account. In rate proceedings, this account will be used as a rate base reduction, with the balance amortized over 10 years. This regulatory liability will be allocated to customer classes on the same basis as the Commission allocates the associated renewable resources in the ratemaking process. In other words, the REC/CFI revenues are returned to PSE's customers in the same way PSE recovers in rates the costs of the assets which gave rise to the REC and CFI revenues.

Q. What are the benefits to PSE's retail customers from Staff's regulatory liability approach?

A. All else equal, PSE's retail customers will receive the benefits of reduced rates due to the lowering of PSE's rate base amount and negative amortization expense. The effects will be long term. In effect, customers receive the benefits of the REC sales, including the Company's rate of return, over 10 years.

Q. Can you suggest an alternative approach that also would pass the benefits of the REC/CFI revenues to PSE ratepayer on an equitable basis?

A. Yes. An alternative is a direct refund approach. Under this approach, the Company would pass the REC/CFI benefits to its customers on a yearly basis, with each year's actual amount allocated to customer classes based on a generation-based allocator. This approach also matches the distribution of REC/CFI benefits with the manner in which the corresponding assets are allocated to customers in the ratemaking process. This approach can be implemented. As I mentioned earlier, this is how PSE treats certain tax benefits associated with its wind facilities.

Q. Please explain why Staff recommends the regulatory liability approach rather than the direct refund approach in this case.

A. The regulatory liability approach provides long term benefits to customers. While the direct refund approach also fairly allocates the benefits to customers, it provides benefits over a shorter term, and it will result in a direct rate increase when the refund rate expires.

V. STAFF'S RESPONSE TO PSE'S THREE-PART PROPOSAL

Q. Please summarize the relief PSE seeks in its Amended Petition filed in this docket on October 7, 2009.

A. In its Amended Petition at pages 1 and 6-9, PSE requests an order from the Commission allowing the Company to defer net revenues from the sale of Renewable Energy Credits ("RECs") and Carbon Financial Instruments ("CFIs"), and use those net revenues pursuant to the following three-part proposal:

1. **Part One: Low Income Proposal.** PSE proposes to use between $10 million and $20 million of REC/CFI proceeds to fund energy efficiency and renewable energy services for low income customers exclusively;
2. **Part Two: California Receivable Proposal.** PSE proposes to use $21 million of REC/CFI proceeds to write down the same amount of an accounts receivable, representing sums owed to PSE by several California utilities which purchased power from PSE during the 2001 western energy crisis. PSE calls this the "California Receivable"; and
3. **Part Three: Regulatory Assets Proposal.** PSE proposes to use the remaining REC/CFI proceeds to provide a benefit to all PSE customers by offsetting the REC proceeds against a regulatory asset on PSE's books.

Q. How should the Commission respond to PSE's three-part proposal?

A. The Commission should reject PSE's proposal, for the reasons I explain next.

A. Part One: PSE's Low Income Proposal

Q. Please explain the first part of PSE's three-part proposal, regarding the use of between $10 million and $20 million in REC/CFI sales proceeds exclusively to benefit low income customers.

A. PSE proposes to use from $10 million to $20 million in REC/CFI proceeds for two specific purposes: 1) To install efficiency measures and energy-related repairs for low income customers exclusively (~ 80% of the total amount); and 2) To install renewable energy systems exclusively for low income residential locations (~20% of the total amount).[4] No other PSE customers would receive this money. The Joint Parties[5] support this part of PSE's case.[6]

Q. Is PSE's low income proposal appropriate?

A. No. First, PSE's low income customers are not the only customers who paid for the assets that generated these RECs and CFIs. As I explained earlier, any REC/CFI sales proceeds available for customers should be returned equally to the customers paying for the assets generating the benefit. Giving $10 million to $20 million exclusively to one group of customers violates this principle of fairness.

Second, awarding low income customers $10 million to $20 million fails to provide a commensurate benefit to the remaining customers because the proposed

---

[4] Amended Petition at 7, ¶17; Exhibit Joint 1-T at 8-12.
[5] The "Joint Parties" refers to the parties filing joint direct testimony: PSE, NW Energy Coalition, Renewable Northwest Project, and the Energy Project.
[6] Joint Testimony Direct, Exhibit Joint 1-T.

measures contained in the low income proposal do not meet the Commission's standard for an appropriate conservation program.

Q. What is the Commission's standard for conservation programs offered by PSE?

A. The Commission requires that PSE's conservation program be cost effective, based on the total resource cost test.[7]

Q. Does PSE's low income proposal meet this standard?

A. No. But, if it did, PSE would acquire the conservation under its existing program, which is designed to meet the Commission's cost effectiveness standard. There would be no need to apply an additional $10 million to $20 million of ratepayer money for this purpose.

Q. Does PSE's low income proposal provide commensurate benefits to other rate payers?

A. No.

Q. Could PSE's current energy efficiency programs contain certain features of PSE's low income proposal, such as repairing a customer's living unit?

A. Yes. However, the repair work must be cost-effective within the Company's program. Again, PSE's low income proposal fails this standard.

---

[7] *Utilities & Transp. Comm'n v. Puget Sound Power & Light Co.*, Docket UE-920630, First Supplemental Order at 11-12 (September 24, 1992).

Q. Please explain Staff's concerns with the second component of the low income proposal: To install renewable energy systems for low income residential locations.

A. While this proposal is laudable, it is not a proper use of rate payer money, for the same reasons I identified regarding the first component. This component also is not cost-effective on the whole, and it does not provide cost-effective benefits to PSE's other customers.

Q. Are there alternatives which PSE and the other Joint Parties could pursue to achieve their low income goals and treat all PSE customers fairly and equitably?

A. Possibly. For example, the Company's shareholders could contribute additional funds for these purposes; PSE could seek voluntary contributions from all customers to help pay for these repairs and new measures; or perhaps the Joint Parties could seek an additional appropriation from the Legislature to fund the low income weather assistance account, which they testify is administered by the Department of Commerce.[8]

B. Part Two: PSE's California Receivable Proposal

Q. Please explain the second part of PSE's proposal, regarding the California Receivable.

[8] See Joint Testimony Direct, Exhibit Joint 1-T at 6:25 to 7:4.

A. The Company is proposing that 40% of the REC/CFI proceeds, up to $21,062,800, be used to offset what PSE calls the California Receivable. The California Receivable is an amount on the Company's books held in reserve (as a receivable) for potential recovery through litigation processes.

Q. What is an account receivable?

A. An account receivable is the amount to be collected by a business from a customer for goods or services previously sold to that customer by the business.

Q. In the normal course of business, how does a business such as PSE account for an account receivable?

A. The business debits the amount of a sales transaction either to an account receivable or a cash account, and credits the sale to a revenue account. In this instance, PSE credited the sale to a Wholesale Revenue account.

Q. How does a business such as PSE treat an account receivable when the amount is disputed?

A. The business either writes off the sale to an uncollectibles account, or, if the business anticipates future payments from the buyers, it may keep the account receivable on its books pending final resolution of the matter. That is what PSE has done in this instance; it has kept the California Receivable on its books.

Q. In the normal course of business, what is the appropriate accounting entry for PSE to make if PSE determines that this $21 million is uncollectible?

A. PSE would have to write off the $21 million account receivable. The accounting entry would be a debit to the uncollectible account and a credit to the account receivable account.

Q. If PSE wrote off the $21 million California Receivable, would that have a rate impact?

A. Not under current practices and procedures. Currently, in rate making, PSE and Staff use uncollectibles amounts in two contexts: This calculation of the net to gross conversion factor; and in determining the test year level of uncollectibles expense. In both contexts, PSE and Staff take the most recent five years of uncollectibles, remove the amounts for the high year and the low year, and average the amounts for the other three years.

In this instance, the $21 million represents a very high level of uncollectibles. Consequently, this amount would be within the high year amount that would be removed in the process. Of course, there could still be some impact, because this could promote another year into the three-year average that would otherwise have been the removable high year.

Q. Please describe how the California Receivable came about.

A. During the western energy crisis of 2000-2001, PSE sold power to the California Independent System Operator ("ISO") and the California Power Exchange ("PX").

The total of these sales was reduced by actual payments, accounting entry reversals, and other miscellaneous transactions, resulting in a net balance which is shown as the $21 million receivable on PSE's books today.

Q. Why haven't the California ISO and the California PX paid this $21 million to PSE?

A. Apparently, the amount is the subject of ongoing litigation. The Company indicates that the dispute involves market pricing issues during the turbulent time in the western energy markets during 2000-2001. More than seven years of litigation has taken place to determine 'who owes how much to whom'.

Q. Should the Commission accept PSE's proposal and grant a compensated write off of the California Receivable using $21 million of the proceeds from REC and CFI sales?

A. No. The Commission should reject PSE's request to provide a compensated write off of the California Receivable.

Q. Why?

A. PSE needs to demonstrate that it received revenues in excess of fair market value for the RECs and CFIs it sold to the California utilities. If PSE had received money in excess of the market value for the RECs and CFIs it sold to the California utilities that indicates that the excess over market can be attributable to a PSE recovery of the California Receivable in the amount of such excess (up to $21 million).

On the other hand, if PSE did not receive any such excess, it indicates PSE did not receive any compensation for the California Receivable. In that circumstance, PSE simply would have received the same compensation it would have had in a market transaction, whether or not there was an account receivable, and there would be no reason for the Commission to give special regulatory treatment to this account receivable.

Q. Has PSE demonstrated that it received revenues in excess of fair market value for the RECs and CFIs it sold to the California utilities?

A. No. While PSE has stated that the REC sales would not have occurred but for the settlement regarding the power sales,[9] PSE has not shown the REC price exceeded market price in the compliance market, or if so, by how much. In this case, the relevant market is the "compliance market" because PSE sold the RECs and CFIs to utilities located in California, which has statutory renewable portfolio standards.

Absent that demonstration by PSE, the Commission should not provide PSE a compensated write-off of the California Receivable.

Q. Is there any other reason why the Commission should not allow the Company to recover the California Receivable from the REC proceeds?

A. Yes. At the time of the original power sales transactions that gave rise to the California Receivable, the Company was under a five-year rate freeze as a condition of the Commission-approved merger between Puget Sound Power & Light Company

[9] DeBoer Direct, Exhibit TAD-1T at 7:19 to 8:2.

and Washington Natural Gas Company. During the rate freeze period, PSE bore the risk and received the rewards for all of its transactions, including all of its wholesale sales to California utilities. PSE should not be granted recovery from the REC proceeds for a cost attributable to a time period where rate payers were not impacted by those transactions, one way or the other.

C. Part Three: PSE's Regulatory Assets Proposal

Q. Please explain the third part of PSE's proposal, regarding Regulatory Assets.

A. The third part of the Company's proposal applies to all REC/CFI proceeds that remain after funding the low income proposal and allowing a compensated write off of $21 million for the California Receivable. PSE proposes to use these remaining REC/CFI proceeds to offset regulatory assets, specifically PSE's Storm Damages regulatory asset.

Q. Apart from its connection to the other two parts of PSE's proposal, is PSE's Regulatory Assets proposal appropriate in principle?

A. Yes. As Mr. DeBoer testifies, all else equal, reducing a regulatory asset lowers PSE's revenue needs by reducing the amount of revenue ratepayers pay for PSE to recover the asset, and it reduces the Company's working capital allowance.[10] This is very similar to the concept that underlies Staff's recommended outcome for this docket, which I explained earlier.

[10] DeBoer Direct, Exhibit TAD-1T at 9.

Q. Is PSE's Regulatory Assets proposal appropriate in calculation?

A. No.

Q. Please explain.

A. As I mentioned, PSE proposes to offset the Storm Damage regulatory asset with REC/CFI revenues. The problem is that the Commission allocates storm damage expenses to customer classes using the allocation factor relating to electric plant in service. By contrast, the Commission allocates the assets that provide the REC/CFI revenues to customers using only generation-based plant factors. This mismatch creates disproportionate shares of the REC/CFI benefits among customer classes.

Q. Do any other regulatory assets on PSE's books meet the criterion of being allocated in the same or similar manner as the resources that give rise to the REC/CFI revenues at issue in this case?

A. Yes. PSE has a number of regulatory assets that meet this criterion. However, a significant portion of these regulatory assets will most likely be fully amortized before the effective date of the Company's next general rate case. Therefore, using REC/CFI proceeds to offset these regulatory assets would produce no long term benefits for ratepayers. The other portion of PSE's regulatory asset accounts that meet this criterion is not large enough to specifically identify and offset.

Q. Has the Commission previously ordered a utility to offset a regulatory asset using a portion of the proceeds from sales of items similar to RECs or CFIs?

A. Yes. Docket UE-001157 involved a PSE accounting petition for Commission approval to defer revenues from the sale of excess sulfur dioxide (SO2) emission allowances. These allowances are similar to the CFIs in this case. In that docket, the Commission ordered the Company to credit the sales to FERC Account 254 – Other Regulatory Liabilities, and amortize the deferred credits annually over 10 years to FERC Account 411.8 – Gains from Disposition of Allowances.[11]

Q. Is Staff proposing this same type of methodology in this proceeding?

A. Yes. Staff is proposing to defer the revenues, thus creating a regulatory liability to be included as a rate base reduction and amortized the remaining balance over 10 years.

VI. CONCLUSION

Q. Please summarize Staff's recommendations in this docket.

A. The Commission should accept Staff's case and require PSE to: 1) Book the net proceeds from the sale of RECs and CFIs in a regulatory liability account; 2) Use the account to reduce rate base; and 3) Amortize the balance in the account over a period of 10 years. The Commission should reject PSE's three-part proposal.

Q. Does this conclude your testimony?

A. Yes.

[11] *In re Petition of Puget Sound Energy Inc., for an Order Regarding Authorization to Sell Sulfur Dioxide Emissions Allowances and an Associated Accounting Order,* Docket UE-001157, Order at 2 (October 25, 2000).

BEFORE THE WASHINGTON UTILITIES AND TRANSPORTATION COMMISSION

Amended Petition of **PUGET SOUND ENERGY, INC.** **For an Order Authorizing the Use of the Proceeds from the Sale of Renewable Energy Credits and Emission Reduction Allowances for Renewable Resource Research, Development, and Demonstration Projects and the Associated Accounting Treatment**	**DOCKET UE-070725**

BRIEF ON BEHALF OF COMMISSION STAFF

March 17, 2010

ROBERT M. MCKENNA
Attorney General

DONALD T. TROTTER
Assistant Attorney General
Office of the Attorney General
Utilities & Transportation Division

1400 S Evergreen Park Drive SW
P.O. Box 40128
Olympia, WA 98504-0128

HIGHLY CONFIDENTIAL PER PROTECTIVE ORDER

Redacted VERSION

TABLE OF CONTENTS

TABLE OF AUTHORITIES

Cases

Administrative Authorities

Statutes

Legislative Materials

Other

I. OVERVIEW AND SUMMARY

1 Puget Sound Energy, Inc. (PSE) must comply with the renewable resource portfolio standards of the Energy Independence Act (Act).[1] The Act, like other similar statutes around the country, requires a utility such as PSE to have a certain percentage of renewable resources in its resource portfolio.[2] A utility may comply with the Act by acquiring renewable resources, or by acquiring an interest in the physical attributes of renewable facilities, embodied in what are called Renewable Energy Credits (RECs).[3]

2 PSE has acquired renewable resources in advance of the Act's compliance deadlines. Consequently, PSE is able to sell RECs to compliance-needy utilities.[4] To a much smaller degree, PSE has also been a seller of similar items called Carbon Financial Instruments (CFIs).

3 To date, PSE has received substantial revenues from sales of RECs and CFIs, and will receive substantially more REC revenues over the next several years, pursuant to existing REC sales contracts.[5] In this docket, PSE seeks an accounting order from the Commission prescribing how these proceeds will be accounted for and distributed.

4 The key question is: Who is entitled to the benefits of these REC proceeds? The obvious and logical answer: The REC benefits should go to PSE's retail ratepayers, because they are the ones burdened with the responsibility of paying rates sufficient for PSE to recover all of the costs of the resources that generate the RECs and CFIs. However, this has

---

[1] RCW 19.285.
[2] RCW 19.285.040(2)(a).
[3] RCW 19.285.040(2)(d).
[4] Compliance-needy utilities may be subject to the Act or a statute with similar renewable portfolio standards. In this case, the RECs were generated from sales to utilities located in California, a state that has renewable portfolio standards even more rigorous that the Act. Among other things, in California, a utility purchasing a REC must also purchase an equivalent amount of energy. De Boer, TR. 158:1-4.
[5] Parvinen, Exh. No. MPP-1HCT at 7:14-17. The specific REC proceeds amounts are confidential, and are shown in ¶ 19, infra.

not stopped two claimants from hoping the Commission will give them exclusive and substantial shares of this money.

