BEFORE THE WASHINGTON UTILITIES AND TRANSPORTATION COMMISSION

Air Liquide America Corporation, Air Products and Chemicals, Inc., The Boeing Company, CNC Containers, Equilon Enterprises, LLC, Georgia-Pacific West, Inc., Tesoro Northwest Company, and The City of Anacortes, Washington	)	
Complainants,	)	DOCKET NO. UE-001952 (consolidated)
v.	)	
Puget Sound Energy, Inc.	)	
Respondent.	)	
. . . . .	)	
In re: Petition of Puget Sound Energy, Inc. for an Order Reallocating Lost Revenues Related to any Reduction in the Schedule 48 or G-P Special Contract Rates	)	DOCKET NO. UE-001959 (consolidated) SIXTH SUPPLEMENTAL ORDER: ORDER REQUIRING FURTHER PROCEEDINGS TO IMPLEMENT TARIFF CHANGES NECESSARY TO ENSURE FAIR, JUST, AND REASONABLE RATES, TERMS, AND CONDITIONS OF SERVICE
. . . . .	)	

SYNOPSIS: *The Commission acts under its general statutes, Chapter 80 RCW, to order Phase Two proceedings to establish a temporary soft cap as an additional term under the Optional Price Stability provisions of Schedule 48 and the PSE/Georgia-Pacific Special Contract, pending further proceedings to determine a final disposition of Schedule 48 in this or other pending dockets. The Commission declines to act under the provisions of the Emergency Adjudicative Proceedings statute, RCW 34.05.479.*

SUMMARY

1 **PROCEEDINGS:** Air Liquide, *et al.* filed their original Formal Complaint Requesting Emergency Adjudicative Proceeding in Docket No. UE-001952 on December 12, 2000. PSE filed its Petition in Docket No. UE-001959 on December 13, 2000.

2 The Commission, on due and proper notice, conducted a prehearing conference on December 14, 2000, before Chairwoman Marilyn Showalter, Commissioner Richard Hemstad, and Administrative Law Judge Dennis J. Moss. Among other things, the Commission established a procedural schedule, invoked the discovery rule (WAC 480-09-480), and entered a Protective Order (First Supplemental Order, December 19, 2000). Evidentiary hearing proceedings were scheduled for December 29, 2000.

3 Complainants filed an Amended Complaint on December 18, 2000. A second prehearing conference was convened before ALJ Moss on December 22, 2000. Among other things, following discussion with the Parties concerning the need for additional time to prepare for hearing, the evidentiary hearings were rescheduled to January 8, 2001. Additional process and procedural dates were established at the conference and by subsequent order. Several discovery/motions conferences were conducted on and after December 22, 2000. Various discovery related and procedural motions were resolved by oral or written orders. Complainants filed a Second Amended Complaint on December 28, 2000. In response to oral requests and a motion from Complainants, the Commission entered its Third Supplemental Order: Amending Protective Order, on December 29, 2000.

4 PSE filed its Motion To Strike Second Amended Complaint, and its Answer to the Amended Complaint on January 2, 2000. The Commission granted PSE's Motion To Strike Second Amended Complaint and went forward on the first Amended Complaint and PSE's Answer. The Parties filed prehearing briefs on January 4, 2001. Evidentiary hearing proceedings were conducted on January 8, 9, 12, and 15, 2001. The Commission heard oral argument on January 16, 2001.

5 **PARTIES:** Melinda Davison and Bradley Van Cleve, Davison Van Cleve, P.C., Portland, Oregon, represent Air Liquide America Corporation, Air Products and Chemicals, Inc., The Boeing Company, CNC Containers, Equilon Enterprises, LLC, Georgia-Pacific West, Inc., Tesoro Northwest Company, and the City of Anacortes.

Stan Berman, Heller Ehrman White & McAuliffe, LLP, Seattle, Washington, and James M. Van Nostrand, Stoel Rives, Seattle, Washington, represent Puget Sound Energy, Inc. (PSE). John A. Cameron and Traci Grundon, Davis Wright Tremaine LLP, Portland, Oregon, represent Bellingham Cold Storage Company (BCS). Brian Walters and Tom Anderson provided *pro se* representation for Public Utility District No. 1 of Whatcom County (Whatcom PUD). Frank Prochaska appeared *pro* se to represent the Association of Western Pulp and Paper Workers (AWPPW). Simon ffitch, Assistant Attorney General, Seattle, Washington, represents the Public Counsel Section, Office of Attorney General (Public Counsel). Robert D. Cedarbaum and Donald Trotter, Assistant Attorneys General, Olympia, Washington, represent the Commission's regulatory staff (Staff).

6 **COMMISSION:** The Commission finds and concludes that Complainants failed to demonstrate the existence of an immediate danger to the health, safety, or welfare requiring immediate agency action under RCW 34.05.479, but also finds that expedited action under RCW 80.04.110 is required. The Commission further finds and concludes that PSE's retail rates under Schedule 48 and the Special Contract that are pegged via Mid-Columbia index pricing to Western wholesale power markets that are volatile and exceedingly high are not fair, just, and reasonable because customers do not have effective options to achieve price stability and reasonable rates under the Optional Price Stability provisions of Schedule 48 and the Special Contract. The Commission orders that there shall be immediate further proceedings to establish a temporary "soft cap" as an additional term under the Optional Price Stability provisions of Schedule 48 and the PSE/Georgia-Pacific Special Contract, pending further proceedings to determine a final disposition of Schedule 48 in this or other pending dockets.

MEMORANDUM

I. Background and Procedural History.

7 Air Liquide, *et al.* filed their original Formal Complaint Requesting Emergency Adjudicative Proceeding in Docket No. UE-001952 on December 12, 2000. PSE filed its Petition in Docket No. UE-001959 on December 13, 2000.

8 Air Liquide, *et al.* complain against PSE and allege that PSE is charging retail electric rates under its Tariff WN U-60, Schedule 48, Optional Large Power Sales Rate, and pursuant to a Special Contract with Georgia-Pacific, that are not just, fair, and reasonable, in violation of RCW 80.28.010. Rates for retail electric service that PSE provides under Schedule 48 and the Special Contract include an energy cost component that is based on certain wholesale price indices published by Dow Jones. These indices nominally reflect prices paid in the wholesale power market for certain categories of transactions, as defined by Dow Jones, for transactions that occur at the Mid-Columbia trading hub.

9 Schedule 48 and the Special Contract fundamentally are the products of negotiations that were conducted in the spring of 1996 between PSE and certain of PSE's large industrial customers. These negotiations led to PSE's filing for approval of the Special Contract on May 6, 1996, and Schedule 48 on May 24, 1996. The Commission approved the Special Contract, subject to certain condition, on June 7, 1996, in Docket No. UE-960612, and approved Schedule 48 with conditions on October 31, 1996, in Docket No. UE-960696. The rate provisions of Schedule 48 and the Special Contract initially were identical in all material respects. In particular, the energy cost component in each was tied to the Mid-Columbia Electricity Price Index for non-firm power. More recently, via certain amendments, the energy component pricing provision of the Special Contract was changed to the Dow Jone's Mid-Columbia firm power index.

10 Formally, at least, the business relationships between PSE and its customers under Schedule 48 and the Special Contract remained uncontroversial for about two years. In November 1998, however, certain of the Schedule 48 customers filed a complaint against PSE alleging that PSE, commencing in June 1998, consistently had applied index prices other than as required under Schedule 48. The customers' complaint was heard in Commission Docket No. UE-981410 and they prevailed on the merits of their claim. *Air Liquide America Corporation, et al. v. Puget Sound Energy, Inc.*, Fifth Supplemental Order Granting Complaint, Ordering Refunds and Other Relief, Docket No. UE-981410 (August 3, 1999).[1] In essence, the Commission found that PSE had violated the terms of its "deal" with the customers by unilaterally employing

[1] The referenced case provides a detailed discussion of the genesis of Schedule 48 and the parties' conduct under its terms from the date of its approval through the period of the complaint in Docket No. UE-981410.

an index other than the Mid-Columbia non-firm index from the time that index first was published in June 1998.

11 Since its determination in the 1998 customer-initiated complaint case in Docket No. UE-981410, the Commission has conducted adjudicative proceedings concerning the operation of Schedule 48 in at least five dockets, either on customer complaint or on its own complaint, and has addressed Schedule 48 and Special Contract matters in several open public meetings.[2] In short, controversies of one type or another, and proposals intended to avoid further controversy, have surrounded Schedule 48 and the Special Contracts more or less continuously for more than two years.

12 All of this controversy arises in one fashion or another from, or at least relates to, the wholesale market-based pricing provisions in Schedule 48 and the Special Contracts. Most recently, events in the wholesale markets on the interconnected Western power grid have brought matters to a critical state, at least from the perspectives of the customers who are Complainants in this proceeding. Volatility in the Western wholesale power markets during the first half of 2000 were reflected in price spikes at the Mid-Columbia trading hub, spikes that became particularly acute in June 2000. Those price spikes led Bellingham Cold Storage Company and Georgia-Pacific to file their Formal Complaint, Request for Expedited, Emergency Action Including Waiver of Regular Notice Periods, Relating to Special Contract Transmission Obligations and Pricing Provisions in Docket No. UE-001014 on June 29, 2000. BCS and Georgia-Pacific characterized their Complaint as "an emergency petition" requiring expedited action by the Commission to prevent employee lay-offs, plant closings, and related adverse impacts on the broader economic sectors served by the industrial operations of the complaining parties. Among other things, BCS and Georgia-Pacific urged that the Commission take action to "relieve [BCS and Georgia-Pacific] from direct

[2] These include Docket No. UE-981238, concerning the price for optional firming service under Schedule 48; Docket No. UE-000735, a formal complaint by Georgia-Pacific under its Special Contract with PSE; Docket No. UE-001014, a formal complaint by Bellingham Cold Storage Company and Georgia-Pacific under their essentially identical Special Contracts with PSE; Docket No. UE-001616, another formal complaint by Georgia-Pacific under its Special Contract with PSE; and Docket No. UE-001521, a Commission-initiated complaint concerning the Georgia-Pacific and Bellingham Cold Storage Special Contracts with PSE. Some of these matters have been resolved; others remain pending. Open meeting matters have included Commission approval of amendments to the energy pricing provisions of the Georgia-Pacific and Bellingham Cold Storage Special Contracts; PSE's refiling of Schedule 48 on January 1, 2001, in Docket No. UE-960696, as required under the terms of the Commission's Order approving Schedule 48; and PSE's filing of a new tariff, Schedule 448, which it proposes as an alternative tariff for these, and other, industrial customers.

linkage to the Mid-Columbia Index." The Commission conducted the Docket No. UE-001014 proceeding on an expedited schedule, as urged by the Complaint. Complainants, however, did not meet the date established for the prefiling of their direct evidence and sought leave to withdraw their pricing claims and have that part of their Complaint dismissed without prejudice. The Commission granted BCS's and Georgia-Pacific's separate requests. Later, Georgia-Pacific sought, and was granted, leave to withdraw from the proceeding entirely and have its remaining claims dismissed without prejudice. The non-price elements of BCS's complaint remain pending.

13 The Western wholesale power markets remained higher than normal through the fall, but were more stable during October and into early November. In mid- to late-November, and in December 2000, however, a series of events converged to again cause prices to rise sharply and to unprecedented levels. The Mid-Columbia firm index, for example reached a peak one-hour price of $714.44 on December 8, 2000, and the non-firm index reached a peak one-hour price of $604.06. Three days later, on December 11, 2000, the corresponding prices for the peak hour were $3,300.00 and $1,285.00. This contrasts sharply to historic prices in the range of $26 for firm on-peak and $23 for non-firm on-peak during all of 1999.[3]

14 As we noted at the outset of this section of our Order, Air Liquide, *et al.* filed their original Formal Complaint Requesting Emergency Adjudicative Proceeding in this docket on December 12, 2000, one day after the Mid-Columbia indices reached these extraordinary levels. The Complaint alleges that "daily spot market pricing at the Mid-Columbia no longer provides a reasonable basis for setting retail electric rates" and that such rates are "unjust, unreasonable, unjustly discriminatory or unduly preferential." The Complaint asserts that "the Commission is required to, 'determine the just, reasonable, or sufficient rates . . . to be thereafter observed and in force, and shall fix the same by order." *Complaint at 2 (citing RCW 80.28.020).*[4]

[3] We note for purposes of illustration that a hypothetical industrial customer who consumed 100 MWh in December 2000 would have paid $34,856 under Schedule 48. This compares to $3,743 for that same 100 MWh of consumption in January 2000. Calculation derived from data included in Exhibit No. 18-C (page 5, line 11).