5 The first claimant is PSE. PSE wants up to 40 percent of REC revenues, capped at $21.1 million, so PSE may enjoy a compensated write-off of an account receivable the Company booked in 2001. This "California Receivable" relates to certain PSE power sales to California. PSE claims these power sales made the subsequent sale of RECs possible, but there are at least two reasons why the Commission should reject that claim:

- PSE incurred the California Receivable while under a rate plan in which PSE took the risk and enjoyed all the rewards of highly lucrative transactions such as these. Therefore, PSE alone must bear all the risk related to the California Receivable; but, in any event,
- PSE failed to prove it would have received fewer REC revenues in the open market, absent those power sales and the subsequent litigation.

Should the Commission decide to award PSE a compensated write-off of the California Receivable using REC money, the Commission should deduct the $4.6 million in outside legal fees associated with the California Receivable litigation, which PSE's ratepayers have supported in the rates.

6 The second claimant consists of PSE and the three low income advocacy groups. They hope the Commission will carve out a special, separate share of REC and CFI proceeds for the exclusive benefit of a single customer group: PSE's low income customers. Not only that, they want $10 million in REC proceeds before anyone else gets a share, and 20% of all further REC proceeds, up to an additional $10 million.[6]

[6] Under this proposal, low income customers would receive not only the exclusive benefits from their proposed low income programs, but also a share of the REC benefits received by all ratepayers. Thus, if the

7 They want this money to fund two programs to provide low income customers energy efficiency benefits that otherwise would not be available, including house structure repairs, and installation of solar panels and solar hot water heating facilities.

8 PSE and the low income advocates could be correct that these special low income programs further various social welfare goals, but that is not the issue. The issue is whether their claim is reasonable and lawful. The record shows it is neither reasonable nor lawful:

- No customer group has a unique status entitling it to an exclusive share of REC proceeds;
- The funding of the proposed low income programs is unduly preferential, in violation of RCW 80.28.090.

In any event:

- PSE and the low income advocates base their claim on certain "public policy" factors as well as the policy in RCW 70.164, none of which is within the Commission's jurisdiction to consider;
- The proposed low income programs are not cost-effective; and
- Using REC money to fund these programs violates the "benefit should follow burden" principle.

9 In the end, the Commission should reject the claims for exclusive shares of REC proceeds made by PSE and the low income advocates. The Commission should return the REC proceeds to all ratepayers by requiring PSE to: 1) Book the net proceeds from the sale

---

Commission granted the Amended Petition as filed, the low income customers' share would greatly exceed $20 million.

of RECs and CFIs in a regulatory liability account; 2) Use that account to reduce rate base; and 3) Amortize the balance in the account over 10 years.

II. FACTS

10 PSE is seeking an accounting order from the Commission specifying the proper disposition of REC proceeds. An accounting order is necessary because without one, PSE would simply book the revenue in the month it is received.[7] The Commission would not otherwise capture these revenues for ratepayers absent a complaint or an appropriately-timed rate filing or other filing, such as the petition here.

A. PSE's Petitions

11 PSE initiated this docket on April 13, 2007, when it filed its original Petition. In that Petition, PSE asked to distribute REC proceeds two ways:

- **For research and development:** PSE would fund research and development (R&D) of renewable energy resources;[8] and
- **For all ratepayers:** For any REC revenue not used for renewable resource R&D within 18 months from when PSE booked that revenue, PSE would credit that revenue to all of its customers.[9]

12 In the Petition, PSE noted that the R&D aspect of its proposal would benefit customers because the revenues would be used to "develop renewable generation resources to be used to serve customers."[10]

13 On October 7, 2009, PSE filed its Amended Petition. In the Amended Petition, PSE abandoned its request that REC and CFI proceeds go first to renewable R&D that would

---

[7] De Boer, Exh. No. TAD-28.
[8] Petition at ¶ 18, 4th bullet (April 13, 2007).
[9] Petition at ¶ 20, last item (April 13, 2007).
[10] Petition at ¶ 17, item (2)(i) (April 13, 2007).

benefit all PSE customers. In its place, PSE wants up to 60 percent of REC revenues (capped at $41.1 million) exclusively for PSE and low income customers, as follows:

- **For PSE**: Up to 40 percent of REC revenues, capped at $21.1 million, for a compensated write-off of the California Receivable;[11]
- **For low income ratepayers**: Up to 20 percent of REC revenues, capped at $20 million, for two new programs exclusively to benefit low income ratepayers, with the first $10 million paid immediately;[12] and
- **For all ratepayers**: Whatever money is left after the PSE and the low income proposals (i.e., the amounts over $41.1 million), PSE would return to all customers via a credit to PSE's Storm Damage regulatory asset account.[13]

14 PSE filed testimony in support of the Amended Petition, through PSE witness De Boer, and a group of witnesses who filed supporting Joint Testimony: PSE, the NW Energy Coalition, The Energy Project, and the Renewable Northwest Project.

B. Nature and Amounts of PSE's RECs and CFIs[14]

15 According to PSE, RECs and CFIs are intangible assets related to certain types of generating facilities that represent the rights to claim the environmental attributes of such facilities. In the case of RECs, these attributes are sufficient to allow the REC owner to comply with renewable portfolio standards to the same extent as if it owned the resource.[15]

[11] Amended Petition at 8, ¶¶ 18-19 (October 7, 2009).
[12] Amended Petition at 6-8, ¶¶ 14-17 (October 7, 2009).
[13] Amended Petition at 8-9, ¶¶ 20-21 (October 7, 2009).
[14] In this docket, it was not necessary for Staff to explore all facets of the nature of RECs and CFIs. Consequently, PSE's descriptions will suffice.
[15] Amended Petition at 3, ¶¶ 4-6 (October 7, 2009). For the REC sales primarily at issue here, PSE "bundled" the RECs with a power sale in the same amount of megawatt-hours as represented by the RECs purchased. De Boer, TR. 158:1-4.

In California, a utility purchasing RECS must buy a "bundled REC," which is a REC plus energy in an amount equal to the energy the REC represents.[16]

16 In the case of CFIs, the resource attributes are sufficient to allow the owner of the CFI to comply with certain emissions standards, to the same extent as if it owned the lower emitting resources.[17]

17 RECs and CFIs are traded in the open market. For CFIs, trading is done on the Chicago Climate Exchange.[18] While there is no similar exchange for trading RECs, two REC sub-markets have evolved: the "compliance market" and the "voluntary market."[19] The compliance market consists of states which have renewable portfolio standards. A utility purchases RECs in this market to comply with a state's renewable portfolio standards. The voluntary market consists of states that do not have renewable portfolio standards. Thus, a utility purchasing RECs in the voluntary market is not doing so to comply with any statutory requirement.[20]

18 In working toward compliance with the renewable portfolio standards in the Act,[21] PSE has acquired certain renewable resources that generate electricity, as well as RECs: The Hopkins Ridge wind plant, the Wild Horse wind and solar plant, the Klondike III Purchased Power Agreement, plus certain upgrades to PSE's hydro facilities.[22] As the Act's requirements become more stringent through time, PSE will need to use these renewable resources to comply with the Act. Consequently, PSE's level of excess RECs will decline,

[16] De Boer, TR. 158:1-4 and Exh. No. TAD-13.
[17] Amended Petition at 4-5, ¶¶ 8-10 (October 7, 2009).
[18] Amended Petition at 4, ¶ 8 (October 7, 2009).
[19] De Boer, TR. 151:22-24. Staff used the term "non-compliance market" to describe this "voluntary" market.
[20] Parvinen, Exh. No. MPP-1HCT at 5:16 – 6:3.
[21] Amended Petition at 3, ¶ 7 (October 7, 2009).
[22] Amended Petition at 3, ¶ 7 (October 7, 2009).

with no excess likely by 2020, when PSE must be in compliance with the Act's most stringent renewable portfolio standard.[23]

19 The result of PSE having excess RECs to sell, and then selling them into the market, has yielded substantial revenues, and will continue to do so. As of November 30, 2009, PSE had [redacted][24] in net cash proceeds from the sale of RECs, and [redacted][25] in net cash proceeds from the sale of CFIs. Based on its existing contracts, PSE estimates that future REC sales from 2009 to 2015 will total [redacted].[26]

C. The Commission's Ratemaking Treatment of the Resources that Generate RECs and CFIs

20 As Staff explained, all of PSE's retail ratepayers pay PSE rates that reflect all the costs of the resources that generate RECs and CFIs:

> The Commission includes the corresponding investment amounts for these projects in PSE's rate base and power supply calculations for ratemaking purposes. The Commission sets PSE's rates to allow PSE an opportunity to recover the operating costs, taxes, and depreciation associated with these resources, as well as a return on the money PSE invested to acquire the resources. The Commission allocates the cost of these resources to the customer classes using a generation-based allocation factor.[27]

21 The foregoing facts are uncontested: Witnesses for Public Counsel, Industrial Customers of Northwest Utilities (ICNU) and The Kroger Company (Kroger) testified to the same facts;[28] PSE agreed to Staff's cost recovery testimony;[29] and PSE and the low income

---

[23] Amended Petition at 3-4, ¶ 7 (October 7, 2009). Similarly, but in much smaller magnitude in terms of dollars and time-frame, PSE also had excess CFIs to sell. However, PSE has no prospects for future CFI sales, and thus its membership on the Chicago Climate Exchange expired in November, 2009. Amended Petition at 4-5, ¶ 10 (October 7, 2009); De Boer, TR. 108:11 – 109:2. Therefore, from here on out, we refer primarily to RECs.
[24] Norwood, Exh. No. SN-4HC at 6, last line, last column.
[25] Norwood, Exh. No. SN-$HC at 9, last line, last column.
[26] Norwood, Exh. No. SN-5HC at 4, last line, last column.
[27] Parvinen, Exh. No. MPP-1HCT at 6:21 – 7:6.
[28] Public Counsel: Norwood, Exh. No. SN-1HCT at 3:16-20; 11:20 – 12:3; ICNU: Schoenbeck, Exh. No. DWS-1CT at 10:19-21; Kroger: Higgins, Exh. No. KCH-1T at 3:14-17; 6:1-7.
[29] De Boer, TR. 145:21 – 146:12: all of PSE's resource-related costs are part of revenue requirements and included in rates, "such things as reasonable operations and maintenance costs, property taxes, income taxes, depreciation, and a reasonable return on shareholders' investment in the wind facilities."

advocates specifically acknowledge that low income customers pay no more in rates reflecting the costs of the REC-related renewable resources than any other residential customers.[30]

III. ANALYSIS

22 PSE has received substantial revenue from selling RECs and CFIs associated with renewable resources. The basic question is who is entitled to the monetary benefit of those sales? The record makes clear that all PSE ratepayers are entitled to all of these benefits, and no one else has proven they are entitled to an exclusive share.

A. The Commission Should Provide All Net REC and CFI Revenue to Ratepayers in the Same Manner Those Ratepayers Pay Rates that Cover the Costs of the Resources Generating those RECs and CFIs

23 All PSE retail ratepayers pay in rates for the resources that generate the RECs and CFI at issue in this docket.[31] No single group of customers made a contribution to these resources to the exclusion of any other customer group, nor do these resources exclusively serve any particular group of PSE customers.[32] In particular, low income residential customers do not pay any more in rates for these resources than any other group of residential customers.[33]

24 Therefore, as Staff concluded: "all retail customers should share the proceeds from the sale of these RECs/CFIs on the same basis as the Commission allocates these resources in the rate making process."[34] Public Counsel, ICNU and Kroger concur.[35]

---

[30] Panel, Exh. No. J-13.
[31] *See* ¶¶ 20-21, supra.
[32] Parvinen, Exh. No. MPP-1HCT at 11:14 – 12:2.
[33] Id. and Panel, Exh. No. J-13.
[34] Parvinen, Exh. No. MPP-1HCT at 3:20 – 4:2.
[35] Public Counsel: Norwood, Exh. No. SN-1HCT at 3:16-20; 4:3-7; 10:3-6; 11:20 – 12:3; 23:22 – 24:2 (Public Counsel takes no position in its testimony regarding the low income proposal: Norwood, Exh. No. SN-1HCT at 4:15-20. Apparently, Public Counsel views the low income proposal as REC money going to "PSE

25 Staff's recommended treatment of REC proceeds satisfies the "benefit should follow burden" principle because the benefits of the RECs and CFIs follow the burden of cost responsibility. Thus, the fair and principled approach to distributing the REC and CFI sales proceeds is to provide them to all ratepayers in the same manner those ratepayers pay in rates for the resources that generate the RECs. Though PSE tries to make the analysis more complicated than it needs to be, the proper analysis is truly as straightforward as that.

1. PSE's "False Premise" Argument Falls Flat

26 PSE stands alone in contesting Staff's principled analysis. PSE contends Staff's analysis is founded on the "false premise" that ratepayers provided the capital to fund the renewable resources at issue, and they buy the resources when they pay their electric bills.[36] Notably, PSE's witness fails to support this contention with a cite to Staff testimony. This is not surprising, because nothing in Staff's testimony supports PSE's contention.

27 In fact, as we just explained, Staff's case is premised on the fact that all ratepayers bear the burden of cost responsibility for these resources that generate the RECs, and thus it is fair and appropriate to give all ratepayers the benefits.

28 In any event, PSE acknowledged that the risks investors take when they invest capital in PSE are reflected in the cost of that capital, and that cost is returned to investors through the fair return element of the ratemaking formula.[37] As such, there is no reason to compensate investors yet again for supplying that capital, by awarding them REC proceeds, too.

---

customers," i.e., as opposed to the Company); ICNU: Schoenbeck, Exh. No. DWS-1CT at 2:19-3:2; Kroger: Higgins, Exh. No. KCH-1T at 3:18-21; at 5:10-22; and at 6:1-7.
[36] De Boer, Exh. No. TAD-3HCT at 4:1-14 and at 6:9-19.
[37] De Boer, TR. 112:13 – 113:1.

29 PSE goes on to suggest that no one anticipated that REC proceeds would be available.[38] However, even assuming the REC proceeds are extraordinary and unanticipated, consistent treatment requires that ratepayers should get the REC proceeds.

30 For example, during the nuclear plant construction era of the 1970s, utility investors provided every penny of the investment PSE made in attempting to construct major nuclear power plants, just as PSE's investors have invested in, and now own, PSE's renewable resources today. A substantially adverse, extraordinary event occurred when PSE had to abandon those projects before they generated a single kilowatt hour of electricity. Investor ownership and funding of these projects did not prevent the Commission from requiring ratepayers to "share" risk with utility investors either indirectly, by approving substantially higher rates through a large increase in the utility's return on equity,[39] or directly, by requiring ratepayers to return to investors every cent of what those investors prudently invested in those failures.[40]

31 The instant case presents the reverse situation. Instead of a substantially *adverse* event, like nuclear plant abandonment, we have a substantially *beneficial* event: PSE's successful sales of RECs for substantial sums of money. Consistent with its nuclear plant abandonment decisions, the Commission could respond, either by: 1) Giving the REC proceeds to investors and then decreasing PSE's return on equity; or 2) Giving the REC proceeds to ratepayers. Inasmuch as PSE has not offered to lower its return on equity, and

---

[38] De Boer, Exh. No. TAD-3HCT at 4:15- 5-22; TR. 114:10-28.
[39] *Utilities & Transp. Comm'n v. Pacific Power & Light Co.*, Cause U-82-12, Fourth Supplemental Order at 29 (February 1, 1983).
[40] *Utilities & Transp. Comm'n v. Puget Sound Power & Light Co.*, Cause U-82-38, Third Supplemental Order at 19-20 (July 25, 1983), *aff'd, People's Org. for Wash. Energy Resources v. Utilities & Transp. Comm'n*, 104 Wn.2d 798, 711 P.2d 319 (1985).

there is no record on the magnitude of that reduction, the preferred course on this record is for the Commission to provide the REC proceeds to ratepayers.

2. Low income customers have no special claim to REC proceeds

32 We invite the Commission to scour the record to find any legitimate justification for tying REC proceeds to the proposed programs that exclusively benefit low income customers. The Commission will come up empty.

33 The closest the low income advocates came to connecting their proposed programs to REC proceeds was when the Panel offered the point that renewable resources generated the RECs, and one of the proposed low income programs would install renewable energy facilities on low income housing structures.[41]

34 However, while their statement is accurate, it does nothing to justify an exclusive share of REC proceeds for low income customers, because *any* customer group could offer the identical point in an attempt to claim an exclusive share of REC proceeds for installing renewable energy facilities on their own homes. In other words, the low income advocates provide no logical reason why their clients should get cutting edge technology before any other PSE customers.

35 The low income advocates made a similar attempt to justify a special status for low income customers by pointing to past low income R&D successes with compact insulation, ducting, door-fans and CFIs.[42] However, there is no evidence that R&D is needed for the programs at issue here. In any event, even if there was such a need, that still would not justify an exclusive share for low income customers, because PSE *all* customers should be able to participate in a renewable R&D program.