[4] The two preceding references are to the original Complaint. Identical allegations and language are included in the first Amended Complaint, which is the formal pleading to which this Order pertains.

15 On December 13, 2000, PSE filed its Petition in Docket No. UE-001959, asking that the Commission "issue an order reallocating lost revenues related to any reduction in the Schedule 48 or G-P Special Contract rates." The Petition, albeit not PSE's formal answer, responds generally to the Complaint and asserts that to the extent the Commission acts to reduce the revenues PSE otherwise would obtain under Schedule 48 and the Special Contract, the Commission should allow PSE to establish a deferral account and determine whether "such deferred revenue requirement should be paid by the industrial customers who have chosen market-based prices or reallocated among other customer classes."

16 The Commission, on shortened notice, conducted a prehearing conference on December 14, 2000, before Chairwoman Marilyn Showalter, Commissioner Richard Hemstad, and Administrative Law Judge Dennis J. Moss. Among other things, the Commission determined it would consolidate the Complaint in Docket No. UE-001952 with the Petition in Docket No. UE-001959, established a procedural schedule, and invoked the discovery rule (WAC 480-09-480). The Commission entered its Order Consolidating Proceedings; Prehearing Conference Order and Notice of Hearing on December 18, 2000. Evidentiary hearing proceedings were scheduled for December 29, 2000. To facilitate discovery, the Commission entered a Protective Order (First Supplemental Order, December 19, 2000).

17 During our first prehearing conference, we urged the Parties to consider entering into mediated settlement negotiations and offered the services of Administrative Law Judge C. Robert Wallis to act as facilitator. Complainants accepted our offer and agreed to commence such discussions at the Commission on December 19, 2000. Complainants requested, however, that the Commission simultaneously move forward with the complaint action. PSE agreed to the mediation and did not object to proceeding in parallel with the adjudication. Following several days of discussion, the Parties reported that "[s]cheduled mediation talks among Puget Sound Energy and several industrial customers about the effects of recent market conditions on electricity rates paid by the industries have concluded without producing an agreement among parties that resolves the rate issue." *Agreed Statement on Mediation (12/21/00).*

18 In its first Prehearing Conference Order, the Commission established the scope of the proceedings as follows:

> **PROCESS AND PROCEDURAL SCHEDULE; NOTICE OF HEARING:** Complainants propose a two-phase proceeding. Complainants propose that the Commission first should convene an evidentiary hearing on December 29, 2000, to determine whether price caps or other emergency rate relief should be implemented for PSE's Schedule 48 customers, and under Georgia-Pacific's special contract with PSE. The Commission determines that it should provide Complainants an opportunity to carry their burden to show that such relief is warranted and legally permissible. **Accordingly, the Commission will convene the requested Phase One hearing on December 29, 2000, beginning at 9:00 a.m., in room 206 at the Commission's offices in Olympia, Washington.**

The Prehearing Conference Order also outlined certain, but not necessarily all, of the legal issues and mixed questions of law and fact the Commission considered pertinent to Phase One. Among others, the Commission expressly raised questions about its authority and obligations with respect to the standards for taking action concerning rates. Those standards are set forth in our organic statutes, Chapter 80 RCW, and are stated in terms of the fairness, justness, reasonableness, and sufficiency of rates. We discuss these standards in more detail below, in Section II.A. of our Memorandum.

19 Complainants filed an Amended Complaint on December 18, 2000. A second prehearing conference was convened before ALJ Moss on December 22, 2000. Among other things, following discussion with, and agreement by, the Parties concerning the need for additional time to prepare for hearing, the evidentiary hearings were rescheduled to January 8, 2001. Additional process and procedural dates were established at the conference and by subsequent order.

20 A schedule was established to permit PSE to depose Complainants' proposed witnesses and for Complainants' to depose PSE's proposed witnesses at the Commission with the presiding ALJ continuously available to resolve any disputes. All proposed Complainant and Respondent witnesses were deposed prior to hearing. Several discovery/motions conferences were conducted on and after December 22, 2000. Various discovery-related and procedural motions were resolved by oral or written orders. In response to oral requests and a motion from Complainants, the Commission entered its Third Supplemental Order: Amending Protective Order, on December 29, 2000. This was to facilitate the exchange, under a heightened degree

of protection from disclosure, of certain documents claimed to be especially sensitive. According to arguments by the Parties at various times, many thousands of pages of documents were exchanged among them during the course of discovery.

21 Complainants filed a Second Amended Complaint on December 28, 2000. PSE filed its Motion To Strike Second Amended Complaint, and its Answer to the Amended Complaint on January 2, 2000. The Commission granted PSE's Motion To Strike Second Amended Complaint and went forward on the first Amended Complaint and PSE's Answer. We note that the basic substance of the three Complaints remained the same throughout. The first Amended Complaint simply added the City of Anacortes as a Complainant, added a few factual assertions, and corrected an arguable technical deficiency in the original Complaint. The Second Amended Complaint merely sought to add Intel Corporation as a Complainant and to withdraw two of the affidavits filed as part of the first Amended Complaint. Later, Complainants were granted leave to withdraw the same two affidavits from the Amended Complaint.[5]

22 The Parties filed lengthy and detailed prehearing briefs on January 4, 2001. Evidentiary hearing proceedings were conducted on an expanded hearing-day basis on January 8 (8:00 a.m. – 10:05 p.m.), January 9 (9:00 a.m. – 11:59 p.m.), January 12 (9:00 a.m. –10:55 p.m.), and January 15 (9:30 a.m. – 10:00 p.m.), 2001, before Chairwoman Marilyn Showalter, Commissioner Richard Hemstad, and Administrative Law Judge Dennis J. Moss. These 55 hours of evidentiary hearings produced a transcript of more than 1550 pages reflecting the direct- and cross-examination of 10 witnesses. Approximately 175 exhibits were introduced into the record. The Commission heard oral argument from Complainants, Staff, Public Counsel, and PSE on January 16, 2001.[6]

[5] The withdrawn affidavits had been filed by Mr. Keith C. Warner for The Boeing Company, and Mr. Mark C. Darnell for Air Liquide as attachments E and G to the Amended Complaint. *See* TR. 351.

[6] The Commission also allowed Parties who elected to not participate actively in the evidentiary proceedings to submit a written closing statement in lieu of oral argument. One Intervenor, AWPPW, made such a filing.

II. Discussion and Decision.

A. Governing Statutes and Rules.

23 The following statutory provisions and rules are most pertinent to our discussion and decision:

> **RCW 80.01.040 General Powers and Duties of Commission.**
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> The utilities and transportation commission shall:
>
> (3) Regulate in the public interest, as provided by the public service laws, the rates, services, facilities, and practices of all persons engaging within this state in the business of supplying any utility service or commodity to the public for compensation, and related activities; including, but not limited to, electrical companies . . ..
>
> **RCW 80.04.110 Complaints--Hearings--. . ..** (1) Complaint may be made by the commission of its own motion or by any person or corporation, . . . or any body politic or municipal corporation, or by the public counsel section of the office of the attorney general, or its successor, by petition or complaint in writing, setting forth any act or thing done or omitted to be done by any public service corporation in violation, or claimed to be in violation, of any provision of law or of any order or rule of the commission: PROVIDED, That no complaint shall be entertained by the commission except upon its own motion, as to the reasonableness of the schedule of the rates or charges of any gas company, electrical company, water company, or telecommunications company, unless the same be signed by the mayor, council or commission of the city or town in which the company complained of is engaged in business, or not less than twenty-five consumers or purchasers of such gas, electricity, water or telecommunications service, or at least twenty-five percent of the consumers or purchasers of the company's service . . ..
>
> (2) All matters upon which complaint may be founded may be joined in one hearing, and no motion shall be entertained against a complaint for

misjoinder of complaints or grievances or misjoinder of parties; and in any review of the courts of orders of the commission the same rule shall apply and pertain with regard to the joinder of complaints and parties as herein provided: PROVIDED, All grievances to be inquired into shall be plainly set forth in the complaint. No complaint shall be dismissed because of the absence of direct damage to the complainant.

(3) Upon the filing of a complaint, the commission shall cause a copy thereof to be served upon the person or corporation complained of, which shall be accompanied by a notice fixing the time when and place where a hearing will be had upon such complaint. The time fixed for such hearing shall not be less than ten days after the date of the service of such notice and complaint, excepting as herein provided. The commission shall enter its final order with respect to a complaint filed by any entity or person other than the commission within ten months from the date of filing of the complaint, unless the date is extended for cause. Rules of practice and procedure not otherwise provided for in this title may be prescribed by the commission. Such rules may include the requirement that a complainant use informal processes before filing a formal complaint. . . .

80.28.010 Duties as to rates, services, and facilities . . ..

(1) All charges made, demanded or received by any gas company, electrical company or water company for gas, electricity or water, or for any service rendered or to be rendered in connection therewith, shall be just, fair, reasonable and sufficient.

(2) Every gas company, electrical company and water company shall furnish and supply such service, instrumentalities and facilities as shall be safe, adequate and efficient, and in all respects just and reasonable.

(3) All rules and regulations issued by any gas company, electrical company or water company, affecting or pertaining to the sale or distribution of its product, shall be just and reasonable. . . .

80.28.020 Commission to fix just, reasonable, and compensatory rates.

Whenever the commission shall find, after a hearing had upon its own motion, or upon complaint, that the rates or charges demanded, exacted, charged or collected by any gas company, electrical company or water company, for gas, electricity or water, or in connection therewith, or that the rules, regulations, practices or contracts affecting such rates or charges are unjust, unreasonable, unjustly discriminatory or unduly preferential, or in any wise in violation of the provisions of the law, or that such rates or charges are insufficient to yield a reasonable compensation for the service rendered, the commission shall determine the just, reasonable, or sufficient rates, charges, regulations, practices or contracts to be thereafter observed and in force, and shall fix the same by order.

RCW 34.05.479 Emergency adjudicative proceedings. (1) Unless otherwise provided by law, an agency may use emergency adjudicative proceedings in a situation involving an immediate danger to the public health, safety, or welfare requiring immediate agency action.

(2) The agency may take only such action as is necessary to prevent or avoid the immediate danger to the public health, safety, or welfare that justifies use of emergency adjudication.

(3) The agency shall enter an order, including a brief statement of findings of fact, conclusions of law, and policy reasons for the decision if it is an exercise of the agency's discretion, to justify the determination of an immediate danger and the agency's decision to take the specific action.

(4) The agency shall give such notice as is practicable to persons who are required to comply with the order. The order is effective when entered.

(5) After entering an order under this section, the agency shall proceed as quickly as feasible to complete any proceedings that would be required if the matter did not involve an immediate danger.

(6) The agency record consists of any documents regarding the matter that were considered or prepared by the agency. The agency shall maintain these documents as its official record.

(7) Unless otherwise required by a provision of law, the agency record need not constitute the exclusive basis for agency action in emergency adjudicative proceedings or for judicial review thereof.

(8) This section shall not apply to agency action taken pursuant to a provision of law that expressly authorizes the agency to issue a cease and desist order. The agency may proceed, alternatively, under that independent authority.

WAC 480-09-510 Emergency adjudicative proceedings. (1) The commission may use emergency adjudicative proceedings pursuant to RCW 34.05.479 to suspend or cancel authority, to require that a dangerous condition be terminated or corrected, or to require immediate action in any situation involving an immediate danger to the public health, safety, or welfare requiring immediate action by the commission. Such situations include, but are not limited to:

(a) Failure to possess insurance;

(b) Inadequate service by a gas, water, or electric company when the inadequacy involves an immediate danger to the public health, safety, or welfare; and

(c) Violations of law, rule, or order related to public safety, when the violation involves an immediate danger to the public health, safety, or welfare.

(2) The commission shall hear the matter and enter an order. If a majority of the commissioners is not available, a commissioner shall

> hear the matter. If no commissioner is available, a commission administrative law judge shall hear the matter.
>
> (3) The commission's decision shall be based upon the written submissions of the parties and upon oral comments by the parties if the presiding officer has allowed oral comments. The order must include a brief statement of findings of fact, conclusions of law, and justification for the determination of an immediate danger to the public health, safety, or welfare. The order is effective when entered. The commission must serve the order pursuant to WAC 480-09-120.

B. Procedural Issues

1. Is The Commission Limited To Emergency Adjudicative Procedures (RCW 34.05.479 and WAC 480-09-510) or May It Act Pursuant To Standard Complaint Procedures (RCW 80.04.110)?

24 Complainants initially urged the Commission to act under its emergency adjudicative procedures as specified in WAC 480-09-510, the Commission's procedural rule that implements the Emergency Adjudicative Procedures section of the Administrative Procedure Act. *RCW 34.05.479.* The original Complaint asserted that "[t]he [Commission's] standard complaint procedure [under RCW 80.04.110], in which the Commission must order relief in up to ten months, will not provide an adequate remedy to the Complainants' immediate and dire need for power at just and reasonable rates." *Amended Complaint at 2.* Although not mentioned in the original Complaint, one reason RCW 80.04.110 might not have afforded adequate or, indeed, any relief, is that Complainants arguably lacked standing under RCW 80.04.110 to bring a complaint against PSE's rates.

25 The question whether Complainants met the standing requirements under RCW 80.04.110 arose at our first prehearing conference. RCW 80.04.110 provides in relevant part that

> no complaint shall be entertained by the commission except upon its own motion, as to the reasonableness of the schedule of the rates or charges of any . . . electrical company, . . . unless the same be signed by the mayor, council or commission of the city or town in which the company

> complained of is engaged in business, or not less than twenty-five consumers or purchasers of such gas, electricity, water or telecommunications service, or at least twenty-five percent of the consumers or purchasers of the company's service . . ..

26 The original Complaint did not name as a complainant any city or town in which PSE is engaged in business. The entire class of PSE customers to whom market-based rates are available (*i.e.,* Schedule 48 and certain Special Contract customers) includes fewer than 25 customers. Arguably, the third test for standing stated in the statute means 25 percent of PSE's total customer base, not simply 25 percent of the customer class. Thus, there was the prospect of a challenge to Complainants' standing to bring a formal complaint against PSE's rates under our standard complaint procedures as set forth in RCW 80.04.110.

27 By stating their cause as one permitting Commission action under the Emergency Adjudicative Procedures statute, RCW 34.05.479, Complainants might have avoided the standing issue, but faced the burden to show "an immediate danger to the public health, safety, or welfare requiring immediate agency action." *RCW 34.05.479(1).* By filing the Amended Complaint, which adds the City of Anacortes as a Complainant and includes the signature of H. Dean Maxwell, Mayor, Complainants clearly met the standing requirements under RCW 80.04.110, thus expanding the procedural options available to the Commission for considering the merits of their claims.

28 By filing their Amended Complaint, Air Liquide, *et al.* cured the alleged deficiencies in their original Complaint that arguably would have precluded the Commission from considering the dispute under its "standard complaint procedure," as specified in RCW 80.04.110. Nevertheless, the Amended Complaint continued to urge us to proceed under the Emergency Adjudicative Proceedings statute and our related procedural rule.

29 It is useful to analogize the procedural options available to the Commission under the Amended Complaint to those in civil court where a petitioner may seek injunctive relief. The Administrative Procedure Act allows an agency to grant relief analogous to a preliminary injunction. *See RCW 34.05.479(1)-(4), (6), and (7) ("Emergency Adjudicative Proceedings").* Thus, the Commission may hold a brief hearing, or perhaps even proceed *ex parte,* to develop and consider a record that consists of "any

documents regarding the matter that were considered or prepared by the agency." Moreover, "the agency record need not constitute the exclusive basis for agency action in emergency adjudicative proceedings." It is necessary, however, for the party seeking such relief to satisfy a three-part test.

30 The general criteria governing the issuance of a preliminary injunction are outlined in *Tyler Pipe Indus., Inc. v. Department of Rev.*, 96 Wn.2d 785, 638 P.2d 1213 (1982):

> [O]ne who seeks relief by temporary or permanent injunction must show (1) that he has a clear legal or equitable right,[7] (2) that he has a well-grounded fear of immediate invasion of that right, and (3) that the acts complained of are either resulting in or will result in actual and substantial injury to him.

Id. at 792 (quoting *Port of Seattle v. International Longshoremen's & Warehouseman's Union*, 52 Wn.2d 317, 319, 324 P.2d 1099 (1958)). The Court in *Tyler Pipe* clarified, however, that

> since injunctions are addressed to the equitable powers of the court, the listed criteria must be examined in light of equity including balancing the relative interests of the parties and, if appropriate, *the interests of the public.*

96 Wn.2d at 792 (emphasis added). Significantly, under our principal jurisdictional statute, RCW 80.01.040, it is our mission always to regulate in the public interest. As we weighed and considered the evidence that was presented in this proceeding, and our procedural options, it was necessary that we consider not only the prospect of harm alleged by individual customers if we denied them the relief they requested and the counterbalancing harm PSE alleged would befall it were we to grant the relief requested, but also the effect on the public interest.

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[7] The state's appellate courts have consistently held that a preliminary injunction "will not issue in a doubtful case." *E.g.*, *Tacoma Stands Up For Life*, 106 Wn.2d 261, 265, 721 P.2d 946 (1986); *Tyler Pipe*, 96 Wn.2d at 793. To determine whether a clear right has been shown, the court must analyze the moving parties' likelihood of prevailing on the merits. *Id.* Obviously, however, in making this determination, the court does not adjudicate the ultimate rights of the parties in the lawsuit. *Id.*

31 We considered that the Emergency Adjudicative Proceedings statute itself requires that if relief analogous to a preliminary injunction is granted, the agency must then consider more deliberately on the basis of a more fully developed record, as would a court, whether some form of permanent relief should follow. *RCW 34.05.479(5).* Consistent with that principle, we recognized from the outset that whether or not we granted relief analogous to a preliminary injunction following an abbreviated process, it was our obligation to continue to proceed as quickly as feasible to complete proceedings to address any matters that obviously require expedited action even though they do not involve an immediate danger to the public health, safety, or welfare.

32 At its first prehearing conference in this proceeding, the Commission determined that a hearing would be required to determine, among other things, whether circumstances confronting the Complainants constituted an immediate danger to the public health, safety, or welfare. Thus, at the earliest phase of this proceeding, relief analogous to a preliminary injunction was not granted. Nevertheless, the Commission recognized that the circumstances facing Complainants were urgent and required expedited process. Accordingly, the Commission ordered that it would conduct an evidentiary hearing as quickly as possible, consistent with all Parties' rights to due process, to determine whether price caps or other emergency rate relief should be implemented for PSE's Schedule 48 customers, and under Georgia-Pacific's special contract with PSE. The Commission determined that it should provide Complainants an early opportunity to carry their burden to show that such relief is warranted and legally permissible. *Air Liquide, et al. v. PSE, Order Consolidating Proceedings; Prehearing Conference Order; and Notice of Hearing, Docket No. UE-001952 (December 18, 2000) at 3.*

33 Thus, on and after December 18, 2000, this proceeding was conducted in a fashion consistent with the requirements of both the Emergency Adjudicative Proceedings statute, RCW 34.05.479(5), and the Commission's Complaint statute, RCW 80.04.110. As related above, in Section I of this Order, the Parties were afforded the opportunity to conduct extensive discovery, including both document discovery via data requests and through depositions, to prepare prehearing briefs, and to present extensive evidence and argument during nearly 60 hours of hearing.

34 We conclude, for reasons discussed below in Section II.C.1 of our Order, that Complainants did not show the existence of an emergency in the sense that term is

used in the Emergency Adjudicative Proceedings statute. We find, however, that Complainants demonstrated the existence of circumstances that call for prompt action by the Commission. We followed a procedural course that allows us to respond expeditiously, appropriately, and legally, in light of this finding. In the final analysis, we act under the requirements of our formal complaint procedures (RCW 80.04.110), including the requirement for a hearing, and measure the evidence presented against the standards established under RCW 80.28.010 and RCW 80.28.020.

C. Substantive Issues

1. Did Complainants Carry Their Burden To Show That There Exists An Immediate Danger To The Public Health, Safety, Or Welfare Requiring Immediate Agency Action?

a. The Evidence

35 Air Liquide, *et al.'s* Amended Complaint is substantively grounded in RCW 80.28.010 and RCW 80.28.020. Complainants allege that PSE is charging rates under Schedule 48 and the Special Contract that are not just, fair, and reasonable, in violation of RCW 80.28.010(1). More broadly, they contend these tariffs no longer are just, fair, and reasonable. They urge us to find and conclude that price volatility in the wholesale energy markets reported by Dow Jones's Mid-Columbia indices means that the Schedule 48 and Special Contract tariffs no longer provide reasonable bases for setting retail electric rates and otherwise governing the business relationship between PSE and this customer class. Such findings and conclusions, following a hearing, would require the Commission, as a matter of law, to "determine the just, reasonable, or sufficient rates, charges, regulations, practices or contracts to be thereafter observed and in force, and [to] fix the same by order." *RCW 80.28.020.*

36 As discussed in the preceding section of our Order, Complainants assert that the rates being charged are so extraordinarily high that their business operations are in financial jeopardy. Complainants argue that as a consequence of being required to pay "among the highest, if not, the highest retail prices for electricity in the entire United States," several of them "have already closed or curtailed their operations," and that "these closures or reductions in operations, even temporarily, will result in employment terminations, lost revenues, economic and social hardship and pose an

immediate danger to the Puget Sound area economy, and therefore, the public welfare." *Amended Complaint at 2.*

37 Complainants acknowledge in their prehearing brief that "[w]hile the impact of high rates on an individual customer may not threaten the public welfare, when those high prices threaten the viability of the largest industrial facilities in PSE's service territory, the threat to the public welfare is self evident." *Complainants' Prehearing Brief at 48.* This statement begs the question of what evidence in our record shows that the viability of the largest industrial facilities in the Puget Sound region are in immediate jeopardy. In addition, we must consider what effect that situation, if shown, has on the broader public.