---

[41] Panel, TR. 92:15-18 (Gravatt).
[42] Panel, TR. 104:8 – 105:19 (Eberdt).

36 PSE should be able to implement such a utility-wide R&D program, because PSE proposed one in its Petition initiating this docket.[43] Notably, PSE saw no need for an exclusive share of low income R&D in that program.

37 The low income advocates' final attempt to justify a special status for their clients is their argument that "we need to invest in all [energy efficiency]" "to meet the climate challenge."[44] Obviously, this is just one more argument that does nothing to justify an exclusive share of REC proceeds for low income customers, because, assuming the Commission is authorized to address this challenge, there is no reason why *all* customers should not share in that effort and enjoy whatever benefits may come from it. No group of customers should get preferential treatment.[45]

38 When all is said and done, PSE and the low income advocates offer no evidence to challenge Staff's central point that all ratepayers should benefit from the REC proceeds, and no group of ratepayers should get an exclusive share. Therefore, the Commission should require PSE to distribute REC proceeds based on the manner in which the Commission allocates to the customer classes the costs of the renewable resources that generate the RECs.

[43] Petition at ¶¶ 17-18.
[44] Panel, TR. 101:23-25 (Gravatt).
[45] Moreover, as we explain in ¶¶ 90-91, infra, RCW 19.285.040(1) mandates that PSE acquire all cost-effective conservation. Therefore, to the extent the proposed low income programs are cost-effective, there is no need to use REC proceeds to pay for what PSE will do anyway. To the extent the proposed low income programs are not cost-effective, the Commission should not use REC proceeds to fund such programs anyway.

B. PSE is Not Entitled To a Compensated Write-Off of the California Receivable Using REC Proceeds[46]

39 In 2000-2001, PSE made lucrative power sales to California, a few of which ultimately became embroiled in litigation. Many years have passed, yet a $21.1 million account receivable still sits on PSE's books related to those litigated power sales transactions. PSE booked this account receivable in early 2001,[47] and it is now called the California Receivable. PSE wishes the Commission would use REC proceeds to achieve a compensated write-off of that receivable. For the reasons that follow, the Commission should not grant that wish.

1. Rate Plan: PSE reaped all the rewards, so PSE must now bear all the risks surrounding the California Receivable

40 When PSE made the power sales that gave rise to the California Receivable, PSE was operating under a Commission-approved rate plan[48] under which, among other things, PSE bore the risks and reaped the rewards of whatever the market would provide.[49] This includes the risk of an uncompensated write-off for "a good market power sales transaction gone bad." This describes precisely the California Receivable.[50]

---

[46] One point made by Staff was that an uncompensated write-off of the California Receivable would not have any rate impact. Parvinen, Exh. No. MPP-1HCT at 15:7-19. Staff's accounting of such a write-off is explained in De Boer, Exh. No. TAD-9. PSE contested that accounting in De Boer, Exh. No. TAD-3HCT at 21:14-19 and Exh. No. TAD-10, but PSE agreed that under PSE's accounting for an uncompensated write-off, there also would be no ratepayer impact. De Boer, TR. 109:14-25. For Staff, that closes the matter; it is not necessary for the Commission to address the accounting for an uncompensated write-off of the California Receivable.

[47] De Boer, Exh. No. TAD-1T at 6:3-10; Amended Petition at 8:¶ 19.

[48] *In re Application of Puget Sound Power & Light Co. and Washington Energy Co.,* Dockets UE-951270 & UE-960195, 14th Supplemental Order Accepting Stipulation, Approving Merger (February 5, 1997) at Appendix A, Stipulation, page 4:5-24, establishing a five-year rate plan "continuing through December 31, 2001," in which "PSE's financial results will be a function of management's ability to achieve these [merger] savings in order to provide shareholders with an opportunity to earn a reasonable return on investment."

[49] Parvinen, Exh. No. MPP-1HCT at 17:18 – 18:5.

[50] Parvinen, Exh. No. MPP-1HCT at 18:1-3.

41 In other words, because PSE booked the California Receivable during the rate plan, PSE must remain solely at risk for that transaction.[51] As Staff explained:

> During the rate freeze period, PSE bore the risk and received the rewards for all of its transactions, including all of its wholesale sales to California utilities. PSE should not be granted recovery from the REC proceeds for a cost attributable to a time period where rate payers were not impacted by those transactions, one way or the other.[52]

42 As Mr. Schoenbeck similarly testified, PSE's wholesale sales activities during the rate plan were "solely for the benefit or detriment of its shareholders," and thus there is "absolutely no justification for now allowing PSE's current shareholders to benefit from the net revenues from REC the sales ..."[53]

43 The Commission should summarily reject PSE's proposal to award 40% of REC and CFI proceeds (capped at $21.1 million) to enable PSE to achieve a compensated write-off of the California Receivable. However, should the Commission decide not to address the rate plan issue, we next provide ample other reasons for the Commission to deny PSE relief.

2. PSE has not proven a substantial nexus between the litigation over the California Receivable and the amount of REC proceeds

44 As Staff explained, for PSE to prevail in its argument that the account receivable is linked to the REC benefits sufficient to justify a compensated write-off using REC money, PSE needs to prove that PSE received more in REC proceeds than it would have received but for the litigation.[54]

45 In simple terms, PSE needs to produce concrete facts identifying the amount of proceeds it would have achieved from REC sales in the compliance market absent the

[51] Parvinen, Exh. No. MPP-1HCT at 17:18 – 18:5; Public Counsel: Norwood, Exh. No. SN-1HCT at 15:20 – 16:2; ICNU: Schoenbeck, Exh. No. DWS-1CT at 9:19 – 10:15.
[52] Parvinen, Exh. No. MPP-1HCT at 18:1-5.
[53] Schoenbeck, Exh. No. DWS-1CT at 9:21-19 – 10:8.
[54] Parvinen, Exh. No. MPP-1HCT at 16:19 – 20:6.

litigation, and then compare that to the proceeds PSE actually received. If PSE would have achieved less from REC sales absent the litigation, then it is fair to attribute that excess in REC proceeds to the litigation, and the California Receivable. On the other hand, if PSE would have achieved the same or more REC proceeds absent the litigation, that shows PSE simply received no more than what it would have achieved if it sold the RECs in the open market. In that scenario, there is no reason to reward PSE for doing what it otherwise could have done.

46 Instead of concrete facts, PSE tried to shift the burden of proof to other parties to show PSE would have received more in REC proceeds absent the settlement.[55] Obviously, that attempt must fail, because PSE bears the burden of proof in this proceeding.

47 PSE also tried statements such as the California Receivable litigation "led to agreements" to sell the RECs; that this "significantly increased" the REC proceeds;[56] and without the litigation, the REC sales "would not have occurred."[57] While these are conclusions, not facts, they do not hold water anyway, because the evidence shows the REC sales prices at issue are independent of the California Receivable litigation.

a. The auction process

48 The structure of the settlement negotiations exemplifies this separation of the REC prices from the litigation. In fact, [redacted] provides ample evidence for_the Commission to conclude that PSE's REC sales transactions were at market prices, and thus, there is no justification to award PSE a compensated write-off of the California Receivable using REC proceeds.

---

[55] De Boer, Exh. No. TAD-16C, second to last paragraph: [redacted]

[56] De Boer, Exh. No. TAD-1T at 2:11-17.

[57] De Boer, Exh. No. TAD-1T at 7:14 – 8:3.

49 [redacted][58] [redacted][59] [redacted][60]

50 [redacted][61] As for PG&E, PSE testified that "settlement of the California Litigation was not contingent upon a completed agreement for the sale of RECs to [PG&E] …"[62] Because of that, PG&E had a strong incentive to pay no more than market price for the RECs. [redacted][63] [redacted]

b. The public filings before the California Public Utilities Commission

51 The publicly available records also confirm that PSE's REC sales were at market prices. As Mr. Schoenbeck carefully documented, PG&E and SCE confirmed in pleadings

[58] De Boer, Exh. No. TAD-3HCT at 8:12-20; TR. 121:4-10; and Norwood, Exh. No. SN-14HC at 2-3.
[59] TR. 173:14-22.
[60] De Boer, TR. 173:14-22; TR. 124:14-25.
[61] De Boer, TR. 177:3-9; TR. 125:4-7.
[62] De Boer, Exh. No. TAD-1T at 7:3-11. SCE, PG&E and San Diego Gas & Electric were the investor-owned utilities in the litigation. De Boer, TR. 121:4-13.
[63] *See* De Boer, TR 174:24 – 175:7.

filed before the California Public Utility Commission (CPUC) that they paid no more than market price for PSE's RECs.[64]

52 For example, SCE ([redacted]) specifically represented to the CPUC that SCE's REC purchase was a market transaction: "The Puget [REC] Contract's pricing is not dependent on the Settlement Agreement and SCE would have chosen to enter into the Puget Contract independent of the Settlement Agreement."[65]

53 Notably, the CPUC determined the reasonableness of the settlement of the California Receivable litigation [redacted][66] In doing so, the CPUC issued resolutions specifically finding that these California utilities paid a fair market price for the RECs.[67]

54 This substantial, unambiguous evidence proves there is no nexus between the litigation and the amount of REC sales proceeds PSE achieved sufficient to justify the Commission awarding PSE a write-off of the California Receivable at ratepayers' expense.

55 Not only does PSE not challenge the veracity of the foregoing evidence, [redacted][68] but then promptly tries to explain it away, by inviting the Commission to simply chalk it all up to [redacted][69] The Commission should politely decline PSE's invitation.

---

[64] Schoenbeck, Exh. No. DWS-1T at 7:22 – 9:4 and Exh. Nos. DWS-6 through DWS-14 cited therein.
[65] Exh. No. DWS-8 at 3, first new paragraph.
[66] De Boer, TR. 145:5-12; TR. 164:6-10.
[67] **For SCE**: Schoenbeck, Exh. No. DWS-13, CPUC Resolution E-4244 at 17 (June 18, 2009) ("SCE's analysis demonstrates that the Puget contract is reasonable as compared to its 2008 shortlist [etc.]"); and Schoenbeck, Exh. No. DWS-12, CPUC Resolution E-4300 at 10 (December 17, 2009) ("The total expected costs of the PPA, as estimated by SCE, are reasonable based on their relation to bids received in response to SCE's solicitation"); **For PG&E**: Schoenbeck, Exh. No. DWS-14, CPUC Resolution E-4278 at 11 (October 15, 2009) ("PG&E determined that the PPA is reasonable relative to proposals received in response to PG&E's 2008 solicitation because the PPA's market valuation compares favorably with bids from its 2008 solicitation").
[68] De Boer, Exh. No. TAD-23HC; TR. 142:11-23; TR. 144:25-145:4.
[69] De Boer, TR. 171:1-15.

56 Take, for example, Resolution E-4728,[70] where the CPUC evaluated the evidence PG&E submitted to support the reasonableness of the amount PG&E paid PSE for RECs. This factual support included a "least-cost, best-fit bid evaluation" which contained a "determination of the bid's market value," and a comparison to PGE's 2008 resource solicitation.[71] This reflects principled, substantial evidence-based decision-making by the CPUC, not [redacted][72]

c. PSE's own REC price information

57 With all of the foregoing evidence against it, PSE is left with the unenviable task of trying to defend its position with insufficient evidence, consisting of its own bids and transactions. PSE does so by repeatedly and simplistically referencing the [redacted][73] The Commission should emphatically agree with PSE that this [redacted][74] [redacted]

---

[70] Schoenbeck, Exh. No. DWS-14.
[71] Schoenbeck, Exh. No. DWS-14, CPUC Resolution E-4278 at 11 (October 15, 2009).
[72] The Commission also will note that the CPUC resolution regarding the PG&E REC transaction was contested by the Division of Ratepayer Advocates (DRA), which claimed PG&E paid too much for the RECs. Schoenbeck, Exh. No. DWS-14, CPUC Resolution E-4278 at 8 (October 15, 2009) (The Division of Ratepayer Advocates (DRA) protested that "[t]he price of the renewable or green attribute is too high."). If the evidence supporting a fair market price for the RECs PG&E purchased was insubstantial, the DRA could have sought judicial review; DRA did not seek judicial review.
[73] E.g., De Boer, Exh. No. TAD-3HCT at 7-10; TR. 144:17-24; TR. 180:1-12; TR. 185:22-25; TR. 186:1-17.
[74] De Boer, TR. 180:10-16.

[redacted][75]

58 [redacted][76] [redacted]

59 Put another way, a deficiency in the record regarding the market price for RECs is PSE's responsibility, not the Commission's, the Staff's or that of any other party or entity. On this record, PSE simply has not borne its burden of proving it is entitled to a compensated write-off of the California Receivable using REC proceeds.[77]

3. If the Commission awards PSE a compensated write-off of the California Receivable, the Commission should offset any such compensation by the amount of litigation expenses ratepayers have already paid

60 If the Commission decides that shareholders deserve some amount of REC and CFI proceeds, the Commission should offset that amount by \$4.6 million. This is the amount of PSE's outside legal fees for litigating the California Receivable; litigation that arose from

[75] De Boer, TR. 187:13-20.
[76] De Boer, TR. 187:10-11.
[77] Of course, even if PSE could prevail on this aspect of the issue, the Commission still should not direct any REC and CFI proceeds to shareholders because of the rate plan, which we discussed in ¶¶ 40-43, supra.

rate plan era transactions.[78] This offset will credit ratepayers for the $4.6 million in litigation costs by which they already have been unfairly burdened.[79]

61 As we have explained, the litigated power sales transactions at issue here occurred when PSE was enjoying a rate plan under which it bore all the risks and earned all the benefits of these sorts of transactions.[80] Yet, according to PSE, these ongoing litigation costs are simply "regular operations costs and, as such, are included in rates."[81] PSE is wrong. There is no apparent defensible basis for having ratepayers fund litigation arising from, and based on conduct exclusive to, the rate plan era.

62 A review of the Commission's rate orders since 2001 shows that no one raised the issue whether PSE's California Receivable litigation legal fees are recoverable in rates. Surely, there is no basis now for the Commission to let shareholders enjoy even more ratepayer dollars related to these rate plan era transactions.

63 PSE's shareholders cannot have their cake and eat it, too, i.e., enjoy the benefit of a compensated write-off of the California Receivable, plus the benefit of having ratepayers fully fund PSE's outside legal fees for litigation related to that receivable. If the Commission grants PSE an exclusive share of REC proceeds, the Commission should reduce that amount by $4.6 million.

C. Low Income Ratepayers Are Not Entitled To an Exclusive Share of REC Proceeds to Fund Special Low Income Programs

64 PSE and the low income advocates want up to 20 percent of REC money (minimum of $10 million; maximum of $20 million) to solve two problems they apparently are unable

[78] Schoenbeck, Exh. No. DWS-15, Attachment A, last column, "Total" line; De Boer, TR. 183:19-25; TR. 184:4-19.
[79] That figure is shown in Schoenbeck, Exh. No. DWS-15, last line, last column.
[80] *See* ¶¶ 40-43, supra.
[81] Schoenbeck, Exh. No. DWS-15, page 1, part b.

to solve under existing programs. The first problem they describe as "one of the greatest obstacles to making low income homes more efficient", i.e., the need to repair the housing structure before the energy efficiency measures are applied.[82]

65 They searched far and wide to find money to fund this program.[83] They now want to latch onto REC money because other funding sources are "inadequate," "diminishing," subject to competing claims, and on top of all that, no federal "stimulus money" is available.[84] Consequently, they want up to $16 million of REC money (80 percent of the 20 percent overall share of REC proceeds, capped at $16 million) to fund a new program to repair low income housing along with providing energy efficiency measures.

66 The second problem the low income advocates want to solve with REC dollars is to "[e]xpand the capacity of low income agencies to install and maintain" renewable energy systems, such as thermal hot water systems and photovoltaic systems.[85] To solve this problem, they want up to $4 million in REC money to acquire and install solar facilities on low income housing structures.

67 To get this $20 million in REC proceeds, the low income advocates want $10 million from PSE right away, by capturing REC money PSE currently has on hand, plus 20 percent of every new REC dollar that comes in, until they get another $10 million.[86]

68 Needless to say, there are considerable problems with these proposals.

---

[82] Amended Petition at 6-7, ¶ 15. The Panel similarly characterized this as a "bottleneck." Panel, TR. 82:11-18 (Sieg).
[83] According to the low income advocates, the programs currently unable to fulfill their needs include: Energy Matchmaker, HOME, Community Development Block Grants, the Weatherization Assistance Program (U.S. Dep't of Energy), and the American Recovery and Reinvestment Act. Panel, Exh. No. J-1T at 15-16.
[84] Panel, Exh. No. J-1T at 15:4 – 16:10.
[85] Amended Petition at 7, ¶ 16.
[86] Amended Petition at 6, ¶ 13 and at 7: ¶ 17.