38 PSE, Public Counsel, and Staff all advocate that Complainants failed to show the existence of an emergency within the meaning of RCW 34.05.479. PSE, through its prehearing brief and subsequent development of the record, and Staff, in closing arguments, provide us with useful guidance to the evidence relative to each Complainant's circumstances and any effect those circumstances may be having on the broader public.

i. Air Liquide

39 Air Liquide presented no direct evidence that it has suffered any harm to its operations in Washington or to its national or international corporate operations as a result of increased costs under Schedule 48. Although Air Liquide submitted an affidavit in support of the original Complaint and Amended Complaint, it subsequently withdrew its affidavit. PSE asserts in its prehearing brief that Air Liquide provided no response to discovery requests "for data related to Air Liquide's alleged injury by Schedule 48." *PSE Prehearing Brief at 17.* The assertion is undisputed on the record. Staff cites to Exhibit No. 1542, a press release by Air Liquide America announcing a nationwide surcharge on its products "in the face of rising fuel and power related costs [in 2000]." The press release goes on to relate that "[p]ower shortages and curtailments *across the country* have driven costs to extremely high levels over the past months." *Exhibit No. 1542 (emphasis added).* In response to Bench Request No. 8, an inquiry concerning the impact on the labor force of Complainants, the collective response for Air Liquide, CNC, and Air Products is that these companies "have reduced operations or have resorted to intermittent operations, which *could affect* labor force compensation and morale. Other facilities

may be forced to reduce operations. Prices of essential products *may increase*, which *could lead* to more detrimental economic impacts." *Exhibit No. 8 (page 1, emphasis added).* In light of this general and speculative response, the Commission issued Bench Request No. 15 asking for more detailed information. Complainants' response for Air Liquide was that "Air Liquide has no additional information to add to Complainants' initial response." *Exhibit No. 8 (page 3).*

ii. Air Products

40 Air Products provided the affidavit of Mr. Randall B. Clancy, Site Manager for the Gases and Equipment Group, Product Supply Organization, of Air Products and Chemicals, Inc., in Puyallup, Washington. *Attachment C to Amended Complaint*. The affidavit relates that "recently Air Products has been required periodically to curtail or shut down its Puyallup facility to avoid these extraordinary power costs." Aside from this bare statement, Air Products produced no direct evidence that it has suffered any harm to its operations in Washington or to its national or international corporate operations as a result of increased costs under Schedule 48. Complainants' response to our Bench Request No. 8 already has been related. Air Products' supplemental information on the question of labor impacts, provided in response to Bench Request No. 15, is that "[t]o date, . . . Air Products has not reduced or increased its labor force as a result of high electricity prices." *Exhibit No. 8 (page 3).* On deposition examination by PSE, Mr. Clancy verified that there have been no employee layoffs or reductions in pay. *Deposition TR. at 24-25, 38.* He also testified that there has been no curtailment of operations and no reduction in product output. *Deposition TR. at 14, 16.* Mr. Clancy testified that the Puyallup facility remains in full production even at electric prices in the $150 to $200 per MWh range. *Deposition TR. at 21, 42-43*. He testified that Air Products local facility in Puyallup is fully capable of paying invoices submitted to it by PSE. *Deposition TR. at 12, 13.* Speaking for the corporation via a news release, Air Products' chairman and CEO, H.A. Wagner, is quoted as saying with respect to the company's fourth quarter that "[o]ur record operating performance this quarter is particularly noteworthy. By persistently focusing on productivity, we overcame severe increases in raw material and energy prices." *Exhibit No. 1547.*

iii. The Boeing Company

41 The Boeing Company presented no direct evidence that it has suffered any harm to its operations in Washington or to its national or international corporate operations as a result of increased costs under Schedule 48. Like Air Liquide, Boeing submitted an affidavit in support of the original Complaint and Amended Complaint, but subsequently withdrew its affidavit. In response to Bench Request No. 12, Boeing states that

> in this proceeding, Boeing is not claiming that the production of its products in Washington State currently are threatened with curtailment or closure as a result of the high charges for electricity. Nonetheless, Boeing notes that Co-complainants Air Products, Air Liquide and Equilon are Boeing suppliers. *If* Boeing's Washington State suppliers are forced to shut down or curtail operations, Boeing *may* have to procure its supplies from facilities located outside Washington State. Boeing believes that such diversion of business outside of Washington State is not in the interest of the public welfare of Washington State.
>
> Despite the high energy costs and the possibility of further curtailment of operations by its Washington State suppliers, Boeing has no current plans to close or reduce operations in response to high energy charges under Schedule 48.

Exhibit No. 5 (page 4—emphasis added); see also Exhibit No. 8 (page 3).

Exhibit 1549 is an Internet version of a "State of the Company" news conference delivered by Boeing Chairman and CEO Phil Condit on December 13, 2000. Mr. Condit reported to the press that "[t]ogether our employees have produced a year of excellent financial performance. We had powerful cash flow. We have improved earnings and margins . . .." Mr. Condit also reported that while Boeing stock opened the year at just over $41 a share, it closed 67 percent higher for the year, at $69 a share, on the day the Complaint was filed in this proceeding. According to the document, in light of the company's performance, Boeing's Board of Directors authorized a 21 percent increase in the dividend and authorized repurchase of "an additional 85 million shares of stock."

iv. CNC Containers

42 CNC Containers did present evidence, both through the affidavit and live testimony of Matthew G. Franz, Vice President, Operations, CNC Containers. *Attachment F to Amended Complaint; TR. 422-486; Exhibit Nos. 201-203*. Mr. Franz also was deposed by PSE. *Exhibit No. 204-C (Deposition Transcript 12/29/00—confidential at pp. 12-31 and 54)*. Among other things, Mr. Franz is responsible for CNC Containers' energy management in its Tumwater facility, which opened nine years ago. *TR. 423 (Franz)*. CNC Containers, which manufactures "preforms" and plastic bottles such as those used for soft drinks and juice, is one of the smallest Schedule 48 customers with approximately 8 average MWh demand. *TR. 426 (Franz)*. Initially, the company took service under PSE's Schedule 31. Mr. Franz elected to switch to Schedule 48 in March 1997 on the basis of discussions with Mr. Mike Richardson, a PSE key accounts manager. *Id.* Mr. Franz testified that Mr. Richardson "presented a substantial amount of data that showed the benefits of Schedule 48 versus the current schedule we were on." *Id.* Exhibit No. 201 is the data provided to Mr. Franz. These data reflect PSE's expectation at the time that projected energy costs under Schedule 48 would decrease from about $42 per MWh to $28 per MWh from January 1997 through December 2001. These rates compared favorably to fixed rates of approximately $45 per MWh under Schedule 31. Mr. Franz testified that while he understood CNC Containers would be subject to market risk for the price of electricity under Schedule 48, he did not understand "that the price could go up 5 times, 10 times, 50 times in a relatively short period of time." *TR. 431 (Franz)*. Even so, Mr. Franz initially elected to hedge under the Optional Price Stability provision of Schedule 48 for the period March 1997 through mid-1999.[8] *Id.*

43 Turning to the effects of volatile Mid-Columbia prices on CNC Containers, Mr. Franz testified that the company has laid off personnel "due solely to cost reductions we have had to make because of the price of electricity." *TR. 435 (Franz)*. These layoffs include six managerial/administrative personnel. *Exhibit No. 204 (page 19—Franz deposition transcript)*. CNC Containers, however, has not laid off hourly-wage factory workers due to high energy prices. *Id. (pp. 19 and 21)*. Mr. Franz also testified that CNC Containers has shifted assets and equipment to other states and to Peru because of electricity prices in the Pacific Northwest. *TR. 435 (Franz)*. Nevertheless, Mr. Franz testified that CNC Containers continues to meet its

[8] We return to the subject of hedging in greater detail in the next section of our Order.

contractual obligations to its customers, even though its contracts do not permit it to pass through increased electric costs. *TR. 436-437* (Franz). Despite its high electric power costs, Mr. Franz expects that CNC Containers will have positive earnings for 2000 in the range of $1-2 million through November. *TR. 452-53 (Franz)*. He also testified that there is no shortage of bottles in the region and that 2000 was a record year in bottle production. *TR. 469 (Franz)*. Although Mr. Franz testified at some length to his view that an emergency exists for CNC Containers, the critical situation he describes is prospective and assumes prices during 2001 in the range of $260. *TR. 439-44 (Franz)*. If such prices eventuate, however, "that will be a death sentence for our company," according to Mr. Franz. *TR. 444 (Franz)*.

v. Equilon Enterprises

44 Equilon Enterprises is another Complainant that presented no direct evidence that it has suffered any harm to its operations in Washington or to its national or international corporate operations as a result of increased costs under Schedule 48. In response to Bench Request No. 5, Equilon stated that

> Equilon's Puget Sound Refinery produces a full slate of refined petroleum products, including various grades of gasoline, diesel fuel, fuel oils, lubricants, kerosene, and jet fuels. Equilon's products are essential to public health, safety and welfare. Equilon's refinery is one of only four refineries in the Pacific Northwest. *If* production from Equilon's refinery were interrupted or curtailed due to the high price of electricity—which is essential to production—the adverse effects on the state of Washington *would be* immediate. . . . Electricity Prices at current levels are driving Equilon *to consider curtailing* its operations, *which would result* in substantial harm to the state of Washington and public health, safety and welfare.

Exhibit No. 5 (page 5, emphasis added).

Somewhat curiously, in a response to Bench Request No. 15 provided on the same day as the response quoted from above, Equilon states that it "has temporarily shut down one of its alkylation units at the Puget Sound Refinery as a result of the high electricity prices." *Exhibit No. 8 (page 3).* The response goes on to state that no

employees were laid off as a result, but that "if the current crisis continue [sic], Equilon will have to consider laying off employees." *Id.*

vi. Georgia-Pacific

45 Georgia-Pacific presented evidence, both through the affidavit and live testimony of James Cunningham, who is general manager of the company's Bellingham plant. *Attachment D to Amended Complaint; TR. 782-855; Exhibit Nos. 401-C--403.* Mr. Cunningham also was deposed by PSE. *Exhibit No. 404 (Deposition Transcript 12/29/00).* Mr. Cunningham's responsibilities include supply of energy to the Bellingham plant. *TR. 783 (Cunningham).* The Bellingham facility's load is approximately 40 megawatts. The plant produces tissue products, bath products, towel products, 400 to 450 tons of pulp a day, and a stream of chemicals. The Bellingham plant participates in global markets. Georgia-Pacific entered into its Special Contract in the May-June time frame in 1996 as an alternative to bypassing PSE and connecting instead to PUD No. 1 of Whatcom County. *TR. 788-89 (Cunningham).* The Special Contract, like Schedule 48, is pegged to the Mid-Columbia index. Mr. Cunningham testified that toward the end of May 2000, or perhaps early in June, prices on the Mid-Columbia index spiked into the range of $500 per MWh and that this led to his company's decision to "shut our facility down for approximately two days." *TR. 796-97 (Cunningham).* At that time, Georgia-Pacific entered into a hedging arrangement for July 2000, the only short-term option it believed available to it at the time. *Id.* Mr. Cunningham testified further that the company explored physical supply options and, "with the assistance of some of Governor Locke's staff [we] explored what has now come to be known as a buy-sell opportunity to buy physical power in the market . . .." *TR. 798 (Cunningham).* Lower prices had temporarily returned by this time and Georgia-Pacific was attempting to secure power in the "$40 plus or minus" range. *Id.* The effort failed, according to Mr. Cunningham, because PSE raised questions regarding the legality of such arrangements. *Id.* Asked about what happened leading up to December, Mr. Cunningham testified that

> the price projections that we received from Puget were behaving somewhat reasonable through the October, November time frame. In fact, looking ahead, we were down in the $70 range 12, 15 months out. But then there started to be an increase into the $200, to 300, and eventually we heard some numbers—we have heard numbers in the

> thousands. When those numbers clearly exceeded our ability to cover our variable costs, we shut the facility down on or about December 7.

TR. 803 (Cunningham). Since then, Georgia-Pacific has installed portable diesel generators capable of producing approximately 15 megawatts of power and has reopened its tissue mill and a portion of its chemical operation. *TR. 803-804 (Cunningham)*. Georgia-Pacific has brought back approximately one-half of its 500 hourly-wage employees. *TR. 807-808 (Cunningham).* At the conclusion of his direct testimony, Mr. Cunningham stated that:

> I would simply like to reinforce the fact that we have a tremendous amount of uncertainty in our Bellingham community, both at our own facility with our hundreds of employees who are affected by this shutdown and curtailment, the uncertainty about the future of their employment, and of course the impact it has on our whole community. And we're looking for some relief in terms of pricing and looking for a way to get ourselves to a reasonable cost structure and back in operation.

TR. 818 (Cunningham).

vii. Tesoro Northwest

46 Tesoro Northwest presented evidence through live testimony of Mr. Russell Crawford who is the process engineering manager at the company's Anacortes refinery. *TR. 488-541; Exhibit Nos. 301-C - 303*. Mr. Crawford also was deposed by PSE. *Exhibit No. 304-C (Deposition Transcript 12/28/00)*. Mr. Crawford testified that Tesoro's average electric load is about 20 MWh at its Anacortes facility. *TR. 489 (Crawford).* The refinery produces propane, gasoline, jet fuel, diesel, marine fuel, and road asphalt. *Id.* Mr. Crawford testified that reduced throughput of crude oil at the refinery in response to high electric prices has resulted in reduced production of these fuels, particularly propane, which is "used to heat many homes in the Northwest and Skagit County." *TR. 495 (Crawford).* Nevertheless, Mr. Crawford testified that he is not aware of any shortage of propane in the region due to the impact of high prices for electricity. *TR. 508 (Crawford)*. Mr. Crawford also testified to the importance of Tesoro's production of jet fuel to supply demand at SeaTac International Airport, but stated that he does not know of any shortage of jet fuel in the Northwest region at this

time. *TR. 536 (Crawford)*. Significantly, in this connection, Mr. Crawford confirmed on cross-examination that prior to December 2000, the company operated its refineries at historically high rates. *TR. 527 (Crawford).* If Tesoro continues to operate at a reduced level of production, however, Mr. Crawford expects there will be adverse impacts to supply and prices for propane, jet fuel, and other products produced at the Anacortes refinery. *TR. 500-501 (Crawford).* In terms of effects on Tesoro's labor force, Mr. Crawford testified that the company has not laid off any of its 330 full-time, or 200 contract employees due to higher electricity prices. *TR. 508, 531 (Crawford); see also Exhibit No. 8 (page 3)*. On the financial side, despite higher electricity prices, Tesoro had "a very good year" in 2000. *TR. 529 (Crawford).* Higher electricity prices to the Anacortes refinery resulted in 2000 earnings being some 5 to 7 cents less per share than otherwise would have been the case. *Id.* Even so, Tesoro's earnings per share were about three times what they were in 1999. *Id.* Looking to the future, Tesoro has embarked on a $94 million capital improvement plan at the Anacortes refinery and Mr. Crawford expects those improvements to increase the profitability of the facility.

viii. City of Anacortes

47 Mayor Howard Dean Maxwell appeared as a witness for the City of Anacortes. *TR. 353-421; Exhibit Nos. 101-106, 108*. Mayor Maxwell also was deposed by PSE. *Exhibit No. 107 (Deposition Transcript, 12/29/00).* Among other services and facilities, Anacortes operates a municipal water utility and is the largest provider of water in Skagit County. *TR. 353 (Maxwell)*. Two of the water utility's customers are the Equilon refinery and the Tesoro refinery. *Id.* These customers take the lion's share of the water utility's total output and are responsible for paying approximately 70 percent of its costs, including electric costs. *TR. 362, 379 (Maxwell).* Anacortes switched its water utility's service from PSE's Schedule 49 to Schedule 48 in June 1998. *TR. 355 (Maxwell); Exhibit No. 106 (Anacorte's Schedule 48 Service Agreement with PSE)*. Mayor Maxwell testified that Mr. John Campion of PSE initiated a meeting with Mr. Jim Pemberton, the City's public works director, and Mayor Maxwell early in the spring of 1998. *TR. 355, 358 (Maxwell).* He testified further that Mr. Campion "showed us the benefits that the City of Anacortes could receive under Schedule 48." *Id.* This included information that is of record as Exhibit No. 101. The Exhibit shows a favorable comparison of Schedule 48 prices to Schedule 49 prices on a historic and prospective basis, including projected Schedule 48 prices of between $25 and $23 per MWh for the January 2000 through December

2001 time frames, respectively. *Exhibit 101 (page 2).* Corresponding prices under Schedule 49, which is a fixed-price schedule, were indicated to be $42 per MWh. *Id.* Mayor Maxwell testified that as things turned out, Anacortes has paid approximately $987,000 more under Schedule 48 through year 2000 than it would have paid had it stayed on Schedule 49. *TR. 362 (Maxwell).*

48 Significantly, as previously noted, 70 percent of the water treatment plant's excess costs are passed through to Equilon and Tesoro under the City's contracts with those customers. *TR. 383 (Maxwell); Exhibit No. 20 (Anacortes's Contracts with Equilon and Tesoro).* Mayor Maxwell testified that excess costs incurred by the City's water utility are "passed on to our customers typically." *Exhibit No. 107 (Deposition Transcript at 20).* PSE developed the point on cross-examination, that the remaining "excess costs" could be passed through to the City's 35,000 residential customers with an annual rate increase of approximately $10 per customer. *TR. 401-403 (Maxwell).* Although Mayor Maxwell was unable to testify to the proportion of commercial to residential water consumption in his community, assuming that some portion of the total excess would be charged to commercial customers, the suggested charge for a residential customer would be even less. *Id.*

ix. Other Schedule 48 and Special Contract Customers

49 Although there are a number of Schedule 48 customers other than Complainants, we note that none of these customers intervened in our proceeding. The Second Amended Complaint, which was stricken on PSE's motion, would have added Intel Corporation, but Intel did not furnish an affidavit or other evidence in support of its proposed participation as a party Complainant. Intel did not seek to intervene.

50 In addition to Georgia-Pacific, there are other PSE Special Contracts customers whose retail energy rates are tied to the Mid-Columbia indices. One of these, Bellingham Cold Storage did intervene, but did not participate actively. BCS presented no evidence, did not participate in the cross-examination of witnesses, and did not file a brief or make a closing statement.

b. Commission Decision

51 We cannot find on the basis of this body of evidence that Complainants have demonstrated the existence of an immediate danger to the public health, safety, or

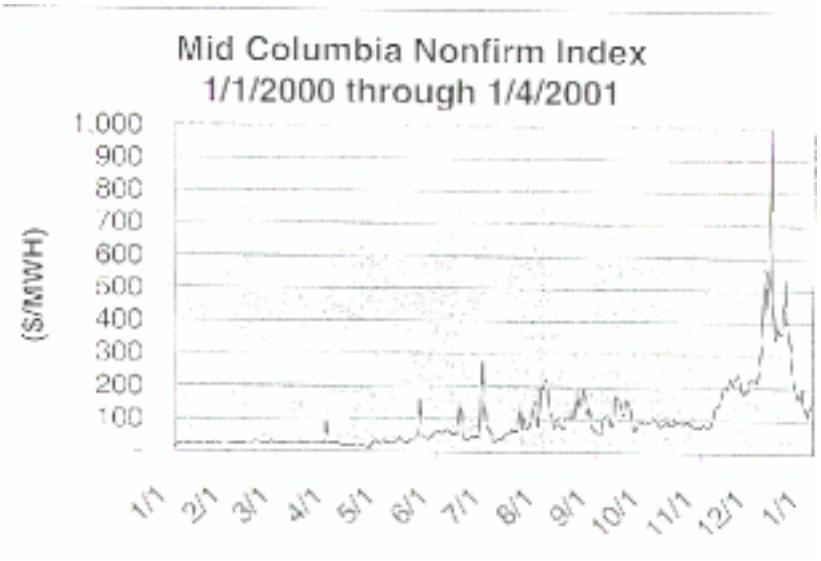
welfare requiring immediate agency action. These Parties raise the prospect of future harm if wholesale market rates remain volatile, and they are required to pay exceptionally high retail rates. Whatever threat there may be to the public health, safety, or welfare, it cannot be found to be "immediate" on the record before us. We conclude, therefore, that there is not an "emergency" within the meaning of RCW 34.05.479.

2. Do The Rates, Terms, And Conditions Of Service Under Schedule 48 And The Special Contract Remain Fair, Just, Reasonable, And Compensatory?

a. The Evidence

52 As previously observed, despite our finding above, there is ample evidence demonstrating that the Schedule 48 and Special Contract customers face financially serious circumstances because of extraordinary electricity price levels and volatility. These circumstances are producing, and threaten to produce, results that are contrary to the public interest and therefore require expeditious action by the Commission. The record shows unanimous agreement, or at least no dispute, that circumstances in the Western wholesale power markets are seriously perturbed relative to historic price levels and degree of volatility. PSE itself described this situation in its closing argument as an emergency faced by all who participate in those markets. *TR. 1779 (Counsel for PSE).* PSE, Complainants, and the Commission all have actively sought intervention in the Western wholesale power markets by the Federal Energy Regulatory Commission, the federal agency charged with exclusive jurisdiction over wholesale power markets. *Puget Sound Energy, Inc. v. All Jurisdictional Sellers of Energy and/or Capacity at Wholesale into Electric Energy and/or Capacity Markets in the Pacific Northwest, Including Parties to the Western Systems Power Pool Agreement, FERC Docket No. EL01-10-000.*

53 Because rates under Schedule 48 and the Georgia-Pacific Special Contract are tied directly to prices in the wholesale market, the volatility of the wholesale prices reported at the Mid-Columbia trading hub translate directly into volatile and sometimes extraordinarily high rates to PSE's retail customers under the subject tariffs. This is illustrated, for example, by Exhibit No.1402, reproduced below.



Such extraordinarily high and volatile prices for electricity are neither appropriate for these customers to pay, nor in the public interest, unless there are provisions in the subject tariffs that provide a certain and practical means for these customers to achieve price stability in the face of unanticipated volatility in the markets.

54 Schedule 48 and the Special Contract do include optional price stability provisions. Schedule 48's Optional Price Stability clause provides:

> Available optional price stability services may include guarantee on an average commodity price, price caps on the non-firm prices, or collars on the non-firm price. Rates for these Optional Price Stability services will be determined according to market conditions.

Exhibit No. 1528 (Schedule 48, Second Revised Sheet No. 48-c). The corresponding provision in the Georgia-Pacific Special Contract states:

> Price of these Optional Price Stability services will be customized to the customer's needs. Those services could include guarantee on an

> average commodity price, price caps on the non-firm prices, or collars on the non-firm price.[9]

Exhibit No. 1531 (page 6, Power Sales Agreement, Schedule RTP).

55 These provisions, along with market-index pricing, were approved in 1996 when competitive conditions in the Western wholesale power markets were just developing. Mr. Canon, who is the Executive Director of the Industrial Customers of Northwest Utilities (ICNU), and who participated in the negotiations that led to Schedule 48, testified that there was emerging at the time Schedule 48 was negotiated "a very robust, evolving market." *TR. 556 (Canon).* One assumption of the industrial customers was "that we would have a competitive market" and an index that would track that competitive market." *TR. 557 (Canon).* Mr. Canon testified further that the general range of wholesale market prices was around $15 to $16 per MWh with the upper range expected to be in the vicinity of $50 per MWh. *TR. 557-58 (Canon); see also Exhibit No. 511 (page 5; Staff Memorandum 9/25/96).*

56 Given these expectations, the customers expressly assumed the risk of price variation under Schedule 48 and the Special Contract. Many of the customers who moved to Schedule 48 also expressly elected not to pursue whatever opportunities existed for price stability under the tariff's Optional Price Stability provisions. *Exhibit No. 203 (page 3—CNC Service Agreement)*[10] Georgia-Pacific also did not pursue such opportunities.

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[9] On May 15, 2000, Georgia-Pacific and PSE agreed to amend their Special Contract by substituting under the heading "Non-Firm Energy" of Section I ("DEFINITIONS") a detailed provision substituting the Dow Jones Mid-Columbia Electricity Index reporting "Firm On-Peak," and "Firm Off-Peak" and "Sunday & NERC Holiday 24 Hour Firm" energy prices for the non-firm indices previously identified in their Special Contract. *Exhibit 1531 (pp. 12-13).* Since they retained the "Non-Firm Energy" heading, this appears to be of no material consequence relative to the Optional Price Stability provision quoted here. The Commission approved the amendment. *In the Matter of the Special Contract Filed by Puget Sound Energy, Second Supplemental Order Granting Amendment to Special Contract on Less Than Statutory Notice, Docket No. UE-960612 (July 12, 2000).*

[10] This exhibit is CNC Containers' Schedule 48 Service Agreement executed February 10, 1997. CNC Containers expressly waived Optional Price Stability service from PSE. We note here, and discuss below in Section II.C.2. of this Order that CNC Containers did obtain a price hedge at the time it began service under Schedule 48, but this apparently was done independently from any Optional Price Stability available from PSE under the tariff.