1. Funding the proposed low income programs would constitute an undue preference; the "safe harbor" of RCW 80.28.068 does not apply

69 PSE is prohibited from giving preferential treatment to any customer class or group:

> No … electrical company … shall make or grant any undue preference or advantage to any person … or to any particular description of service in any respect whatsoever, or subject any person ... or any particular description of service to any undue or unreasonable prejudice or disadvantage in any respect whatsoever.[87]

70 As we explained earlier,[88] PSE and the low income advocates provide no reasonable, fact-based justification for giving PSE's low income customers a $20 million preference over other PSE customers. Therefore, we conclude their proposed funding of the low income programs would constitute an undue preference, in violation of RCW 80.28.090.

71 The ensuing legal issue is whether the low income proposals are nonetheless lawful under the "safe harbor" of RCW 80.28.068, which states:

> Upon request by an electrical or gas company, or other party to a general rate case hearing, the commission may approve rates, charges, service, and/or physical facilities at a discount for low income senior customers and low-income customers. Expenses and lost revenues as a result of these discounts shall be included in the company's cost of service and recovered in rates to other customers.

72 In their direct testimony, PSE and the low income advocates cite RCW 80.28.068 for the sole proposition that this is where "the Legislature has also demonstrated the importance of low-income energy assistance."[89] Consequently, it is not apparent whether they also rely on this section as authority for the Commission to approve their specific proposals in this docket, or not.

[87] RCW 80.28.090.
[88] *See* ¶¶ 32-38, supra.
[89] Panel, Exh. No. J-1T at 7:5-13.

73 What is apparent is that RCW 80.28.068 operates in a context other than this docket. For example, under that section, the context is a request by a party in a "general rate case hearing,"[90] for PSE to offer services and/or physical facilities to low income customers "at a discount," and where PSE collects the expenses and lost revenues related to the discount through the cost of service.

74 That is not the context here. This docket is not a "general rate case hearing;" there is no "discount"[91] from the price of other PSE services or facilities PSE provides; and the inclusion of expenses and lost revenues in PSE's cost of service has not been addressed, let alone accomplished.

75 Therefore, if approved, the low income proposal would constitute an undue preference in violation of RCW 80.28.090. The "safe harbor" of RCW 80.28.068 does not apply. However, should the Commission decide not to reach this legal issue, we next offer several other reasons why the Commission should reject the exclusive low income programs proposed in this case.

---

[90] The Legislature made a deliberate choice to limit low income discount requests to general rate case hearings. As originally enacted, RCW 80.28.068 authorized only the utility to request a low income discount. Laws of 1999, ch. 62, § 1 ("Upon request of an electrical or gas company …"). The Legislature amended that section in 2009. The original bill would have also authorized a low income discount request by "a party." S.B. 5290, § 1, 61st Leg., Reg. Sess. (Wash. 2009). However, that bill was amended to change "a party" to "a party *in a general rate case hearing*." S.S.B. 5290, § 1, 61st Leg., Reg. Sess. (Wash. 2009) (emphasis added). This is the version that was enacted. Laws of 2009, ch. 32, § 1.

[91] Given the context of RCW 80.28.068, the obvious meaning of "discount" is its plain meaning: a "reduction from the gross amount of value of anything … as … a reduction from the price made to a specific customer or class of customers." Webster's Third New Int'l Dictionary (1968) at 646. Therefore, even if this docket were a general rate case hearing, RCW 80.28.068 would not apply because PSE and the low income advocates have proposed no discounts from anything.

2. PSE and the low income advocates base their case on "public interest" factors the Commission cannot consider

76 To justify their proposed low income programs, PSE and the low income advocates rely on a long list of what they call "public interest" factors,[92] including:

- "Preservation of the affordable housing stock";[93]
- "Expand[ing] the capacity of low income agencies to install and maintain small-scale renewable systems";[94]
- Developing "a skilled support network" for placing solar facilities on low income houses;[95]
- Having renewable energy "available to all economic strata";[96]
- Putting people to work "right away" making home repairs;[97] and
- "Enhanc[ing] the work of providers" who are implementing the federal Weatherization Assistance Program (WAP).[98]

77 The question[99] is not whether these "public interest" factors are important; they are. The question is not whether the Legislature could authorize the Commission to cure these problems. It clearly could. The question is whether the Legislature granted the Commission this authority. In fact, the Legislature did not empower the Commission to do these things.

---

[92] While the prepared testimony of PSE and the low income advocates recites these factors, Exh. Nos. J-9 and J-10 indicate PSE has not taken into account any of these factors in analyzing the cost-effectiveness of any conservation measure. However, in those exhibits, PSE stated it could take such factors into account. Staff asked what statute PSE relied on for that statement. PSE responded that it had not reviewed the statutes sufficiently to determine whether such considerations were legally justified. Exh. No. J-10 at 1, last paragraph.
[93] Panel, Exh. No. J-1T at 18:10-11.
[94] Panel, Exh. No. J-1T at 10:5-6.
[95] Panel, Exh. No. J-1T at 10:7.
[96] Panel, Exh. No. J-1T at 18:20-21; Panel, TR. 102:5-9 (Gravatt).
[97] Panel, Exh. No. J-1T at 18:15-16.
[98] Panel, Exh. No. J-1T at 19:8-11. The Panel explains the "WAP" acronym in Exh. No. J-1T at 15:18-19.
[99] This paragraph paraphrases the issue statement of the United States Supreme Court in *Nat'l Assoc. for the Advancement of Colored People v. Fed. Power Comm'n,* 425 U.S. 662, 665, 98 S. Ct. 1806, 48 L. Ed 2d 284 (1976). In that case, the Court held that the Federal Power Commission (FPC) was not statutorily empowered to combat employment discrimination by prescribing utility employment policies and adjudicating violations of those policies.

78 As the court stated in *Jewell v. Utilities and Transportation Commission,* 90 Wn.2d 775, 777, 585 P.2d 1167 (1978), "the commission is not the keeper of the social conscience of the citizens of this state." Rather, the Commission's charge is to regulate "in the public interest, *as provided by the public service laws*",[100] and it is clear that Title 80 is the source for the "public interest."[101]

79 For example, in *Cole v. Utilities & Transportation Commission,* 79 Wn.2d 302, 485 P.2d 71 (1971), the court upheld the Commission's decision to disallow intervention in a natural gas proceeding to competing unregulated fuel oil dealers. The court observed: "[The fuel oil dealers] fail to point out any section of Title 80 that suggests that non-regulated oil dealers are within the jurisdictional concern of the commission."[102] The court went on to conclude that "the commission correctly determined that it has no authority to consider the effect of a regulated utility upon an unregulated business."[103]

80 Another case in which the court distinguished the public interest associated with Commission action from other public interests is *Washington Independent Telephone Association v. Telecommunications Ratepayers Association for Cost-Based and Equitable Rates,* 75 Wn. App. 356, 880 P.2d 50 (1994) (*WITA*). In that case, the court affirmed a superior court order that reversed a Commission decision to create the Community Calling Fund (CCF). The court noted that the challenger (TRACER) "does not contest that the CCF

---

[100] RCW 80.01.040(2) (emphasis supplied).
[101] This is not to say the Legislature cannot charge the Commission with statutory duties outside the four corners of Title 80. For example, the Commission must adhere to RCW 34.05, the Administrative Procedure Act, because the Legislature includes the Commission within the scope of that chapter. Other examples are RCW 42.21C (the State Environmental Policy Act) and RCW 54.48 (under which the Legislature provides the Commission a limited regulatory to approve boundary agreements between Commission-regulated electrical companies and non-regulated electrical cooperatives). By the terms of these statutes, they apply directly to the Commission. This is different from the approach of PSE and the low income advocates, which is to rely on statutes and other policies that do not apply to the Commission.
[102] 79 Wn.2d at 306.
[103] Id.

is in the public interest, but it correctly observes that the CCF is not authorized by the public service laws."[104]

81 In other words, the issue is not how many public interest factors PSE and the low income advocates can muster, but whether the Commission is empowered to consider them in the first place. As a matter of law, the Commission cannot consider the principal factors upon which PSE and the low income advocates rely.

82 This fundamental flaw in their presentation is further showcased in their reliance on programs from other states: Oregon's net metering program; the California Solar Initiative; and Montana's System Benefits charge.[105]

83 It is true these programs generate funds for low income programs, and two of these programs (the California Solar Initiative and the Montana System Benefits charge) grant low income customers exclusive shares of overall program funding. However, the critical fact ignored by PSE and the low income advocates is that each of these programs is created and administered pursuant to an explicit grant of statutory authority:

- Oregon's net metering statute authorizes the use of excess energy credits for low income energy assistance (among other things);[106]
- The California Solar Initiative was launched by two decisions of the California Public Utility Commission (CPUC) pursuant to a statute requiring the CPUC to create incentives for renewables and other distributed

---

[104] 75 Wn.2d at 368.
[105] Panel, Exh. No. J-1 at 11:14 – 12:6.
[106] OR. REV. STAT. § 757.300(3)(d): "...any remaining unused kilowatt-hour credit accumulated during the previous year shall be granted to the electric utility for distribution to customers enrolled in the electric utility's low-income assistance programs, credited to the customer-generator or dedicated for other use as determined by the commission, for a public utility, ... following notice and opportunity for public comment."

generation resources.[107] The California Legislature promptly endorsed the Solar Initiative,[108] and mandated that a minimum 10 percent of total Solar Initiative funding be used to benefit low income customers.[109]

- Montana's "System Benefits" statute mandates that a minimum 17 percent share of total program funding be used for low income weatherization assistance.[110]

84 The Commission enjoys no similar statutory authority to create a comparable, exclusive fund to benefit low income customers.

85 To be sure, PSE and the low income advocates itemize a few benefits their new programs might have to PSE in its capacity as a regulated electric utility, though this is not a focus of their presentation. For example, they offer generalized claims that these programs will make PSE's generation and distribution system more efficient and reliable,[111] and even

---

[107] In these decisions, the CPUC cited various statutes, including California Public Utility Code § 399.15(b), Paragraphs 4-7, now codified as § 397.15(b)(4) – (7). Subparagraph s (6) & (7) respectively require the CPUC to implement "incentives for … distributed generation" and "differential incentives for renewable or super clean distributed generation resources." *See* CPUC Rulemaking Docket 04-03-107, *Order Instituting Rulemaking Regarding Policies, Procedures and incentives for Distributed Generation and Distributed Energy Resources*, Decision 05-12-044, *Interim Order Adopting Policies and Funding for the California Solar Initiative* (December 15, 2005) at 6 and Decision 06-01-024, *Interim Order Adopting Policies and Funding for the California Solar Initiative* (January 12, 2006) at 3-4. (Among other statutory support, these decisions reference "AB 970" (Assembly Bill 970), which initially was codified California Public Utility Code § 399.15 (it is now codified as §397.15), and "AB-1890," which was California's 1996 electric industry restructuring legislation. That statute contained a $540 million program for renewables).

[108] E.g., CAL. PUB. UTIL. CODE § 2851(a) (refers to the CPUC "implementing the California Solar Initiative," and prescribes implementation standards and funding limits for that implementation).

[109] CAL. PUB. UTIL. CODE § 2851(4)(c)(1): "The commission shall assure that not less than 10 percent of the funds for the California Solar Initiative are utilized for the installation of solar energy systems on low-income residential housing. Notwithstanding any other law, the commission may modify the monetary incentives made available pursuant to the California Solar Initiative to accommodate the limited financial resources of low-income residential housing."

[110] MONT. CODE § 69-8-402(1): "Universal system benefits programs are established for the state of Montana to ensure continued funding of and new expenditures for energy conservation, renewable resource projects and applications, and low-income energy assistance"; MONT. CODE § 69-8-402(5): "A utility's minimum annual funding requirement for low-income energy assistance and weatherization assistance is established at 17 percent of the utility's annual universal system benefits funding level and is inclusive within the overall universal system benefits funding level."

[111] Panel, Exh. No. J-1T at 19:1-5 and TR. 92:7-14 (Gravatt).

reduce peak and capacity demand.[112] However, there is no showing these considerations confer $20 million of benefits to PSE ratepayers as a whole. In fact, when Staff asked PSE to support these claims by quantifying these and similar alleged impacts on PSE as a regulated utility, PSE failed to provide that support.[113] All of this leaves the Commission only to guess what the exact nature and magnitude of these benefits might be. In any event, to the extent these factors apply, PSE already should have considered them in the cost-effectiveness analysis. As we explain later,[114] that analysis comes up short. The Commission deserves better.

86 The Commission should be faithful to the *Cole* and *WITA* cases and rule that the public service laws under which the Commission regulates simply do not contain "public interest" factors such as preserving affordable housing, improving the quality of services offered by unregulated low income agencies, enhancing federal programs in which the Commission has no role, or putting people to work repairing deficient housing structures. Because none of these factors are within the jurisdictional concern of the Commission, the Commission should not and cannot consider them.

3. RCW 70.164 does not apply to the Commission

87 PSE and the low income advocates also want the Commission to rely on "policy direction" from RCW 70.164.[115] However, like almost all of the "public interest" factors we just discussed, this statute provides no basis for Commission action, either, because the Legislature did not "direct" any policy to the Commission.

[112] Panel, Exh. No. J-1T at 19:1-5.
[113] Panel, Exh. No. J-11. In this data request, Staff specifically asked for this information because "[w]e wish to consider the impact of the proposed programs on each of the foregoing elements." Exh. No. J-11, second paragraph, last sentence. The lack of responsive information renders the record lacking in any details regarding the actual impact of the proposed low income programs on reducing peak demand, improved system reliability, etc., and whether such benefits are worth $20 million.
[114] *See* ¶¶ 90-94, infra.
[115] Panel, Exh. No. J-1T at 5:17-7:21.

88 For example, in the last paragraph of RCW 70.164.010 (the only part of that section which PSE and the low income advocates fail to quote in their direct testimony at page 6), the Legislature states: "The program implementing the policy of this chapter is necessary to support the poor and infirm and also to benefit the health, safety and general welfare of all citizens of this state." Obviously, the Legislature is giving "policy direction" only to the Department of Commerce, the agency the Legislature charged with implementing and administering the program referenced in that section.[116] Put another way, in RCW 70.164, the Legislature did not direct the Commission to do anything.

89 PSE and the low income advocates have tied their boat to the wrong dock. If they want to foster the legislative policy embodied in RCW 70.164.010, or advance such public interests as affordable housing and other matters the Commission does not regulate, their recourse is to the Legislature, not to REC proceeds.

4. The proposed low income programs are not cost-effective

90 Staff raised the issue whether the proposed low income programs are cost-effective,[117] but it may not be necessary for the Commission to resolve that issue. The Commission could first assume the proposed programs are indeed cost-effective. Under that assumption, PSE likely will acquire the conservation without REC proceeds, pursuant to PSE's statutory obligation under RCW 19.285.040(1) to "acquire all available conservation that is cost-effective, reliable and feasible." In that circumstance, the Commission should

[116] RCW 70.164.030 establishes the "Low Income Weatherization Assistance Account" to be administered by "the department," per RCW 70.164.040 et al. "Department" means the Department of Commerce. RCW 70.164.020(1). The Commission is not mentioned in RCW 70.164, either by name or by way of a general reference to all state agencies, for example.
[117] Parvinen, Exh. No. MPP-1HCT at 11:19 – 13:7.

reject the proposed low income programs, because there would be no reason for the Commission to use REC money to fund what PSE would otherwise do.[118]

91 Then, the Commission could assume the proposed programs are not cost-effective. In that circumstance, the Commission should also reject the low income proposal, because using REC proceeds to fund non-cost-effective conservation is an inappropriate, wasteful use of precious ratepayer dollars. Either way, the Commission would reject the use of REC proceeds for the proposed programs, without resolving the cost-effectiveness issue. Nonetheless, we will address that issue.

92 Under PSE's tariff, a conservation measure must pass the total resource test [TRC test] and the utility cost test [UC test].[119] PSE may only consider "non-energy benefits" under the TRC test.[120] Consequently, with a .94 benefit/cost ratio,[121] the proposed low income programs fail the UC test and therefore, they are not cost-effective.[122]

93 The Panel confirmed the proposed low income renewable program is not cost effective: "There is no cost-effectiveness test that I know of that is applied to solar installations" because solar facilities "have above market costs."[123] The record shows this testimony to be somewhat of an understatement. According to the Panel, the proposed low income solar program contemplates a cost of $7 per watt,[124] for a whopping $7,000 per

---

[118] In Panel Exh. No. J-12, last page, paragraph (a), PSE suggests only conservation it will pursue under the mandate in RCW 19.285.040(1) is conservation the Commission approves. If the Commission might approve the proposed low income programs in compliance with the statutory mandate, it would be premature for the Commission to fund those programs using REC proceeds now. If the Commission would not approve the proposed low income programs under the statutory mandate because they are not cost effective, then the Commission should not use REC proceeds for that purpose.
[119] Panel, Exh. No. J-8 at 5, PSE Tariff G, Schedule 83, ¶ 7: "a Measure must reasonably be expected to satisfy the Total resource Cost Test and the Utility Cost Test." *See also,* Parvinen, TR. 204:15-24.
[120] Panel, Exh. No. J-8 at 3 and the page after 3 (which is unmarked), PSE Tariff G, Schedule 83, ¶¶ 4p and 4aa.
[121] Panel, Exh. No. J-4.
[122] Parvinen, TR. 204:15 – 205:13.
[123] Panel, TR. 79:14-17 (Gravatt).
[124] Panel, TR. 90:12-18 (Gravatt).

megawatt.[125] As Commissioner Oshie observed, if the facilities contemplated by the low income renewable program were cost-effective today, "almost everybody would have one on their roof . . . ."[126]

94 The proposed low income programs are not cost-effective, and for that reason alone, the Commission should not authorize the use of REC proceeds to fund them.