57 The customers' expectations were realized during the first several years following Schedule 48's approval. *TR. 623-24 (Canon).* Indeed, prior to June 2000, rates based on the non-firm prices at Mid-Columbia never exceeded $60 per MWh. With prices remaining in the range expected, most Schedule 48 customers elected not to hedge or purchase other price stability mechanisms that might have been available. Some customers, however, did hedge even in the stable market environment. As previously noted, for example, CNC Containers elected to hedge under the Optional Price Stability provision of Schedule 48 for the period March 1997 through mid-1999. *TR. 431 (Franz).* Mr. Franz testified that as the company gained experience and recognized that markets remained stable over longer periods, CNC elected to not continue hedging. *Id.* In addition, Mr. Franz testified that he was influenced by PSE's projections of continued "low and stable" Schedule 48 prices and the recommendation of "our key account manager at that time . . . who said he believed we didn't need to hedge anymore." *Id.*

58 Beginning in June 2000, however, the Western wholesale power markets began behaving in a markedly different fashion from what was observed during the prior several years. *TR. 613-14 (Canon).* According to Mr. Canon, the customers who had taken the risk of market-index prices, and had not protected themselves via whatever options were available under the Price Stability provisions of Schedule 48 and the Special Contract, viewed the early summer price spikes as "just a temporary, you know, two or three month excursion, and they were looking at prices going down." *TR. 614-15 (Canon).* This helps explain why even after June 2000, the utility of financial hedging against Mid-Columbia indices as a price stability mechanism was viewed with skepticism by at least some customers. *See, e.g., TR. 799-801 (Cunningham); TR. 432, 472-74 (Franz).*

59 Prices remained volatile, however, after June 2000. Mr. Schoenbeck, an expert on energy markets who has advised industrial electricity and gas customers for more than 20 years, testified to his astonishment over prices in the Western wholesale power markets in the range of $150 per MWh. *TR. 890 (Schoenbeck).* Mr. Schoenbeck described such prices in the Pacific Northwest as "unconscionable." *Id.* He observed that prices in the Pacific Northwest "have generally been in the $20 to $30 per megawatt hour range" and expressed his opinion that "[m]ost industries have located here, have located here over the years because of the historic low prices." *Id.* Wholesale market prices continued on average to exceed $100 per MWh through July and August, spiking dramatically higher from time-to-time during that period.

Beginning in mid-November, however, prices went even higher and persisted at a level of more than $200 per MWh on most days. The situation worsened in early December. The Mid-Columbia firm index, for example reached an hourly on-peak price of $714.44 on December 8, 2000, and the non-firm index reached an hourly on-peak price of $604.06. Three days later, on December 11, 2000, the corresponding hourly on-peak prices were $3,300.00 and $1,285.00. Mr. Canon testified that "what happened in December obviously was—was something I think that calls into question the whole West Coast energy market." *TR. 615 (Canon).*

60 It is in the light of these market conditions that we must consider what options are available, and what options should be available to permit customers to achieve some degree of price stability, even at high prices. We must do so, of course, with an eye to what also is necessary to ensure that PSE is not deprived of its opportunity to recover its prudently incurred wholesale power costs and a reasonable margin.

61 Financial hedges, as previously discussed, remain an option. Mr. Canon testified, however, that financial hedging is very difficult in conditions of market volatility. *TR. 635 (Canon).* Mr. Schoenbeck testified that:

> You obviously can do some hedges. Timing is obviously everything. You have to be careful. Generally you can not hedge against the Mid-C Non-firm price, but you can hedge against the Mid-C Firm price. You also, of course, in doing a hedge generally, there's not only the price factor, but there's also a block or a load factor as well.

TR. 892-93 (Schoenbeck). He testified further that hedges may or may not be available at a given time depending on market conditions. *TR. 893 (Schoenbeck).*

62 When Mid-Columbia prices spiked in August 2000, Mr. Franz again inquired of PSE about the prospect of hedging and received rate projections for the fourth quarter 2000 forward. PSE communicated to Mr. Franz indicative hedge prices in the range of $63.35 per MWh for a two-year term, to $85.80 per MWh for a four-month hedge. *Exhibit 204-C (attachment exhibit PSE-10 to Franz deposition transcript).* Mr. Franz testified, however, that Mr. Charlie Black of PSE presented data that showed Mid-Columbia index prices were expected to drop to the $50 per MWh range by second quarter 2001. *TR. 432 (Franz).* Mr. Franz testified further that Mr. Black said that "buying a hedge when prices are high is not a particularly good idea, because you will

pay more for a hedge. With price projections going lower, it's a much more sound course of action to purchase a hedge at the end of the first quarter, beginning of second quarter, because you will get a better deal." *Id.; TR. 472-74 (Franz).* According to Mr. Franz, he intended to follow this advice. *Id.* Asked again on cross-examination about the hedges PSE communicated to CNC Containers in August 2000 Mr. Franz testified:

> You know, hindsight is 20/20 on all of these things. Obviously in retrospect knowing what we know now, you know, it was a terrible decision. We should have hedged. But, you know, the data we had to make that information came from PSE, and it was bad, and the recommendations we had from PSE were wrong. So yeah, we made a bad decision, no doubt about that. It was a terrible decision, but you know, we had a lot of help getting there.

TR. 478 (Franz); see also TR. 481-82 (Franz).

63 When prices did not decrease after August 2000 and, in fact, increased, Mr. Franz again investigated the possibility of hedging. Exhibit No. 202 is a communication CNC Containers received from Enron Corporation offering a hedge for all of 2001 at a flat rate of $260 per MWh. Mr. Franz testified that CNC Containers did not purchase this hedge "[b]ecause we could not afford it. At $260 a megawatt hour with our load [we'd] have paid approximately $18 million a year for electricity . . . we can't do that." *TR. 433 (Franz).* This compares to approximately $2.1 million CNC Containers paid for electricity under Schedule 48 in 1999. *TR. 438 (Franz).* Even with the high prices experienced in 2000, Mr. Franz estimates CNC Containers' total electric costs paid to PSE for the year are $6.4 million. *Id.*

64 Mr. Crawford, for Tesoro, also testified on cross-examination with respect to hedges. He stated that he has not pursued financial hedges because "I really don't understand hedging real well, and it's hard for me to find a good reasonable point in time to buy or even recommend a hedge." *TR. 524 (Crawford).* Mr. Crawford went on to testify that he is unaware of the fact that Tesoro, at the corporate level, acquires financial derivative products to protect itself from variability in market valuation of crude oil and other products. *TR. 524-26 (Crawford); Exhibit No. 304-C (attachment to Deposition Transcript-Tesoro Response to PSE DR-5).*

65 Mayor Maxwell testified that the City of Anacortes attempted in 1998 to purchase a financial hedge or similar financial instrument pursuant to the Optional Price Stability provision in Schedule 48. *TR. 364 (Maxwell).* Ultimately, after working with Mr. Campion at PSE through the summer to obtain information about hedge prices that might be available through a business relationship between PSE and Duke Energy, the City was informed in September 1998 that it was too small a load to obtain a hedge from Duke Energy at a price Anacortes would find attractive. *Id.; Exhibit No. (Tab I)* Also in September 1998, Mr. Campion informed the City through its finance director, Mr. George Khtaian, that PSE was investigating other hedging opportunities but that the "two different electricity commodity trading companies" that had been contacted by PSE "are somewhat reluctant to [give the City a firm price] since the City's load is [1.5] aMW. They typically want to deal in loads of 10 aMW or greater."[11] *Exhibit No. 102 (e-mail, 9/30/98, Campion to Khtaian).* Mayor Maxwell testified the City was unable to obtain a hedge. *TR. 365 (Maxwell).*

66 Georgia-Pacific also attempted financial hedging during the early months of market price volatility. Mr. Cunningham testified that Georgia-Pacific obtained a one-month hedge for July following the initial price spike in June 2000. *TR. 799 (Cunningham).* At the end of the hedge period, Georgia-Pacific determined it had spent $700,000 more under the hedging instrument than it would have spent without the hedge. *Id.* Mr. Cunningham testified further that

> [a]t this point in time, we were given advice that this is not the time to lock in the higher cost for a longer period of time. We decided to go for the month of August without a hedge—and we were in the [midst] of conversations with Puget Sound Energy at this point relative to what's termed a buy-sell arrangement and thought that that had promise. Furthermore, we thought that come the fall time frame, and we had some projections to indicate this to be the case, that prices would tend to come down from the peak pricing in the summer months, so we were looking ahead past August to the fall.

[11] The "1.5 aMW" is inserted in brackets because it is partially obscured in Exhibit No. 102. However, we note that this is in line with other evidence that shows the City's load is in the range of 1.5 to 2.0 aMW. *See, e.g.,* Exhibit No. 19 (Records Requisition No. 2—City of Anacortes annual load).

TR. 799-800 (Cunningham). As previously discussed in Section II.C.1. of this Order, the hoped-for buy-sell arrangement was not successfully negotiated with PSE due to the company's concern at the time over its legal implications.

67 Physical hedges in the form of alternative supplies of non-utility power are another option available to customers faced with high, volatile prices. CNC Containers, for example, leased and installed nine 1.25 megawatt diesel generators and disconnected from PSE on December 10, 2000. *TR. 436 (Franz).* These generators power CNC Containers' facility at a cost of approximately $120-$140 per MWh. *TR. 483 (Franz).* Mr. Franz testified that this form of physical hedging is working out as a marginal solution "at best." *TR. 437 (Franz).* He testified that there are environmental issues associated with burning approximately 440,000 gallons of diesel fuel a month, and a number of operational difficulties associated with the use of multiple generation units. *TR. 437-38 (Franz).* CNC Containers' current permit that allows it to operate diesel generators expires at the end of April 2001, and it requires the company to remove the generators by May 1, 2001. *TR. 476, 484-85 (Franz).* Mr. Franz testified that based on "lots of discussions with the Olympic Air Pollution Control Authority . . . their position is now it's highly unlikely that they will extend the air permit." *TR. 485 (Franz).*

68 Tesoro is another Schedule 48 customer that is beginning to use physical hedges in the form of temporary diesel generators. *TR. 495 (Crawford).* Mr. Crawford testified that Tesoro is "pursuing installing, I think, up to 12 of these temporary emergency generators to help supplement most of the power for the refinery, not all of it." *Id.* Like Mr. Franz, Mr. Crawford testified to operational and maintenance issues associated with using diesel generators. *TR. 495-96 (Crawford).* The cost of the electricity produced by Tesoro's generators is between $133 to $144 per MWh. *TR. 504 (Crawford).* Mr. Crawford understands that Tesoro can operate its generators without an emissions permit for 90 days; after that, a permit will be required. *TR. 504 (Crawford).* In addition to diesel generators, Tesoro has effected physical hedging by implementing "emergency power curtailment procedures where we actually put on our steam emergency drive pumps in a lot of our units." *TR. 494 (Crawford).* Tesoro also has effected demand side reductions by curtailing approximately 20 percent of its throughput of crude petroleum. *Id.* Mr. Crawford describes these measures as "very extraordinary moves that we have taken in an emergency basis." *TR. 498 (Crawford).* He does not consider diesel generation to be a viable, long-term solution. *TR. 498-99 (Crawford).*

69 The City of Anacortes also has resorted to a physical hedge in response to the high prices experienced in 2000. At the time of hearing, the City was operating a diesel emergency generator on a temporary basis "to try to get around the high costs of electricity, the high and unreasonable costs of electricity that we have experienced over the course of the last month." *TR. 372 (Maxwell).* The per MWh cost to the City for operating the generator is approximately $110. *TR. 405 (Maxwell).* Mayor Maxwell does not view this as a long-term solution for the City. *TR. 373 (Maxwell).* Mayor Maxwell believes the City's permit from the Northwest Air Pollution Control Board is tied to emissions levels, but, in any event, is for a period of 90 days. *TR. 416 (Maxwell).* Like other witnesses, Mayor Maxwell testified to operational difficulties and to the environmental concerns associated with operating such generators. *TR. 371-74 (Maxwell).*

70 Georgia-Pacific has installed approximately 15 megawatts of temporary generation to restore a portion of its overall operation that requires more in the range of 40 megawatts at full production. *TR. 803-04 (Cunningham).* The per megawatt cost of alternative physical power from diesel generation is in the range of $110 to $125. *TR. 821 (Cunningham).* Georgia-Pacific faces operational and environmental permitting issues just as other customers who have undertaken this form of physical hedging. *TR. 804-05 (Cunningham).* In addition, Georgia-Pacific simply has run out of room to locate additional generators unless it locates to "a generating farm, you might say, farther away." *TR. 804 (Cunningham).*

71 Another means by which customers might achieve price stability and lower prices is through a forward contract between the customer and an independent power producer or marketer, with PSE as the nominal purchaser and reseller at pass-through costs for the commodity—a so called buy-sell arrangement. So far, at least, buy-sell has not proven to be an available option for the Schedule 48 and Special Contract customers. Like all other mechanisms that might be available to customers under the terms of the Optional Price Stability provision in Schedule 48 and the Special Contract, to effect this mechanism it is necessary for the customer to work with PSE and negotiate satisfactory terms.[12] Efforts by Georgia-Pacific to achieve such an agreement under

[12] We distinguish here between alternatives for financial and physical hedging that the customers might have achieved for themselves without regard to the Optional Price Stability provisions of the tariffs, and those that are generally provided by those tariff provisions. By definition, any price stability mechanism effected via the tariff requires PSE's participation and cooperation. Price stability options

the Optional Price Stability provision of its Special Contract with PSE during the summer of 2000 failed, as we discussed above in this section and in Section II.C.1. of our Order. Lately, PSE has filed for approval of Schedule 448, which it presents as a tariff PSE hopes will largely, if not entirely, replace Schedule 48. Proposed Schedule 448 provides for buy-sell arrangements. The filing has been suspended by the Commission. *WUTC v. PSE, Complaint and Order Suspending Tariff Revisions, Docket No. UE-010038 (January 16, 2001).*

b. Commission Decision

72 We find that the available price stability options, either those that might be offered by PSE under the Optional Price Stability provisions of Schedule 48 and the Special Contract, or those available from independent sources are, under current and foreseeable circumstances, inadequate to the task they were intended to perform. Regardless of whether Complainants could have or should have secured hedges in the past, the tariff on a going-forward basis must allow reasonable methods of securing reasonable prices. In light of the unexpected volatility that has developed in the wholesale power market, financial hedges either are unavailable, or are available only at exceedingly high prices. Physical hedges in the form of alternative supplies of non-utility power (*i.e.*, temporary diesel generators) suffer from various operational problems, are inefficient, are not adequate in all cases to supply sufficient power to keep larger facilities up and running, and pose significant environmental risks for the communities in which they are operated. Physical/financial hedges in the form of buy-sell options are not yet available. On balance, we find that the tariffs that provide for market-index based rates under Schedule 48 and the Special Contract are no longer just and reasonable unless customers are afforded terms and conditions of service that include meaningful optional price stability under the Optional Price Stability provisions of the subject tariffs.

3. What Remedy Is Required?

73 Our findings of fact, discussed in the preceding sections of this Order and summarized in the Commission's Findings of Fact below, lead us to make three essential conclusions of law. First, Complainants have not shown there exists an

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available from independent financial markets, or physical options such as leased generators, do not depend on PSE's participation or cooperation and could have been effected even were there no Optional Price Stability provisions in the tariffs.

immediate danger to the public health, safety, or welfare requiring immediate agency action pursuant to RCW 34.05.479. Complainants have shown, however, that they face urgent circumstances that require us to act expeditiously on the basis of our record, developed pursuant to our authority under RCW 80.04.110 and our procedural rules in Chapter 480-09 WAC that govern adjudicative proceedings.

74 Second, we conclude that Schedule 48 and the Special Contract, which provide retail rates that are pegged to Western wholesale power markets that are volatile and exceedingly high, are not fair, just, and reasonable because customers do not have effective options to achieve price stability and reasonable rates under the Optional Price Stability provisions of Schedule 48 and the Special Contract. *RCW 80.28.010 and RCW 80.28.020.*

75 Our third essential conclusion of law follows necessarily from the second. The Commission having found that the tariffs are unjust and unreasonable, now must determine the just, reasonable, and sufficient rates, charges, regulations, practices or contracts to be hereafter observed and in force, and must fix the same by order.

76 PSE's argument that "a deal is a deal" and that Schedule 48 and the Special Contract should be left untouched by Commission action must be subordinate to our continuing statutory duty to ensure that all rates, terms, and conditions of service provided to all customers of jurisdictional utilities remain fair, just, and reasonable at all times. Our order approving Schedule 48 expressly provides that the Commission may, at any time on 60 days' notice, require PSE to re-file the tariff and bear the burden of proof to show it remains fair, just, reasonable, and sufficient, in accordance with the requirements of RCW 80.28.010. *WUTC v. Puget Sound Power and Light Co., Commission Order Approving Schedule 48 with Conditions, Docket No. UE-960696 (October 31, 1996).* Our order approving Schedule 48 also required that even if we did not notice such a hearing, PSE was required to re-file the tariff by January 1, 2001, again for the purpose of allowing the Commission to consider whether the tariff remains fair, just, reasonable, and sufficient. Our earlier Order expressly provides that we may, after hearing, continue, modify, or terminate Schedule 48. Finally, neither PSE nor its customers who agreed to Schedule 48 and the Special Contract, surrendered their statutory rights to have the Commission review the rates, terms, and conditions of service under these tariffs at any time if, for some reason, they ceased to be fair, just, reasonable, and sufficient.

77 It is, then, entirely consistent with the "deal" memorialized in Schedule 48 and the Special Contract that we now simultaneously have under consideration not only the customers' Amended Complaint, but also PSE's re-filed Schedule 48. *WUTC v. PSE, Complaint and Order Suspending Tariff Filing, Docket No. UE-010046 (filed under Docket No. UE-960696).* We note, too, that PSE also has filed another market-based tariff proposal in the form of Schedule 448, a buy-sell tariff that PSE describes as the economic equivalent of open access.

78 In light of our findings and conclusions in Phase One of this proceeding, and pending further review in this docket and/or our review of PSE's re-filing in Docket No. UE-960696, our statutes require that we effect a temporary remedy to establish rates, terms, and conditions of service that are fair, just, reasonable, and sufficient. The Commission intends to conduct further proceedings immediately in this proceeding, and expeditiously in Docket No. UE-960696. In Phase Two of this proceeding, we will hear evidence and determine the details of temporary remedies proposed in Phase One. Following that we will consider, either in a Phase Three proceeding in this docket or in Docket No. UE-960696, what permanent disposition should be made with respect to Schedule 48 specifically, and PSE's market-based tariffs generally. Proceedings in the related docket concerning PSE's request for approval of Schedule 448 also will be undertaken expeditiously.

79 Three forms of temporary relief were proposed and described with varying degrees of detail by Complainants and other Parties in the Phase One proceedings. Complainants originally proposed that PSE be required to serve them based on Schedule 49 at a rate "to be subject to refund, or surcharge, as the case may be, with interest, to reflect the difference between such Schedule 49 rate and the cost-based just and reasonable rate." *Amended Complaint at 10.* In the alternative, Complainants requested that the Schedule 48 and Special Contract rates "include an interim price cap based on Schedule 49 subject to refund or surcharge or another interim price cap level which the Commission considers to be just and reasonable." *Id.*

80 Complainants did not provide at hearing any additional detail concerning their proposals based on Schedule 49 rates. Instead, they proposed through their expert witness, Mr. Schoenbeck, to replace the Mid-Columbia indices under Schedule 48 and the Special Contract with a new index based on the forward-market price of

natural gas at Sumas, Washington. Mr. Schoenbeck proposes that pricing under these tariffs

> move off the Mid-Columbia Index and use the Sumas gas index on a bid week basis. In other words, we would use a publication such as Inside FERC, Gas Market Report, the gas price reported in the first publication of the month at Sumas would be the price used in a formulated straightforward approach. That gas price would be multiplied times the average heat rate of Puget's CT's [*i.e.*, combustion turbine], set and fixed at 12,130 btu's per kilowatt hour. To be added to that would be the variable cost of $9 per megawatt hour, in my view which would be reflective of a margin. And that would be the resulting energy rate component under Schedule 48 and the applicable contracts.

TR. 774 (Schoenbeck). Complainants represent that an index based on the price of natural gas properly tracks the cost of producing electricity since the marginal generating units that supply capacity to PSE's system and that operate throughout the interconnected electricity system in the Western wholesale power markets are fueled by natural gas.

81 Mr. Schoenbeck testified generally, based on a forecast of natural gas prices and his calculation of the cost PSE incurs to serve the Schedule 48 and Special Contract customers, that use of the proposed natural gas index would lead to lower prices and less volatility in prices than recently experienced on the Mid-C electricity index. Moreover, Mr. Schoenbeck is satisfied from his calculations that using his proposed index method would not impair PSE's ability to recover its costs to serve the Schedule 48 and Special Contract customers. *TR. 776 (Schoenbeck).* Mr. Schoenbeck notes, however, that his analyses are highly sensitive to the assumptions he has made regarding the future prices of electricity and natural gas. *TR. 904, 1018 (Schoenbeck).*

82 The third proposal put before us in Phase One is a joint proposal by Staff and Public Counsel. These Parties propose that we adopt a mechanism that would impose a "soft cap" on rates pegged to prices reflected in the Mid-Columbia Price indices. *Exhibit No. 1001 (Staff and Public Counsel Joint Proposal).* Staff and Public Counsel's proposal essentially would work as follows:

1. When the Mid-C Index is at or below $125 per MWh, the energy price is the Mid-C Index.

2. When the Mid-C Index is above $125 per MWh, the billing rate is the greater of a) $125 per MWh or b) PSE's demonstrable costs plus a margin equal to $25 per MWh, subject to a maximum billing rate equal to the Mid-C Index amount.

Id.

83 In other words, the billing rate for the energy component of the Schedule 48 and Special Contract rates is capped at $125/MWh unless PSE can demonstrate that the costs it actually incurred to serve the customers exceeds that amount up to the level of the Mid-Columbia index. If PSE demonstrates that it has incurred costs in excess of $125/MWh, the energy rate is set equal to PSE's demonstrated costs plus a margin of $25/MWh, so long as the sum does not exceed the Mid-Columbia index. If the Mid-Columbia index is at or below $125/MWh the energy component of the rate is set equal to the index, regardless of PSE's costs. The level of the soft cap is set at $125 per MWh because that is Staff and Public Counsel's estimate of the approximate cost to obtain and operate on-site diesel-fueled generation units. *TR. 1234 (Buckley)*.

84 Staff and Public Counsel represent that their proposal provides a reasonable level of price protection and stability for the customers, yet ensures that PSE will be able to recover its costs, and will retain the opportunity to earn a reasonable margin. *TR. 1265-66 (Lazar)*. According to Staff and Public Counsel, their joint proposal preserves aspects of the original Schedule 48 and Special Contract pricing because when the index is below the cap the customers face the risk of market-price fluctuations. Since the energy cost component is set by the Mid-Columbia index when it is less than $125 per MWh, regardless of PSE's costs, PSE is placed at no more risk for cost recovery than it faces today.[13] Under the proposal, only when the market price indicated by the Mid-Columbia index exceeds the $125 per MWh cap is the customers' rate tied to PSE's actual cost to provide service. In that circumstance, PSE is entitled to demonstrate its actual cost and recover those costs plus a $25 margin but never more than the Mid-Columbia index price. According to Staff and

[13] We note that under these circumstances PSE should be able to control its risk since power presumably is available to PSE at the Mid-Columbia index price. PSE thus would not need to incur costs in excess of the index.