5. The proposed low income programs fail the "benefit should follow burden" principle

95 Assuming the low income advocates can surmount each of the foregoing hurdles,[127] the Commission is still left with the gaping hole in PSE and the low income advocates' case: There is no evidence that low income customers are burdened any differently than other customers with regard to these resources. As Staff put it, the proposed $20 million low income programs do not provide commensurate benefits to other PSE customers.[128] Consequently, low income customers are not entitled to an exclusive $20 million benefit in the form of their proposed low income programs.

96 Nor have the low income advocates provided any justification why they should receive immediately $10 million of REC proceeds currently in PSE's hands, plus a 20 percent claim on each subsequent REC dollar as it comes in (capped at an additional $10 million). As ICNU demonstrated, all by itself, this "up front" payment featured in their proposal visits a significant economic disadvantage upon other PSE customers.[129]

97 In the end, because all PSE retail customers pay rates designed to recover all costs of these resources, all such customers should get REC benefits in a commensurate manner.

---

[125] Parvinen, TR. 207:1-5. We apologize for our arithmetic failure at TR 206:6-7; it was getting late.
[126] TR 79:2-5.
[127] *See* ¶¶ 69-94, supra.
[128] Parvinen, Exh. No. MPP-1HCT at 12:14-16.
[129] Schoenbeck, Exh. No. DWS-1HCT at 6:5-12.

Giving $20 million to one group of customers to the exclusion of all others would violate the "benefit should follow burden" principle in every respect.[130]

D. The Commission Should Adopt Staff's Regulatory Liability Method to Distribute REC and CFI Proceeds to Ratepayers

98 Staff proposes the Regulatory Liability method as an equitable means to implement Staff's recommendation that the Commission provide REC and CFI proceeds to all ratepayers.[131] As Staff explained, the Regulatory Liability method matches the goal that REC and CFI revenues should be returned to the ratepayers who pay rates to cover all of the costs of the related resources, in the same manner in which rate classes are assigned cost responsibility for those resources.[132] The mechanics of this method are acceptable to PSE.[133]

99 Under the Regulatory Liability method, PSE will book the REC and CFI proceeds in a regulatory liability account, which will be used to reduce PSE's rate base for ratemaking purposes. PSE would amortize the balance in the account over ten years, to give customers a long-term benefit of the unamortized balance.[134] This method is substantially the same accounting treatment the Commission approved in Docket UE-001157,[135] which involved revenues from PSE's sales of excess sulfur dioxide emissions credits, which are similar to CFIs.[136]

---

[130] Parvinen, Exh. No. MPP-1HCT at 11:17-18.
[131] Kroger also proposes a regulatory liability method. Higgins, Exh. No. KCH-1T at 9:4-6. Kroger suggestion of a rolling, three-year amortization is not substantially different from Staff's proposal.
[132] Parvinen, Exh. No. MPP-1HCT at 8:15-23.
[133] De Boer, Exh. No. TAD-3HCT at 19:13-19; TR. 110:1-17.
[134] Parvinen, Exh. No. MPP-1HCT at 3:14-4:18 and at 9:4-5.
[135] *In re Petition of Puget Sound Energy Inc., for an Order Regarding Authorization to Sell Sulfur Dioxide Emissions Allowances and an Associated Accounting Order,* Docket UE-001157, Order at 2 (October 25, 2000); Parvinen, Exh. No. MPP-1HCT at 20:1-6.
[136] Parvinen, Exh. No. MPP-1HCT at 20:3.

100 Staff's proposed method is the same in concept as the method PSE has proposed for returning REC and CFI revenues to ratepayers, i.e., using REC proceeds to reduce PSE's Storm Damage regulatory asset.[137] However, as Staff explained, in setting rates, the Commission does not allocate the Storm Damage account in the same manner as it allocates the resources that generate the REC and CFI proceeds.[138] The result of PSE's selection of the Storm Damage account is a "mismatch [that] creates disproportionate shares of the REC/CFI benefits among customer classes."[139]

101 Staff considered a direct refund approach, which could be accomplished via a rate credit, or as an immediate rate base reduction of the sort proposed by Public Counsel for the REC and CFI revenues currently on PSE's books.[140] This approach is conceptually sound, in terms of returning the REC benefits to customers in the same way customers pay for the underlying resources. However, it provides only short term benefits and produces rate instability, evidenced by a likely rate increase as the credit expires.[141]

102 In sum, the Commission should accept Staff's proposed Regulatory Liability method as the means to return REC and CFI revenues to ratepayers. First, it is conceptually sound, and the amortization period more closely matches the period the benefits will accrue. Second, it is a workable method, evidenced by the fact that it is being used by PSE today for revenues from PSE's sales of excess sulfur dioxide emissions credits. Finally, unlike the direct refund approach, the Staff's proposed method also provides long-term benefits and stable rates, and it does not result in a rate increase when the REC monies are used up.

---

[137] Parvinen, Exh. No. MPP-1HCT at 18:10-22.
[138] Parvinen, Exh. No. MPP-1HCT at 19:6-9.
[139] Parvinen, Exh. No. MPP-1HCT at 19:8-10.
[140] *See* Norwood, Exh. No. SN-1HCT at 4:7-14.
[141] Parvinen, Exh. No. MPP-1HCT at 9:8-23; *see also* De Boer, Exh. No. TAD-1T at 10:3-7.

E. The Commission Need Not Order Additional REC Reporting by PSE

103 Public Counsel recommends the Commission require PSE to file reports on RECs in the same manner as PacifiCorp.[142] The Commission should not adopt this recommendation because the accounting for PSE's RECs in the Amended Petition should address any reporting concerns. Moreover, as PSE correctly points out, in whatever manner the Commission decides to distribute REC proceeds, PSE filings will be required,[143] and appropriate mechanisms are in place to allow Staff and others to scrutinize those filings. Should a need for further information arise in the future, the Commission can require reporting at that time.[144]

IV. CONCLUSION

104 Many cases before the Commission present perplexing and complex issues. In most respects, this case is not one of them. In this case, the right choice is the obvious one: Provide REC money to the ratepayers in the same manner the Commission sets the rates for PSE to recover the costs of the resources that generated the RECs in the first place. No more, but certainly no less.

105 For the reasons stated in this brief, the Commission should return the REC proceeds to all ratepayers by requiring PSE to: (1) Book the net proceeds from the sale of RECs and

//

//

//

142 Norwood, Exh. No. SN-1HCT at 25:9-20.
143 De Boer, Exh. No. TAD-3HCT at 20:9-12.
144 RCW 80.04.210.

CFIs in a regulatory liability account; (2) Use that account to reduce rate base; and (3) Amortize the balance in the account over a period of 10 years.

Dated this 17th day of March 2010.

Respectfully submitted,

ROBERT M. MCKENNA
Attorney General

DONALD T. TROTTER
Assistant Attorney General
Counsel for Washington Utilities and
Transportation Commission Staff

BEFORE THE WASHINGTON UTILITIES AND TRANSPORTATION COMMISSION

WASHINGTON STATE ATTORNEY GENERAL'S OFFICE AND THE INDUSTRIAL CUSTOMERS OF NORTHWEST UTILITIES, Joint Complainants, v. PACIFICORP d/b/a PACIFIC POWER & LIGHT CORP. Respondents	DOCKET NO. UE-110070 RESPONSE OF BEHALF OF COMMISSION STAFF TO PACIFICORP'S MOTION TO DISMISS COMPLAINT

I. THE COMPLAINT

1 The "Joint Complaint of ICNU and Public Counsel" (Complaint) alleges the rates the Commission set in Docket UE-090205 (*2009 GRC*) are excessive.[1] ICNU/Public Counsel say the reason those rates are excessive is because in that prior docket, the Company allegedly failed to supplement data responses,[2] provided inaccurate data request responses,[3] and proposed an improper pro forma adjustment.[4]

II. RESPONSE TO PACIFICORP'S MOTION TO DISMISS

2 PacifiCorp's Motion to Dismiss raises several arguments, to which Staff responds as follows:

[1] E.g., The Complaint alleges "excessive" charges (Complaint at 5, ¶ 6) and "unreasonable rates" (id. at 4, ¶ 4), and relies on the reparations statute (id. at 3, ¶ 2 & at 13, ¶ 25).
[2] Joint Complaint at 12-13, ¶ 24.
[3] Joint Complaint at 10-12, ¶¶ 21-23.
[4] Joint Complaint at 9-10, ¶¶ 19-20, plus the un-numbered paragraph after ¶ 20.

A. The Commission Should Grant PacifiCorp's Motion as to RCW 80.04.230

3 PacifiCorp correctly argues that ICNU/Public Counsel are not entitled to relief under RCW 80.04.230 because that section applies only to charges in excess of the lawful (i.e., published) rate.[5] The Complaint fails to allege PacifiCorp charged a rate other than the filed tariff rate, so the Commission should dismiss the claim for relief under RCW 80.04.230.

B. PacifiCorp is Correct in its Legal Analysis of the Limitations Period in RCW 80.04.230; Applying the Law to the Facts is Difficult

4 PacifiCorp argues the Commission should dismiss the Complaint because RCW 80.04.240 sets a six-month limitation period for filing an unreasonable rates claim, and ICNU and Public Counsel were aware of the facts underlying their claim, or should have been aware of those facts, more than six months before they filed the Complaint.[6]

5 Staff agrees with PacifiCorp's legal analysis, i.e., a six-month limitation period applies; and it runs from the date ICNU and Public Counsel reasonably should have known about the REC information in controversy. More difficult is the factual question: when did ICNU or Public Counsel know, or when should they reasonably have known about the REC information in controversy?

6 PacifiCorp says the REC information in controversy was contained in its April 30, 2010, Commission-basis report.[7] However, no one has a duty to audit that report (which runs several hundred pages[8]) in an attempt to discern that information.

7 However, PacifiCorp is correct that its direct evidence in the *2009 GRC* (filed May 4, 2010) showed significantly higher REC revenues for the calendar year 2009 test year than were contained in the settlement filed and approved in that case.[9]

---

[5] PacifiCorp Motion at 16, ¶ 42-43.
[6] PacifiCorp Motion at 11-16, ¶¶ 30-41.
[7] PacifiCorp Motion at 10, ¶ 27.
[8] PacifiCorp fails to tell us where in that two inch thick document we might find the REC information at issue.

8 PacifiCorp also argues the Commission should impute knowledge to the Public Counsel Section of the Washington Attorney General's Office based on information allegedly known to the Utah Office of Consumer Services,[10] but that is obviously wrong because those are two entirely different entities. Also wrong is PacifiCorp's attempt to impute to ICNU the knowledge Mr. Falkenburg may have had available to him when he appeared for someone else in Utah.[11] On the other hand, it may be fair to impute to ICNU knowledge acquired by Mr. Falkenburg during his work for ICNU in Oregon.[12]

9 Despite the foregoing comments, Staff does not have the benefit of ICNU/Public Counsel's view of these matters. We trust the Commission will carefully consider their view in reaching a decision whether the Complaint is untimely.

C. The Commission Should Deny PacifiCorp's Motion Regarding the Request to Amend the Commission's Order in the *2009 GRC*

10 PacifiCorp argues the Commission should dismiss the Complaint to the extent it seeks to amend the Commission's order in the *2009 GRC*, and the Company offers three reasons why amending that order would be bad policy.[13] However, PacifiCorp has not sustained its burden to show there is no set of facts under which the Commission could apply a different policy, the same policy differently, or is otherwise powerless to amend that order. Therefore, the Commission should deny the Motion on this issue.[14]

11 PacifiCorp goes on to make a formalistic point that a request to amend an order is distinct from a complaint,[15] and then uses that point to argue that ICNU/Public Counsel's alternative

---

[9] PacifiCorp Motion at 14, ¶ 39.
[10] PacifiCorp Motion at 8, ¶ 23.
[11] PacifiCorp Motion at 8-9, ¶ 24.
[12] PacifiCorp Motion at 9, ¶ 25.
[13] PacifiCorp Motion at 16-19, ¶¶ 44-49.
[14] Staff agrees with PacifiCorp that the soon to be issued Commission final order in the current rate case, Docket UE-100749, likely will moot this particular claim for relief. Still, that is an argument for a later day.
[15] PacifiCorp Motion at 17, ¶ 45.

request to amend the Commission's order in the *2009 GRC* must be an improper collateral attack on that order.[16] The Commission should elevate substance over form and reject this argument because the Commission construes pleadings liberally,[17] the issue here is notice, and PacifiCorp has notice.

D. The Commission Should Grant PacifiCorp's Motion to Dismiss Claims for Violations of Commission Statutes and Rules Because Those Violations Are Irrelevant to an Excessive Rates Claim

12 PacifiCorp asks the Commission to dismiss on their merits the claims in the Complaint alleging violations of specific rules regarding pro forma adjustments, accuracy of data request responses, and the obligation to supplement data request responses.[18] The Company makes various factual and legal arguments, and we assume ICNU/Public Counsel will contest them. The more direct route is to dismiss these violations claims because they are irrelevant.

13 Evidence is relevant if it makes the existence of a fact "more probable or less probable than it would be without the evidence."[19] This case is an excessive rates complaint, and the issue is what rates are fair, just and reasonable, and by how much (if any) do the filed rates exceed those fair, just and reasonable rates. If PacifiCorp violated a rule, that does not make a particular level of rates more probable or less probable, nor does a rule violation make more or less probable the amount by which existing rates exceed reasonable rates.

14 Therefore, ICNU/Public Counsel's rule and statute violations claims are irrelevant and the Commission should dismiss them for that reason.

15 Staff observes at this juncture that it appears ICNU/Public Counsel intend to prove PacifiCorp's current rates are excessive based on an assumption that the settlement in the *2009*

[16] Id.
[17] WAC 480-09-395(4).
[18] PacifiCorp Motion at 19-23, ¶¶ 50-62.
[19] ER 401.

GRC would have been different had different facts earlier come to light.[20] If that is indeed the basis for their excessive rates claim,[21] ICNU/Public Counsel will not able to rely on that assumption; they will need to prove every other party would have exercised their discretion the same way and signed a different settlement, and the Commission would have exercised its discretion to approve it. Obviously, that is a very difficult (if not impossible) task.[22]

III. CONCLUSION

16 Should ICNU/Public Counsel's excessive rates claim survive PacifiCorp's Motion to Dismiss, the Commission should set a date for ICNU/Public Counsel to file their direct evidence supporting their claim for excessive rates. At that time, we will be able to discern whether ICNU/Public Counsel can make a *prima facie* showing of excessive rates.

DATED this 28th day of February 2011.

Respectfully submitted,

ROBERT M. MCKENNA
Attorney General

DONALD T. TROTTER
Assistant Attorney General
Counsel for Washington Utilities and
Transportation Commission Staff

[20] ICNU/Public Counsel identify a level of REC revenues and say the difference between that amount and $657,755 (the amount listed in the *2009 GRC* settlement) must be given back to ratepayers. Complaint at 4, ¶ 4, last sentence.
[21] As an alternative, ICNU/Public Counsel could make a rate case-type presentation demonstrating by how much the rates set in the *2009 GRC* exceed a fair and reasonable rate. However, the Complaint does not suggest a present intent or willingness to do that.
[22] We seriously doubt ICNU/Public Counsel can prove these discretionary acts would in fact have occurred, and that may be the subject of a future motion. For example, PacifiCorp simply could assert in good faith it would not have signed a settlement in the form ICNU/Public Counsel posit. In any event, we cannot conceive how ICNU/Public Counsel will prove what the Commission would have done had it been presented a different settlement on a different record, neither of which exist.

Exhibit No. KHB-1TC
Dockets UE-090704/UG-090705
Witness: Kathryn H. Breda
REDACTED VERSION

BEFORE THE WASHINGTON UTILITIES AND TRANSPORTATION COMMISSION

WASHINGTON UTILITIES AND TRANSPORTATION COMMISSION, **Complainant,** **v.** **PUGET SOUND ENERGY, INC.,** **Respondent.**	**DOCKET UE-090704** **DOCKET UG-090705** ***(Consolidated)***

TESTIMONY OF

KATHRYN H. BREDA

STAFF OF
WASHINGTON UTILITIES AND
TRANSPORTATION COMMISSION

Electric and Natural Gas Revenue Requirements; Company Accounting Proposal For Major Maintenance Activities; Ratemaking Adjustments for Power Cost O&M, and Major Plant Additions

November 17, 2009

CONFIDENTIAL PER PROTECTIVE ORDER

TABLE OF CONTENTS

LIST OF EXHIBITS

I. INTRODUCTION

Q. Please state your name and business address.

A. My name is Kathryn Breda. My business address is The Richard Hemstad Building, 1300 S. Evergreen Park Drive S.W., P.O. Box 47250, Olympia, WA 98504. My e-mail address is kbreda@wutc.wa.gov.

Q. By whom are you employed and in what capacity?

A. I am employed by the Washington Utilities and Transportation Commission ("Commission") as a Regulatory Analyst.

Q. How long have you been with this agency?

A. I have been employed by the Commission since 2008.

Q. Please state your educational and professional background?

A. I graduated from the University of Washington in 1980 receiving a Bachelor of Arts in Business Administration with a major in accounting. I am a licensed Certified Public Accountant in the State of Washington.

My responsibilities at the Commission generally comprise financial, accounting and other analyses in general rate cases, accounting petitions, other tariff filings, and compliance filings. I participated in the Staff review of PacifiCorp Dockets UE-080220 and UE-090205, and NW Natural Docket UG-080546. My responsibilities in these dockets included the review of major plant additions along with various other adjustments and accounting issues.

Prior to my employment with the Commission, I held various corporate accounting and regulatory management positions from 1980 through 2000 with Qwest Communication and Pacific Gas and Electric Company. My corporate accounting responsibilities included accounting policy and procedures, and internal and external reporting including SEC reporting. As a regulatory manager for Qwest Communications, I was responsible for regulatory accounting support for six jurisdictions, including revenue requirement in rate case filings and compliance reporting. I participated in internal state planning and review processes. I also analyzed and monitored state accounting issues, reviewed new accounting pronouncements, and proposed initial policy or practice for various accounting issues.

II. SCOPE AND SUMMARY OF TESTIMONY

Q. Please describe the purpose of your testimony.

A. In Sections III and IV of this testimony, I present Staff's overall recommendation regarding the electric and natural gas revenue requirements of Puget Sound Energy, Inc. ("PSE" or "the Company"). The starting point for all Staff witnesses for the development of these recommendations was the Company's Supplemental Testimony and Exhibits, filed September 28, 2009.

In Section V of my testimony, I present the Staff recommendation that the Commission reject the Company's proposed changes in accounting for planned major maintenance activities.

In Section VI, I sponsor several ratemaking adjustments recommended by Staff to develop the Company's electric revenue requirement. These adjustments address: 1) the operation and maintenance expense portion of Adjustment 10.03, Power Costs; and 2) major plant additions such as the Mint Farm Energy Center and the expansion of the Wild Horse Wind Farm.

Q. Please summarize Staff's overall revenue requirement recommendation in these consolidated electric and natural gas dockets.

A. Staff recommends that the Commission:

1. Increase the Company's electric service revenues by $ 5,826,516, or 0.3 percent, based on the overall rate of return of 7.89 percent recommended by Staff witness Parcell.
2. Increase the Company's gas service revenues by $ 7,130,348, or 0.6 percent, based on the same overall rate of return of 7.89 percent.

Q. Do you sponsor any exhibits in support of your recommendations?

A. Yes, I sponsor the following exhibits in support of my testimony:

- Exhibit No. KHB-2, Electric Results of Operations and Revenue Requirement

- Exhibit No. KHB-3, Gas Results of Operations and Revenue Requirement
- Exhibit No. KHB-4C, PSE Maintenance Under Long-Term Service Agreements From 2010 to 2015
- Exhibit No. KHB-5C, Maintenance Expense Comparison, Company Proposed Change Versus Current Accounting Method
- Exhibit No. KHB-6C, Comparison of Staff Versus Company Adjustment 10.03 Power Costs – Operations and Maintenance.

III. ELECTRIC REVENUE REQUIREMENT

Q. Please describe Exhibit KHB-2, Electric Results of Operations and Revenue Requirement.

A. Exhibit No. KHB-2 develops the Staff recommended revenue increase for the Company's electric operations. Page 1 of Exhibit No. KHB-2, the first column entitled "Actual Results of Operations," reflects the test year (January through December 2008) amounts and indicates that PSE earned a total rate of return of 6.51 percent on its electric operations in the test period. The second column entitled "Total Adjustments" is the sum of all the restating and pro forma adjustments shown on pages 2.2 through 2.7. The adjustment numbers used in my exhibit, and by all other Staff witnesses, correspond to PSE's presentation in its supplemental September 28, 2009 filing. The column entitled "Revenue Requirement Deficiency" shows the impact of Staff's recommended $ 5,826,516 electric revenue increase, given the 7.89 percent overall rate of return recommended by Staff witness Parcell.

Q. Are you responsible for all of the adjustments shown on Exhibit No. KHB-2?

A. No. On page 1 Exhibit No. MPP-2, Staff witness Parvinen lists each Staff witness and the contested and uncontested adjustments for which each witness is responsible.

Q. Did you review any adjustments on Exhibit No. KHB-2 that are uncontested as between Staff and PSE?

A. Yes. I sponsor Adjustment 10.13, Bad Debts, which is uncontested.

Q. Please list the adjustments on Exhibit No. KHB-2 that you sponsor that are contested as between Staff and the Company.

A. I sponsor the following contested adjustments, as discussed in Section VI of my testimony:

Adjustment 10.03, Power Cost – Operations and Maintenance Expenses Only
Adjustment 10.06, Hopkins Ridge Infill Project
Adjustment 10.07, Wild Horse Expansion Project*
Adjustment 10.08, Mint Farm Energy Center*
Adjustment 10.09, Sumas Cogeneration Station
Adjustment 10.10, Whitehorn Generating Station
Adjustment 10.11, Baker Hydroelectric Project Relicensing
Adjustment 10.31, Regulatory Assets
Adjustment 10.33, Fredonia Power Plant*

* Staff does not contest the prudence of these new generation resource additions, as explained by Staff witness Nightingale. Staff's challenge to these adjustments stems from other accounting issues that I explain in Section VI of my testimony.

Q. Does Staff agree with the Company's electric conversion factor of 0.621262?

A. Yes, the conversion factor used to convert electric net operating income to a revenue requirement level is appropriate and is not an issue.

IV. GAS REVENUE REQUIREMENT

Q. Please describe Exhibit No. KHB-3, Gas Results of Operations and Revenue Requirement.

A. Exhibit No. KHB-3 develops the Staff recommended increase in revenue for the Company's gas operations. Page 1 of Exhibit No. KHB-3, the first column entitled "Actual Results of Operations", reflects the test year (January through December 2008) amounts and indicates that PSE earned a total rate of return of 7.55 percent on its gas operations in the test period. The second column, entitled "Total Adjustments" is the sum of all the restating and pro forma adjustments shown on pages 3.2 through 3.5. The adjustment numbers correspond to PSE's presentation in its supplemental filing dated September 28, 2009. The column entitled "Revenue Requirement Deficiency" shows the impact of Staff's recommended $ 7,130,348 revenue increase, given the overall rate of return requirement of 7.89 percent recommended by Mr. Parcell.

Q. Did you review any adjustments on Exhibit No. KHB-2 that are uncontested as between Staff and PSE?

A. Yes. I sponsor Adjustment 9.08, Bad Debts, which is uncontested.

Q. Are you responsible for any of the contested adjustments included on Exhibit No. KHB-3?

A. No. On page 2 of Exhibit No. MPP-2, Staff witness Parvinen lists the other Staff witnesses and the contested and uncontested adjustments for which each is responsible.

Q. Does Staff agree with the Company's natural gas conversion factor of .621891?

A. Yes, the conversion factor used to convert natural gas net operating income to a revenue requirement level is appropriate and is not an issue.

V. COMPANY PROPOSED CHANGE IN ACCOUNTING FOR PLANNED MAJOR MAINTENANCE ACTIVITIES

Q. Please explain the Company's proposal to adopt a new method of accounting for planned major maintenance activities.

A. The Company states that it is required to change the way it accounts for major maintenance expense for ratemaking purposes because the method it *claims* to use, the "accrue-in-advance" method, is not allowed for financial reporting purposes. Exhibit No. JHS-1T at pages 12-13. The accrue-in-advance method has been disallowed for financial reporting purposes since 2006, but that has no bearing on how the Company accounts for major maintenance expense for ratemaking purposes.

The accounting method the Company actually currently uses to account for major maintenance is the "deferral method". Under the deferral method, major maintenance expense is amortized from completion of the maintenance event to the next occurrence of similar maintenance. For example, if major maintenance is completed in January 2010 and the next major maintenance is scheduled for January 2020, one tenth would be recorded as expense each year from 2010 through 2019. This method is an acceptable method under generally accepted accounting principles ("GAAP").

For rate making purposes, the Company proposes to abandon the deferral method of accounting and replace it with a "hybrid" self-developed method that is not required or suggested by any authority. PSE's proposal arbitrarily creates two categories of maintenance expense:[1]

1. Expenses under $2 million would be expensed directly when the major maintenance is completed, instead of amortized to the next occurrence of similar maintenance; and
2. Expenses over $2 million, where a regulatory asset would be created and amortized over five years with carrying costs. PSE suggests it would seek

[1]The Company defines its proposed method in its response to Staff Data Response No. 155(a): "Less than $2 million per occurrence would be accounted for on the Direct expensing methodology and greater than $2 million per occurrence would be accounted for following the Deferral methodology. The Direct expensing would be used for relatively consistent, predictable occurrences while the Deferral methodology would be used on the larger, less constant occurrences."

recovery of these expenses in the next general rate case,[2] therefore providing the expectation of total recovery, with interest, while the decision is delayed.

Staff recommends that the Commission should reject the Company's proposed changes in accounting for maintenance expense for the following reasons:

1. There is no accounting authority or Commission order that requires or even suggests the proposed changes;
2. The deferral method PSE currently uses for planned major maintenance provides superior accounting and test year presentation for rate making purposes.

A. The Proposed Accounting Method is Not Required By Accounting Authority Or Commission Order

Q. Please explain the current accounting authority for planned major maintenance activities.

A. The guidance on accounting for planned major maintenance activities is provided in the American Institute of Certified Public Accountants ("AICPA") Guide for Airlines, which has been applied by correlation to electric power plants, as well as oil refineries, ships and heavy-manufacturing equipment and facilities. This guide has been incorporated into the current authoritative GAAP, Financial Accounting Standards Board ("FASB") Accounting Standards Codification.

---

[2]Exhibit No. JHS-1T at 14:18-19.

Q. How is planned major maintenance defined by the AICPA Guide?

A. Planned major maintenance means a significant overhaul or maintenance of plant and equipment.

Q. What are the acceptable expensing methods for planned major maintenance, per the AICPA Guide?

A. The Airline Guide provides three acceptable methods for accounting for planned major maintenance activities:

> *Expense as incurred method.* Under this method, all maintenance costs are expensed in the period incurred because maintenance activities do not represent separately identifiable assets or property units in and of themselves; rather, they serve only to restore assets to their original operating condition.
>
> *Deferral method.* Under this method, the actual cost of each planned major maintenance activity is capitalized and amortized to expense in a systematic and rational manner over the estimated period until the next planned major maintenance activity.
>
> *Built-in overhaul method.* Under this method, costs of activities that restore the service potential of airframes and engines are considered a component of the asset. This method cannot be applied to leased aircraft. The cost of airframes and engines (upon which the planned major maintenance activity is performed) is segregated into those costs that are to be depreciated over the expected useful life of the airframes and engines and those that represent the estimated cost of the next planned major maintenance activity. Thus, the estimated cost of the first planned major maintenance activity is separated from the cost of the remainder of the airframes and engines and amortized to the date of the initial planned major maintenance activity. The cost of that first planned major maintenance activity is then capitalized and amortized to the next occurrence of the planned major maintenance activity, at which time the process is repeated.[1]

The accrue-in-advance method used to be an acceptable method to account for planned major maintenance according to the AICPA Airline Guide. However, FASB

Staff Position AUG AIR-1 eliminated the accrue-in-advance method effective in 2006.[3]

Q. You stated earlier that the Company claims to be currently recovering major maintenance expense in rates under the "accrue-in-advance" method of accounting. Please explain.

A. Company witness Story states on page 12 of Exhibit No. JHS-1T, "PSE calculated rate year maintenance costs based upon actual test year costs plus normalized rate year major maintenance costs." Furthermore, he states, "Normalized major maintenance for PSE's own simple-cycle gas and oil-fired combustion turbines ("SCCTs") represented an average annual cost of the *expected* major maintenance over a *ten year forecast* period." (Emphasis added). On page 13, he defines the rate year calculation: "For financial accounting purposes this calculation is defined as an accrue-in advance method."

Q. Please explain what Company witness Story means by "actual test year costs plus normalized rate year major maintenance costs."

A. In past rate cases, the Company's stated approach to rate year maintenance expense was to forecast maintenance costs ten years into the future.[4] PSE then would take a simple average of those costs and replace test year actual expense with that average.

[3]PSE's Response to Public Counsel Data Response No. 109(a).
[4]Exhibit JHS-1T page 12.

This method does not consider normalization of actual maintenance expense. It considers only future expense based on forecasts.

Q. Can the Company's accounting method for ratemaking purposes rely on changes made to the accrue-in-advance method for financial reporting purposes?

A. No. As stated earlier, the accrue-in-advance method was discontinued for financial reporting purposes in 2006. PSE is trying to claim that a method it used only for rate making purposes should be discontinued because it is not allowed for financial reporting purposes. However, ratemaking does not drive financial reporting. PSE does not book for accounting purposes what it claims to be using for ratemaking purposes. Even if it did use the accrue-in-advance method for financial reporting purposes, that method was discontinued in 2006 despite PSE's claim to be using it for ratemaking purposes through the last general rate case.

Q. Did PSE receive Commission approval to use the accrue-in-advance method for ratemaking purposes?

A. No. Recent PSE rate case orders have not specifically adopted the method Mr. Story describes as "accrue-in-advance".

Q. What conclusions can one make about the accrue-in-advance method used by PSE for this rate proceeding?

A. PSE seems to rely on the discontinuance of the accrue-in-advance method for financial reporting purposes to justify its proposed method for determining maintenance costs for ratemaking purposes. That method was permitted for accounting purposes for years prior to 2006, but has not been prescribed for ratemaking purposes by any authority, including this Commission. Therefore, the accrue-in-advance method has no bearing in this case and is irrelevant to the Company's proposal for planned major maintenance expense.

B. The Company's Current Adopted Accounting Method Is Superior For Rate Making Purposes To The Proposed Change

Q. Has the Company adopted a method to account for planned major maintenance activities?

A. Yes, the Company has adopted the deferral method of accounting for planned major maintenance activities.[5] This method recognizes maintenance expense over the period until the next major maintenance. For instance, if major maintenance occurs every ten years, one tenth is recognized each year until the next major maintenance.

Q. What effect does the deferral method of accounting for planned major maintenance have on maintenance expense over time?

---

[5] PSE Response to Staff Data Request 60(a) at paragraph 2, "PSE has applied the Deferral Methodology pursuant to FASB Staff Position AUG AIR-1 on all major maintenance long-term service agreements ("LTSA") since mid-2008. All capital and operation and maintenance ("O&M") costs under LTSAs, regardless of their total dollar amount, are accounted for under the Deferral Method in accordance with FASB."

A. The deferral method essentially spreads the expense of major maintenance over the maintenance interval or until the next major maintenance occurs. It essentially normalizes expense and provides for a consistent expense level over time.

Q. Have you prepared an analysis of the Company's planned major maintenance under the current deferral method?

A. Yes. Exhibit No. KBH-4C, PSE Maintenance Under Long-Term Service Agreements From 2010 to 2015, provides an analysis of major maintenance by plant as provided in Company witness Mills' work papers. This exhibit demonstrates how the deferral method spreads the significant cost of major maintenance over time. Most of the maintenance has a 10-year period between occurrences, which spreads the cost over time. The average maintenance expense from 2011 through 2015 is $3.2 million within a range of $2.5 million to $3.8 million.

Q. Does the deferral method of accounting for planned major maintenance provide a reasonable basis for ratemaking?

A. Yes. This method provides for the recovery of expenses consistently over the maintenance period and decreases the potential for extreme fluctuations than if the maintenance were, instead, recognized when incurred.