Public Counsel, based on their analysis of PSE's costs to serve the Schedule 48 and Special contract customers, their joint proposal of a soft cap at $125/MWH provides PSE with adequate assurance that it will recover its prudently incurred costs and have the opportunity to earn a reasonable margin, just as under the present rate structure. *Id*. Finally, we note that under our Order approving PSE's merger rate plan that remains in effect through the end of this year, PSE is entitled to seek interim rate relief. *In the Matter of the Application of Puget Sound Power & Light Co. and Washington Natural Gas Co. for an Order Authorizing Merger, Fourteenth Supplemental Order Accepting Stipulation; Approving Merger, Docket No. UE-960195 (February 5, 1997).* Thus, if unanticipated events such as the failure of a major generating asset materialize and PSE's costs to serve all customers, including those whose rates would be soft-capped, result in PSE facing conditions that meet the standards for interim rate relief, PSE will be entitled to seek such relief.

85 PSE raised a number of issues regarding the operation of the soft cap proposed by Staff and Public Counsel. In particular, PSE questioned how costs incurred by PSE would be calculated and compared to the Mid-Columbia Non-Firm index *TR. 1336-39 (Buckley/Lazar);* whether these comparisons would be made on an hourly, daily or monthly basis*;* and whether application of the proposed cap would ensure that PSE recovers its prudently incurred wholesale power costs. *TR. 1365 (Buckley).*

Commission Decision.

86 We find that a temporary remedy is required to provide a reasonable level of rates and price stability for Schedule 48 and Special Contract customers that will also permit PSE to retain the ability to recover its prudently incurred costs and the opportunity to earn a reasonable return. Evaluating the three proposals that have been presented, we find that the original request made by the Complainants for service under Schedule 49 or some other PSE rate schedule is unsupported, at this time, by evidence showing how this relief would be fair, just, reasonable and sufficient. Complainants failed to show how such pricing would allow PSE to recover its costs. Finally, Complainants failed to demonstrate how such rates legally could be made subject to surcharge or refund. In fact, Complainants presented evidence which shows that under Complainants' assumptions PSE would not recover its costs if required to fix the rate

for Schedule 48 and Special Contract service at the Schedule 49 rate.[14] This Commission will not impose any remedy that impair, PSE's ability to recover reasonable costs.

87 Complainants' alternative proposal for rates based on natural gas index prices does maintain the market-based pricing concept of Schedule 48 and the Special Contract. However, the natural gas market in the West has become closely tied to volatility in the electricity markets and has itself demonstrated unprecedented price spikes and volatility over the last year. In addition, the proposal to use Sumas as the pricing point under this proposal is risky, at best, considering supply and transmission capacity constraints at the U.S./Canada border. Mr. Schoenbeck testified that using an index derived from natural gas market prices poses risks, just as does using the Mid-Columbia indices. *TR. 1010, 1038 (Schoenbeck)*. Simply replacing the instability of pricing based on an electricity index with instability in pricing based on a natural gas index does not enhance the customer's ability to obtain practical or effective price stability. Further, it does nothing to ensure that PSE will have an adequate opportunity to recover its prudently incurred costs and earn a reasonable return. We find for these reasons that the proposal for tying Schedule 48 and Special Contract customers' rates to an index based on natural gas does not meet the tests by which we measure what constitutes an appropriate remedy under the facts of this case.

88 We turn finally to the joint proposal presented by Staff and Public Counsel. As we understand the proposal, it has, in principle, the following features. When the applicable Mid-Columbia price index is below the cap, PSE can realize net benefits if it manages its power portfolio so that its costs fall below the market. When Mid-Columbia index prices exceed the cap, the risk faced by the customers is moderated because they will only pay the capped rate unless PSE demonstrates that its actual costs exceed $125. In that event, the rate to customers is tied to PSE's actual costs, rather than to the index. PSE recovers its demonstrated costs and has the opportunity to earn a reasonable margin so long as its costs and margin do not exceed the index price. The risk to PSE is the same as under the current pricing arrangement in Schedule 48 and the Special Contract. As we noted previously, PSE's risk in this regard can be mitigated because PSE presumably can always acquire power at the

[14] This is based on a comparison of columns "b," showing estimated revenue for applicable rate schedules, and "d," showing estimated incremental cost of service, in Exhibit No. 617-C, which Mr. Schoenbeck presented for Complainants.

index rate. Finally, the soft cap is proposed as a temporary remedy pending further review of Schedule 48 and related matters on a comprehensive basis.

89 We find that a cap mechanism that operates as the Staff and Public Counsel have proposed satisfies our statutory duty to establish just and reasonable rates for customers, while continuing to provide sufficient rates for PSE. The soft-cap proposal provides the customers with a greater degree of price stability and the assurance that if the wholesale index is high their rates are tied to costs. The soft cap proposal provides PSE with assurance that if Mid-Columbia prices exceed the soft-cap, the energy rate can be severed from the cap and based instead on prudently incurred costs. Thus, PSE will recover its prudently incurred costs and will have the opportunity to earn a reasonable margin.

90 We also find, however, that a number of practical implementation issues have yet to be fully addressed and clarified in the Staff and Public Counsel proposal. Key among these are the following:

1. How is the $25/MWh margin proposed to be included in PSE's costs when the Mid-Columbia market index is less than $25/MWh higher than PSE costs? Does the answer depend on whether PSE's proven costs are above or below the soft cap?

2. Is the soft cap to be applied on an hourly, daily, or monthly basis?

3. What factors are to be included and what factors are to be excluded from PSE's demonstration of costs in the event the Mid-Columbia index exceeds the soft cap? For example, are existing or future contracts with third parties covering the next several months to be considered as superior or subordinate to costs incurred to serve Schedule 48 and Special Contract customers?

4. If the Mid-Columbia index exceeds the soft cap, what process is necessary to provide PSE the opportunity to demonstrate the level of its costs?

5. What are the implications of setting a soft cap at the proposed $125/MWh, when caps in the California wholesale power market are at $150/MWh

and the Federal Energy Regulatory Commission has under consideration a Western wholesale market-wide cap?

We expect to hear from the Parties with respect to these issues in Phase Two of our proceeding.

91 With respect to the level of the soft cap in the Staff/Public Counsel proposal, we are concerned about the potential inconsistency between any soft or hard cap that may be applied in the Western wholesale power market and those applied to the retail power market. We are inclined to prefer consistency throughout the markets, retail and wholesale, when retail rates are pegged in one fashion or another to wholesale rates. Again, we expect to hear from the Parties on this issue during Phase Two, but we direct Staff to include as at least one option a soft-cap at $150.

92 Finally, considering that the requirement for a soft cap in Schedule 48 and Special Contract customers' rates reduces those customers' market risks even though they expressly assumed such risks in agreeing to service under market-indexed tariff rates, we find that it is appropriate to consider removing the risk faced by PSE should Mid-Columbia index prices again fall below the level of billing rates in Schedule 49 or otherwise applicable tariffs. Setting those billing rates as a floor for the energy cost under the capping mechanism on the low side appears to be an appropriate complement to the soft cap proposal. We expect in Phase Two of our proceeding to hear from the Parties on this issue.

93 To resolve the implementation issues we discuss above, and others that may not be immediately apparent given the seminal nature of Staff and Public Counsel's presentation during Phase One, we direct the Staff to work with PSE, Complainants, and Public Counsel to develop a fully detailed soft-cap mechanism that follows the framework of the joint Staff and Public Counsel proposal. We expect the level of detail to include proposed tariff sheets that would make the proposal ready for immediate implementation at the conclusion of Phase Two. The proposed tariff sheets should be framed as an option to be made available to Schedule 48 and Special Contract customers under the "Optional Price Stability" clauses of the tariffs. We direct Staff to make a filing with the Commission no later than January 26, 2001, to initiate Phase Two of our proceeding. If such a filing is not possible by that date, Staff is directed to inform the Commission of that fact by January 25, 2001.

FINDINGS OF FACT

94 Having discussed above all matters material to our decision, and having stated general findings and conclusions, the Commission now makes the following summary findings of fact. Those portions of the preceding discussion that include findings pertaining to the ultimate decisions of the Commission are incorporated by this reference.

95 (1) The Washington Utilities and Transportation Commission is an agency of the State of Washington, vested by statute with authority to regulate rates, rules, regulations, practices, and accounts of public service companies, including electric companies.

96 (2) Complainants have not demonstrated the existence of an immediate danger to the public health, safety, or welfare requiring immediate agency action. At most, these Parties raise the prospect of future harm if wholesale market rates remain volatile, and result in exceptionally high retail rates.

97 (3) Western wholesale power markets, and retail power rates under Schedule 48 and the Special Contract that are pegged to those markets via Mid-Columbia index pricing, have been consistently volatile and have produced unreasonably high rates for PSE's customers since June 2000. Projections are that there will be continued volatility and extraordinarily high prices in the Western wholesale power markets during 2001.

98 (4) Existing options available to customers within the terms of the Optional Price Stability provisions of Schedule 48 and the Special Contract do not provide adequate terms to achieve actual price stability at reasonable rates during periods when the Western wholesale power markets are volatile and exceedingly high relative to historic behavior and price levels.

99 (5) Schedule 48 and the Special Contract, which include retail rates that are pegged via Mid-Columbia index pricing to the Western wholesale power markets that are volatile and exceedingly high, are not fair, just, and reasonable unless customers have effective options to achieve price stability under the Optional Price Stability provisions of Schedule 48 and the Special Contract.

CONCLUSIONS OF LAW

94 Having discussed above in detail all matters material to our decision, and having stated general findings and conclusions, the Commission now makes the following summary conclusions of law. Those portions of the preceding detailed discussion that state conclusions pertaining to the ultimate decisions of the Commission are incorporated by this reference.

100 (1) The Washington Utilities and Transportation Commission has jurisdiction over the subject matter of, and all parties to, these proceedings. *Title 80 RCW.*

101 (2) Puget Sound Energy, Inc. is a "public service company" and an "electrical company" as those terms are defined in RCW 80.04.010, and as those terms otherwise may be used in Title 80 RCW. Puget Sound Energy, Inc. is engaged in Washington State in the business of supplying utility services and commodities to the public for compensation.

102 (3) Under the evidence presented in this proceeding, there is not an immediate danger to the public health, safety, or welfare requiring immediate agency action. *RCW 34.05.479.*

103 (4) Schedule 48 and the Special Contract, which include retail rates that are pegged via Mid-Columbia index pricing to Western wholesale power markets that are volatile and exceedingly high, are not fair, just, and reasonable because, under current conditions, customers do not have effective options to achieve price stability and reasonable rates under the Optional Price Stability provisions of Schedule 48 and the Special Contract. *RCW 80.28.010 and RCW 80.28.020.*

104 (5) The Commission having found, after a hearing had upon the Amended Complaint of certain PSE customers, that the rates or charges demanded, exacted, charged or collected by PSE and the rules, regulations, practices or contracts affecting such rates or charges are unjust and unreasonable, must determine the just, reasonable, and sufficient rates, charges, regulations, practices or contracts to be hereafter observed and in force, and must fix the same by order. *RCW 80.28.020.*

ORDER

105 THE COMMISSION ORDERS That PSE's Schedule 48 and the PSE/Georgia-Pacific Special Contract tariffs are not fair, just, and reasonable.

106 THE COMMISSION ORDERS FURTHER That there shall be immediate proceedings in Phase Two of this docket to establish temporary terms under the Optional Price Stability provisions of Schedule 48 and the Georgia-Pacific/PSE Special Contract that will provide customers effective options to achieve price stability and reasonable rates, consistent with the Commission's discussion in the body of this Order.

107 THE COMMISSION ORDERS FURTHER That it will consider and dispose of any remaining issues in these consolidated dockets in subsequent phases of these proceedings.

DATED at Olympia, Washington, and effective this ___ day of January 2001.

WASHINGTON UTILITIES AND TRANSPORTATION COMMISSION

MARILYN SHOWALTER, Chairwoman

RICHARD HEMSTAD, Commissioner

NOTICE TO PARTIES: This is an Interlocutory Order of the Commission. Administrative review may be available through a petition for review, filed within 10 days of the service of this Order pursuant to WAC 480-09-760.