Q. What is the effect of PSE's proposed method for major maintenance compared to the deferral method?

A. Under the Company's proposed method, the ratepayer has the burden of providing recovery of the expense in half the time, five years, based on projected future maintenance expense including carryings cost at the cost of capital.

Q. Does the Company compare the current deferral method to its proposed new method?

A. Yes and no. Company witness Mills' work papers include a comparison of what the Company's purports the proposed changes would be, compared to what it suggests has been included previously in rates. He compares the total expense to the suggested method with major maintenance over $2 million removed.

However, his approach does not provide a consistent and meaningful comparison. To correct his error, the Company would need to include the effect of maintenance over $2 million it proposes to defer as a regulatory asset. PSE is proposing a delay in the recognition of this expense, not its entire removal, as it reflects in this comparison.

Q. Has Staff compared the Company's proposed accounting practice for maintenance and the current accounting practice using the deferral method?

A. Yes. Exhibit No. KBH-5C, Maintenance Expense Comparison, Company Proposed Change Versus Current Accounting Methods, provides this comparison. For the Company's proposed category of major maintenance under $2 million, this exhibit compares the difference by year and for the total period to the current deferred accounting method. Based on this comparison, under the proposed method the Company would include $3.2 million more expense for recovery, or $9.6 million, compared to $6.4 million based on the current accounting method. In addition, this exhibit reflects the variation in expense by year resulting from the Company's proposed method compared to its actual accounting practice that normalizes expense over time. This exhibit confirms that, for maintenance expense under $2 million, the current deferred accounting practice is superior to the proposed method.

For the Company's proposed category of major maintenance expense over $2 million, this exhibit reflects the deferral of $19.7 million consistent with the Company's presentation, including the accrual of carrying charges at the authorized rate of return, with a rate year ending May 2012. The resulting amortization for the five-year period is $4.4 million per year for a total of $22.0 million. This compares to the Company's current accounting under the deferral method, which results in $14.6 million over the five-year period. This again clearly demonstrates that the current accounting practice used by the Company is far superior to the accounting change the Company is requesting.

Q. Please summarize your conclusion that the Company's current accounting method is superior for ratemaking purposes to the Company's proposed change.

A. Under the deferral method already adopted by PSE for financial reporting purposes, all expenses are amortized until the next maintenance, which provides for greater consistency over time and a superior basis for ratemaking purposes. This is preferable to the Company's proposal to direct expense maintenance, which causes peaks and valleys in the under $2 million category. The direct expense method, as the Company has applied it, also shifts expenses from the future period to current periods since it does not reflect the deferral over time.

The deferral method is also preferable to the Company's proposal for major maintenance expense over $2 million, which includes the creation of a regulatory asset subject to carrying costs and an amortization period of five years. Planned maintenance activities over $2 million have, on average, a 10-year interval between maintenance events, which would be used under the deferral method to spread costs, compared to the five year period the Company proposes. The five year amortization period PSE proposes allows, on average, recovery of significant maintenance costs by ratepayers in half the time than would be recognized for financial reporting purposes without considering the carrying charges PSE is requesting.

Q. Will the Company encounter an increase in maintenance in the future?

A. Yes. The Company has acquired significant generation facilities in recent years. In 2005, the Company added the Hopkins Ridge Wind Facility, in 2006 the Wild Horse Wind Facility, in 2007 the Goldendale Facility, and in 2008 both the Sumas and Mint Farm facilities. With these new facilities, PSE has reduced risk from the need to acquire purchase power agreements and has acquired commitments to maintain these complex facilities.

Q. Should an increase in maintenance in future years be addressed in this rate case?

A. No. Rates are set based on a historic test year. Pro forma adjustments are allowed for "known and measurable changes that are not offset by other factors."[6] This relates to the "matching principle" of rate making. Staff witness Parvinen discusses the matching principal and its significance in detail.

Q. Please summarize the reasons for your recommendation that the Commission reject PSE's proposed changes to the accounting for planned major maintenance.

A. The Commission should clearly reject the Company's proposal because there is no accounting authority or Commission order requiring this change. Moreover, the deferral method the Company uses currently is far superior and normalizes the cost over time. The Company has not provided any reasonable justification for the proposed change.

VI. CONTESTED ELECTRIC ADJUSTMENTS

A. Adjustment 10.03, Power Cost – Operations And Maintenance Expenses Only

Q. Please explain your responsibility for Adjustment 10.03, Power Costs?

[6] WAC 480-07-510(3)(e)(iii).

A. I will discuss Staff's adjustment for O&M included in Adjustment 10.03, Power Cost. Staff witness Buckley addresses the balance of this adjustment.

Q. Please describe the Company's Power Cost adjustment for O&M expense.

A. PSE includes pro forma adjustments to power cost O&M based on budget projections and forecast levels for certain facilities through the rate year. For maintenance on thermal plants, PSE uses a forward forecast based on average annual maintenance expense for 2010 through 2014.[7] PSE also applies the proposed change for planned major maintenance activities, as discussed above.

Q. Please summarize the flaws in PSE's approach to base the O&M portion of its Power Cost adjustment on budgeted and forecast levels of expense.

A. The flaws to PSE's approach are numerous:

1. The use of a forecast, budget or projection does not meet the definition of a pro forma adjustment.
2. The Company may include costs in a budget that could be revealed in an audit of actual results to be inappropriate and removed for rate making purposes.
3. The Company's accounting proposal for maintenance is included in this adjustment.

[7] Exhibit No. JHS-1T at 15 and Exhibit No. LEO-1T at 22.

I will address each of these deficiencies and then present Staff's Power Cost adjustment for O&M expense that corrects these deficiencies.

1. Use Of Forecasts, Budgets, And Projections Violates The Definition Of A Pro Forma Adjustment

Q. Please define a Pro Forma Adjustment.

A. WAC 480-07-510(3)(e)(iii) defines pro forma adjustments as adjustments that "give effect for the test period to all known and measurable changes that are not offset by other factors." The work papers must identify dollar values and underlying reasons for each proposed pro forma adjustment. Staff witness Parvinen provides a detailed discussion of the theory and regulatory policy underlying this definition.

Q. Does the use of a forecast, budget or projection, as proposed by PSE for the O&M element of its Power Cost adjustment, meet the definition of a known and measurable change?

A. No. A forecast, budget or projection by its very nature is not known. It might be based on historical information, but with a forward looking estimate of a future event that may or may not materialize.

Q. Are there other reasons to reject the Company's use of forecasts, budgets and projections in the O&M portion of its Power Cost adjustment?

A. Yes. Forecasts, budgets or projections are based on assumptions that, by definition, are unknown or of unspecified determinants. Each assumption can be interpreted differently and arguably supported by documentation. As a result, different outcomes can result based on different underlying assumptions. Moreover, the estimated timing of the event can be incorrect. For instance, a planned addition to plant can be forecast to occur within the rate year, but, once it becomes known and measurable, it may actually occur beyond the rate year. History proves that forecasts can be significantly different from actual results.

Q. Has PSE provided a consistent approach in its use of forecasts for the Power Cost adjustment in this case?

A. No. The Company uses different assumptions in its calculations of the adjustment. PSE's Response to Staff Data Request No. 143(b) states:

[redacted]

This response exemplifies how different assumptions can result in different outcomes. It also illustrates how actual results can vary considerably from a forecast.

Q. Are the assumptions used by the Company in its forecasts and budgets of power cost O&M supported in testimony or work papers?

A. Not usually. Many of these calculations are embedded in the work papers without any reasoning as to why an assumption was used, or the outside source or basis for the assumption.

Q. Does the O&M portion of PSE's Power Costs adjustment overlap with other known and measurable changes addressed by other adjustments?

A. Yes. This adjustment provides forecasts and budgets of wage increases and related items for which the known and measurable portions are already included in the wage-related adjustments. To this extent, the Company's Power Cost adjustment double recovers wage-related expenses.

2. Inherent Audit Issues Reflected In Forecasts

Q. Please explain how budgeted costs, if provided as actual results, can be revealed in an audit as inappropriate and removed for rate making purposes.

A. Typically, a budget or forecast does not provide the level of detail that actual results provide to enable Staff to audit the information. Costs are included in categories and do not reveal their true character until they become actual expenditures. Even though Staff is not supporting forecast or budget data, it is worth pointing out that the Company did include questionable information in the expense budgets for some plant facilities. For instance, the [redacted]

3. Application Of The Company's Proposed Change In Planned Major Maintenance Activities

Q. Does the Company include its proposed change to planned major maintenance in the O&M portion of its Power Cost adjustment?

A. Yes. One of the embedded pro forma adjustments in Company witness Mills' work papers reflect this change. Staff has provided an alternate presentation, described below, for Adjustment 10.03, Power Costs, that is consistent with the Company's current accounting method for planned major maintenance activities.

Q. Please summarize the Company's O&M expense portion of Adjustment 10.03, Power Costs.

A. The Company adjusts test year maintenance expense for its proposed change in accounting for major maintenance. It also includes budget projections for O&M expense [redacted] Other restating adjustments are consistent with Staff's presentation.

Q. Please discuss Staff's overall approach to the O&M portion of its Adjustment 10.03, Power Costs.

A. Staff uses a five year normalized level of expense for thermal facilities to represent an appropriate test year level of expense. For O&M on plant that has only a partial year in the test year, or plant that was brought in to service during the test year, Staff includes an annual level of expense based on actual expense through August 2009. Staff has removed all forecast and budget information included by the Company.

Q. Have you compared Staff's O&M expense portion of Adjustment 10.03, Power Costs to the Company's?

A. Yes. That comparison is included in Exhibit No. KHB-6C, Comparison of Staff Versus Company Adjustment 10.03 Power Costs – Operations and Maintenance. The first section of this exhibit summarizes the differences between Company and Staff adjustments. Following that summary is a detailed discussion of those differences. Staff's adjustment for O&M decreases the Company's amount by $17,791,888. The difference can be attributed to the following:

1. *Thermal Facilities*. As stated above, Staff's adjustment for maintenance on thermal facilities is based on a five year normalized level of historic expense for established facilities and an average annual expense level based on August 2009 actual expense for new facilities. The Company's proposed accounting change for maintenance is removed in the Staff adjustment. Staff's adjustment for thermal facilities reduces the Company's adjustment by $4,512,931.

2. *New facilities with partial results in the test year.* Staff included an annual expense level based on August 2009, as compared to the Company's inclusion of a budget level of expense. This results in a decrease of $3,309,550 for Staff's adjustment, as compared to the Company's expense level.

3. *Additional Rate Year Budget.* The Company provided an additional budget for [redacted]. Staff's removal of the budget amounts accounts for a decrease of $9,969,407 from the Company adjustment.

Q. What conclusion can be made about the Company's O&M portion of Adjustment 10.03, Power Costs?

A. The Company has inflated its presentation of O&M costs with projected budget levels of expenses and the new accounting proposal for maintenance, which forecasts costs five years into the future.

Q. What is Staff's recommendation for O&M expenses?

A. Staff recommends that the Commission reject the Company's accounting proposal for major maintenance that is incorporated in this adjustment, reject the Company's use of forecasts, projections and budgets, and reflect a normalized level of expense, as proposed by Staff.

B. Pro Forma Adjustment For Major Plant Additions

Q. Please explain the issues common to all adjustments for major plant additions included in this section.

A. The issues common to all the adjustments for major plant additions are similar to the issues I discussed earlier regarding power cost O&M:

1. The Company's plant addition adjustments are based on forecasts, budgets and projections, which do not meet the requirement of a proper pro forma adjustment. Staff has assumed the burden of replacing the forecasts, budgets and projections with actual dollars from beyond the test year. Staff does not feel comfortable choosing a "cut-off" date for adjustments of this nature that fall between the test year and rate year. That being said, Staff has used information as of August 2009, which is the most current information available at the time this testimony was prepared. Staff witness Parvinen discusses this issue further in his testimony.

2. The Company did not use a consistent date for its adjustments. For instance, some adjustments included plant balances through the end of the test year with expenses forecasted through the rate year, while another adjustment includes projected plant balances through the end of 2009. Staff has consistently used the most current actual dollar information for August 2009.

1. Adjustment 10.06, Hopkins Ridge Infill Project

Q. **Please summarize the Company's Adjustment 10.06, Hopkins Ridge Infill Project.**

A. This pro forma adjustment involves the installation of four 1.8 megawatt ("MW") Vestas turbines at the Company's existing 149.4 MW Hopkins Ridge Wind Project. This expansion was placed in service in August 2008. The Company's adjustment is an example of an addition that is reflected in the test year at a partial level and the Company proposes a pro forma adjustment to include the expansion through the rate year. The actual rate base from the test year was used and depreciated through the rate year. Operations and maintenance expense was budgeted through the rate year and included in Adjustment 10.03, Power Costs. A forecast of property tax and property insurance for the rate year were also included by the Company.

Q. **Please summarize Staff's pro forma adjustment for the Hopkins Ridge expansion.**

A. Staff has removed the forecast and budgeted amounts for O&M expense, and property tax and property insurance, consistent with the proper application of a pro forma adjustment. A pro forma adjustment for property insurance has been included by Staff based on the premium notice effective April 1, 2009 through April 1, 2010. Staff has also adjusted the rate base for actual results through August 2009.

Staff's adjustment decreases net operating income by $204,970 and increases rate base by $4,075,268. The calculation of this adjustment is shown on my Exhibit No. KHB-2, page 2.13.

2. Adjustment 10.07, Wild Horse Expansion Project

Q. Please summarize the Company's Adjustment 10.07, Wild Horse Expansion.

A. This pro forma adjustment relates to a 44 MW, 22 Vestas turbine expansion to the existing 228.6 MW Wild Horse Wind Generating Facility. The expansion became operational on November 9, 2009. Both rate base and expense calculations were projected by PSE and presented through the end of the rate year.

Q. Please summarize Staff's proposed Adjustment 10.07, Wild Horse Expansion.

A. Staff removes all forecasts, budgets, and projections to meet the requirements of a proper pro forma adjustment. Actual dollars are provided through August 2009. O&M expense included in this adjustment reflects only [redacted].[8] The Company's projected property tax dollars were also removed. Property insurance projections were removed since the latest premium information did not separate the expansion from the total Wild Horse facility. However, Staff's pro forma adjustment for property insurance, Adjustment 10.32, includes the entire Wild Horse facility.

[8]Company in Response to Staff Data Response No. 180.

Staff's Adjustment 10.07 decreases net operating income by $3,289,703 and increases rate base by $63,260,836. The calculation of this adjustment is shown on my Exhibit No. KHB-2, page 2.14.

3. Adjustment 10.08, Mint Farm Energy Center

Q. Please summarize the Company's Adjustment 10.08, Mint Farm Energy Center.

A. This pro forma adjustment presents the Company's forecast of the Mint Farm Energy Center through the rate year. This facility was purchased by PSE on December 5, 2008 and included in the test year. The Company forecast plant additions through December 2009 and applied them to the rate year. In addition, rate year forecasts were used for O&M expense, property tax and property insurance. Projections for fuel and wheeling were also included.

Q. Please summarize Staff's proposed Adjustment 10.08, Mint Farm Energy Center.

A. Consistent with all Staff pro forma adjustments for plant additions, Staff has eliminated all forecasts, budgets and projections. Actual dollars through August 2009 are used, instead. O&M forecasts were replaced with annualized August 2009 expense. Projections for property tax were removed because they are not known and measurable. Property insurance was updated to the latest premium information.

Staff's proposed adjustment decreases net operating income by $46,387,881 and increases rate base by $217,569,921. The calculation of this adjustment is shown on my Exhibit No. KHB-2, page 2.15.

4. Adjustment 10.09, Sumas Cogeneration Station

Q. Please summarize the Company's Adjustment 10.09, Sumas Cogeneration Station.

A. The Sumas Cogeneration Station was placed in service on July 25, 2008. The Company's adjustment includes actual plant balances through February 2009, adjusted through the rate year for accumulated depreciation and amortization, and accumulated deferred taxes. Fuel costs and forecasts for O&M expense are included by PSE in Adjustment 10.03, Power Costs, and have been addressed previously in this testimony. Property tax and insurance premiums were projected by PSE through the rate year.

Q. Please summarize Staff's proposed Adjustment 10.09, Sumas Cogeneration Station.

A. Once again, Staff has eliminated all forecasts, budgets and projections consistent with all pro forma adjustments for plant additions. Again, Staff uses actual dollars through August 2009 for this adjustment. Projections for property tax were removed and property insurance was updated to the latest premium information.

Staff's proposed adjustment decreases net operating income by $593,802 and increases rate base by $7,583,822. The calculation of this adjustment is shown on my Exhibit No. KHB-2, page 2.16.

5. Adjustment 10.10, Whitehorn Generating Station

Q. Please summarize the Company's Adjustment 10.10, Whitehorn Generating Station.

A. In February 2009, PSE acquired the Whitehorn Generating Station. The Company's adjustment includes the purchase transaction based on February 2009, adjusted through the rate year for accumulated depreciation and amortization, and accumulated deferred taxes. Fuel costs and forecasts for O&M expense are included in Adjustment 10.03, Power Costs, and have been addressed previously in this testimony. Property tax and insurance premiums were projected through the rate year by the Company.

Q. Please summarize Staff's proposed Adjustment 10.10, Whitehorn Generating Station.

A. Consistent with all pro forma adjustments for plant additions, Staff has eliminated all forecasts and budgets, and included actual dollars through August 2009.

Staff's proposed adjustment decreases net operating income by $2,025,047 and increases rate base by $16,776,280. The calculation of this adjustment is shown on my Exhibit No. KHB-2, page 2.17.

6. Adjustment 10.11, Baker Hydroelectric Project License

Q. Please summarize the Company's Adjustment 10.11, Baker Hydroelectric Project License.

A. The Company includes a pro forma adjustment for the cost of obtaining a new license for the Baker Hydroelectric Project. PSE used the actual balance capitalized in rate base as of February 2009, adjusted through the rate year for accumulated depreciation and amortization, and accumulated deferred taxes. Projected expenses through the rate year were included in Adjustment 10.03, Power costs.

Q. Please summarize Staff's proposed Adjustment 10.11, Baker Hydroelectric Project License.

A. Staff has included only known and measurable adjustments based on August 2009.

Staff's proposed adjustment decreases net operating income by $855,481 and increases rate base by $33,112,870. The calculation of this adjustment is shown on my Exhibit No. KHB-2, page 2.18.

7. **Adjustment 10.31, Regulatory Assets and Liabilities**

Q. Please summarize the Company's Adjustment 10.31, Regulatory Assets.

A. This adjustment brings forward to the end of the rate year all regulatory assets and liabilities previous authorized by the Commission. In addition, the Company proposes the following adjustments:

1. West Coast Pipeline Capacity
2. Colstrip Settlement Payment
3. Over Recovery of Major Maintenance

Q. Does another Staff witness provide testimony on the West Coast Pipeline Capacity element of the adjustment?

A. Yes. Staff witness Martin provides testimony on this subject.

Q. Please explain the background of the Colstrip Settlement Payment.

A. This lawsuit was originally filed in 2003. There are three types of claims at issue: differential settlement claims, contamination claims, and emotional distress claims.

The Company accrued a reserve of $700,000 in 2004. Approximately $479,173 is PSE's share of the cost to extend the city's water to 13 plaintiffs and $220,827 was accrued as a reserve. In the 1st Quarter of 2008, the Company expensed $10,487,159 reflecting its portion of the pending payment of $10,707,986 per the settlement. The Company and other defendants plan to seek recovery from applicable insurance carriers. PSE has an estimated insurance recovery of $2,083,590 per the settlement.

Q. Please explain the Company's proposed adjustment for the Colstrip Settlement Payment.

A. The Company has established a regulatory asset for the full payment made in 2008 of $10,487,159, amortized over five years including carrying costs at the authorized rate of return.

Q. Please explain Staff's proposed inclusion of the Colstrip Settlement Payment in the test year.

A. Staff has reserved to Account 186, Miscellaneous Deferred Debits, the amount identified in the settlement to be recovered from insurance, or $2,083,590. The remaining $8,404,396 was included in O&M expense. Staff includes this settlement payment in expense.

Q. Turning to the portion of Adjustment 10.31 related to over recovery of major maintenance expense, has the Company calculated the amount of major maintenance that was over-collected?

A. Yes. Company witness Story includes a regulatory liability in this adjustment that reflects the Company's calculation of an over-collection of maintenance expense since 2002.

Q. How does that adjustment affect O&M expense for this proceeding?

A. It confirms that the approach the Company has used to compile O&M expense in past proceedings is not reasonable for this proceeding.

Q. The Company demonstrated an over-collection due to the method it employed when determining rates. Would this problem exist under Staff's proposed method for recognizing maintenance costs?

A. No, since rates would be set on actual expenditures that are booked or recorded in a normalized fashion.

Q. How does Staff address this liability?

A. Staff removes this liability because it is retroactive rate making.

Q. What is the overall impact of Staff's Adjustment 10.31, Regulatory Assets and Liabilities?

A. Staff's proposed adjustment decreases net operating income by $4,659,619 and decreases rate base by $105,539,454. The calculation of this adjustment is shown on my Exhibit No. KHB-2, page 2.38.

8. Adjustment 10.33, Fredonia Power Plant

Q. Please summarize the Company's Adjustment 10.33, Fredonia Power Plant.

A. This adjustment reflects PSE purchase of the Fredonia Power Plant in January 2010. This facility had previously been leased by the Company. The Company's adjustment includes an estimated purchase transaction based on January 2010, adjusted through the rate year for accumulated depreciation and amortization, and accumulated deferred taxes. Fuel costs and forecasts for O&M expense are included in Adjustment 10.03, Power Costs, and have been addressed previously in this testimony. Property tax and insurance premiums were projected through the rate year by the Company.

Q. Please state Staff's issues regarding this adjustment.

A. This adjustment is based on projected information. The Company's response to Staff Data Request No. 146 indicates that the Company does not have any updated information. Staff is left with only projected dollars for the actual purchase transaction, which does not meet the requirement of a pro forma adjustment. Therefore, Staff has removed the projected purchase and reinserted the lease for Fredonia.

Staff's proposed adjustment decreases net operating income by $3,441,784. The calculation of this adjustment is shown on my Exhibit No. KHB-2, page 2.40.

Q. Does this conclude your testimony?

A. Yes, it does.

PACIFIC POWER
A DIVISION OF PACIFICORP

825 NE Multnomah, Suite 2000
Portland, Oregon 97232

December 31, 2009

VIA OVERNIGHT DELIVERY

Ms. Sarah Shifley
Washington State Attorney General's Office
Assistant Attorney General, Public Counsel Section
800 Fifth Avenue, Suite 2000
Seattle, WA 98104

Dear Ms. Shifley

Pursuant to the all-party settlement stipulation in Washington Docket UE-090205, PacifiCorp agreed to provide a report related to renewable energy credits to Washington Commission Staff, Public Counsel, and the Industrial Customers of Northwest Utilities prior to January 1, 2010. In accordance with the settlement stipulation, enclosed is a copy of PacifiCorp's report on renewable energy credits. The files providing the detailed accounting for renewable energy credits are voluminous and are provided in an electronic format on the enclosed CD. Please note that the data included on the CD is confidential and provided subject to the terms of the protective order in UE-090205. A copy of the report and CD is also being provided to Washington Commission Staff and the Industrial Customers of Northwest Utilities.

If you have any questions regarding this information, please contact Cathie Allen, Regulatory Manager, at (503) 813-5934.

Sincerely,

Andrea L. Kelly/ca

Andrea L. Kelly
Vice President, Regulation

Enclosures - CD

PACIFICORP
A MIDAMERICAN ENERGY HOLDINGS COMPANY

PacifiCorp General Rate Case Washington Docket No. UE-090205

Reporting Related to Renewable Energy Credits

December 31, 2009

Docket No. UE-090205
Reporting Related to Renewable Energy Credits
December 31, 2009

Table of Contents

List of Tables

PacifiCorp General Rate Case
Docket No. UE-090205
Reporting Related to Renewable Energy Credits
December 31, 2009

1. Reporting Requirements Outlined in the Settlement Stipulation

The all-party Settlement Stipulation (Stipulation) dated August 25, 2009 in Washington Utilities and Transportation Commission (WUTC) Docket No. UE-090205, section III.I, paragraph 20, outlines certain of PacifiCorp's (the Company) reporting requirements related to renewable energy credits. Prior to January 1, 2010, the Company has agreed to provide a report to WUTC Staff, Public Counsel, and the Industrial Customers of Northwest Utilities that includes the following:

1) An explanation of how Renewable Energy Credits (RECs)[1] and associated costs and/or revenues are allocated among the six states in which PacifiCorp operates (California, Idaho, Oregon, Utah, Washington and Wyoming);

2) An explanation of how the Company determines proper disposition of RECs on a total-company and state-by-state basis; and,

3) A detailed accounting of the total-company RECs that were sold and the total-company RECs that were retained for each year from calendar year 2005 through June 2009.

This report addresses each of these requirements and is provided in compliance with the commitment made in section III.I, paragraph 20 of the Stipulation. Consistent with the provisions in the Stipulation, confidential data is provided subject to the terms of the protective order in UE-090205.

2. Explanation of Allocation of Renewable Energy Credits

Each PacifiCorp state receives an allocation of the RECs generated by Company owned renewable resources or acquired through power purchase agreements for the resources reflected in rates in the state. Initially, PacifiCorp uses forecast allocation factors to approximate the allocation of RECs to each state. Forecast allocation factors are updated to actual historical factors during the second quarter of the following year, once actual load data is finalized.

RECs are allocated using the System Generation (SG) factor under the Revised Protocol methodology and the Control Area Generation West (CAGW) factor under the West Control Area (WCA) methodology. This allocation ensures that the allocation of RECs is consistent with the allocation of resource costs. Under both the Revised Protocol and the WCA, the SG and CAGW factors are used to allocate the fixed costs of renewable resources which account for the vast proportion of the overall costs of renewable resources.

PacifiCorp employs the WCA inter-jurisdictional allocation methodology for the purpose of allocating its costs to customers in the state of Washington. The WUTC approved the WCA allocation methodology in Order 08, Docket UE-061546. The west control area includes California, Oregon and Washington. Generation assigned to the west control area includes resources located within the west control area or with physical capability to deliver energy into the west control area. As noted above, RECs generated by renewable resources that have been found prudent and used and useful for service to Washington customers

[1] Also known as Green tags, Renewable Energy Certificates, or Tradable Renewable Certificates, where one REC represents one-megawatt hour of renewable energy that is physically metered and verified from the generator, or the renewable energy project.

PacifiCorp General Rate Case
Docket No. UE-090205
Reporting Related to Renewable Energy Credits
December 31, 2009

are allocated to Washington based on the CAGW factor. As such, Washington does not receive an allocation of RECs associated with renewable resources that have not been included in rates in Washington those located in the east control area.[2] This results in an unallocated portion of RECs from east control area renewable resources. The tables attached to this report apply the WCA allocation methodology throughout the period from January 2005 through June 2009. PacifiCorp employs the Revised Protocol inter-jurisdictional allocation methodology for purpose of allocating its costs to PacifiCorp customers in California, Idaho, Oregon, Utah, and Wyoming. RECs associated with all renewable resources are allocated to these states based on the SG factor. The application of different allocation methodologies implies a deficit of RECs associated with west control area resources. Although the different allocation methods among states require additional tracking, consistent with WREGIS and state RPS requirements, under no circumstances will any RECs be double-counted as adherence to the WREGIS Operating Rules eliminates that possibility.

3. Explanation of Disposition of Renewable Energy Credits

PacifiCorp manages the generation, retention, and disposition of RECs in conjunction with the Company's obligation to:

(1) manage the supply of Bundled[3] and Unbundled[4] RECs to meet annual renewable portfolio standard (RPS) compliance obligations;

(2) achieve lower revenue requirement through the sale of Unbundled and Rebundled[5] RECs in excess of the Company's RPS compliance obligations;

(3) maintain an accurate and up-to-date REC Book report that is relied upon by the Company to satisfy various compliance obligations including the publication of various retail electricity fuel mix reports and the filing of various emissions reports.

PacifiCorp does not sell Oregon's REC share allocation because that state's RPS permits unlimited REC banking for RECs generated after January 1, 2007 and the first RPS target is near-term (2011). PacifiCorp does not sell California's REC share allocation because the RPS targets for that state are already applicable. Beginning January 1, 2011, under current laws and rules, PacifiCorp will not sell Washington's REC share allocation because the first RPS target will become applicable; however, Washington RECs may be sold in the future if not needed for meeting the target and if the RECs cannot be banked.

Due to the uncertainty of federal greenhouse gas regulation and legislation,, PacifiCorp currently does not expect to sell RECs it has acquired after December 31, 2012. PacifiCorp will review this situation as federal developments occur.

The Company's current policy for the states for which PacifiCorp is selling RECs, is to sell through December 31, 2012, on a firm forward basis no more than 75% of the forward estimated output of

[2] Similarly, Oregon does not receive an allocation of RECs associated with the Rolling Hills resource because it was not included in rate base in Oregon.
[3] Bundled REC is defined as a REC which is generated by or delivered to PacifiCorp along with the original resource's underlying energy.
[4] Unbundled REC is defined as a REC which has been contractually separated from the original underlying energy or a REC (bundled or unbundled) withdrawn from the REC bank and sold to another party.
[5] Rebundled REC is defined as an unbundled REC which is delivered along with PacifiCorp "system" energy or other source of undifferentiated power supply.

production of RECs or up to 100% on a unit contingent basis, provided that any such sales of unit contingent output of production of RECs shall be subtracted from the forward estimated output (on a monthly basis) which are subject to the 75% restriction for firm forward sales. PacifiCorp may sell up to 100% of historical actual RECs after banking eligible RECs for future RPS compliance.

4. Detailed Accounting for Renewable Energy Credits

4.1 Renewable Energy Credits – Megawatts Generated, Retained, Sold

Confidential Table 1, on the attached CD, provides a detailed summary of the megawatt hours (MWh) of RECs generated, retained and sold from January 2005 through June 2009. Note that the data provided in this report is confidential and provided subject to the terms of the protective order in WUTC Docket No. UE-090205. The format of the report is based on the template provided as Appendix C to the Stipulation and provides the following information in MWh:

- RECs generated, by resource;
- RECs generated, by resource, allocated by state;
- Total RECs generated, allocated by state;
- RECs held for compliance, by resource, allocated by state;
- Total RECs held for compliance, allocated by state;
- RECs sold, by resource, allocated by state;
- Total RECs sold, allocated by state;
- RECs retained for sale, by resource, allocated by state; and,
- Total RECs retained for sale, allocated by state.

Note that data for 2009 is preliminary and allocations are based on forecast allocation factors. This data will be updated in the Company's next report. Please refer to Section 5 for a schedule of dates for additional reporting related to renewable energy credits. PacifiCorp has included its large hydro (>30MW) resources in its renewable portfolio because those resources have been registered in WREGIS. The generation from each of those resources is allocated to each state however the RECs from those resources do not meet any states' RPS criteria at this time and show up in the non-RPS REC category. At this time there is no market to sell these RECs[6].

4.2 Renewable Energy Credits – Revenue from Sales

Confidential Table 2, on the attached CD, provides a summary of the revenue recorded from the sale of renewable RECs generated from January 2005 through June 2009. Note that the data provided in this report is confidential and provided subject to the terms of the protective order in WUTC Docket No. UE-090205.

<u>PacifiCorp Renewable Energy Credit Revenue Recognition Policy</u>

Consistent with generally accepted accounting principles, PacifiCorp has adopted the following revenue recognition policy related to the sale of renewable energy credits.

[6] The generation from incremental hydro upgrades may count toward a specific state RPS requirement.

PacifiCorp General Rate Case
Docket No. UE-090205
Reporting Related to Renewable Energy Credits
December 31, 2009

For sales of unbundled RECs, the revenue is recorded at the time the attestation statements are delivered to the counterparty with the recorded amount of revenue established at the date of execution of the agreement. The Company does not record revenue until the renewable energy is generated from a PacifiCorp facility, a firm sales commitment is entered into and the PacifiCorp contract administration group submits the attestation statement to the counterparty.

For sales of bundled electricity and RECs the revenue is recorded for the RECs the same month as the electricity sold to the counterparty physically flows to that counterparty.

5. Schedule for Additional Reporting Related to Renewable Energy Credits

Section III.I, paragraph 21, of the Stipulation also outlines quarterly reporting requirements related to renewable energy credits. Note that some data provided in these reports may be based on preliminary data. Any preliminary data will be updated in future reports as final numbers become available. The timeline below lays out the Company's expected schedule for providing these future reports:

Date of Report	Quarterly Report
July 2010	Period of July 2009 through Quarter Ending March 2010
October 2010	Quarter Ending June 30, 2010
January 2011	Quarter Ending September 30, 2010
April 2011	Quarter Ending December 31, 2010
July 2011	Quarter Ending March 31, 2011
October 2011	Quarter Ending June 30, 2011
January 2012	Quarter Ending September 30, 2011
April 2012	Quarter Ending December 31, 2011
July 2012	Quarter Ending March 31, 2012
October 2012	Quarter Ending June 30, 2012
January 2013*	Quarter Ending September 30, 2012
April 2013*	Quarter Ending December 31, 2012

*The Parties to the Stipulation have agreed that the quarterly reporting will continue at least through December 31, 2012. Prior to January 1, 2013, the Parties have agreed to meet and agree on appropriate changes, if any, to the content or frequency of reports. As such, the dates for future reports may change.