

**BEFORE THE
WASHINGTON UTILITIES AND TRANSPORTATION COMMISSION**

WASHINGTON UTILITIES AND
TRANSPORTATION COMMISSION,

Complainant,

v.

PUGET SOUND ENERGY, INC.,

Respondent.

Docket No. UE-072300
Docket No. UG-072301
(consolidated)

BRIEF OF PUGET SOUND ENERGY, INC.

SEPTEMBER 26, 2008

TABLE OF CONTENTS

I.	INTRODUCTION	1
II.	HISTORY AND PURPOSE OF THE PCA AND THE PCORC	4
	A. Market Conditions Leading to the Establishment of the PCA and PCORC	4
	B. The PCA and PCORC Were Designed To Work Together	5
	C. The Settling Parties Anticipated a Long-Term Need for the PCORC and the Need For the PCORC Remains	8
	D. PSE Customers Have Benefited From Timely Acquisition of Resources through the PCORC.....	8
	E. The PCORC Is Not the Reason the PCA Over or Under Recovers Power Costs	9
III.	THE COMPANY NEEDS TO ACQUIRE SIGNIFICANT RESOURCES OVER THE NEXT SEVERAL YEARS, AND THE PCORC IS ESSENTIAL TO THIS PROCESS.....	10
	A. The Company’s Need To Acquire Significant Resources Is Undisputed	10
	B. The PCORC Is Necessary to Timely Recover the Incremental Cost of PSE’s Power Portfolio and to Send a Proper Price Signal to Customers	11
	C. The Alternatives Suggested by Public Counsel Are Insufficient	12
	1. The PCORC Was Created To Complement Traditional Ratemaking By Aligning the Company and Customers Goals to Move From a Market Purchase Portfolio To a Utility Portfolio Where the Company Owns and Operates Resources	13
	2. Accounting Petitions Serve a Different Purpose Than a PCORC	14
	3. General Rate Case Takes Twice As Long As a PCORC	15
	D. Elimination of the PCORC Would Only Exacerbate the Company’s Chronic Under earning	15
IV.	THE PCORC WAS DESIGNED TO UPDATE ALL POWER COSTS.....	16

TABLE OF CONTENTS

(continued)

V.	THE PCORC SHOULD CONTINUE TO BE AVAILABLE TO UPDATE POWER COSTS AS WELL AS TO INCORPORATE NEW RESOURCES INTO THE POWER COST RATE.....	19
VI.	THE PCORC SCOPE IS LIMITED	21
	A. The PCORC Deals With Power Costs	21
	B. The PCORC Does Not Pose an Unreasonable Regulatory Burden	22
VII.	THE COMPANY HAS AGREED TO REVISIONS TO THE PCORC THAT ADDRESS THE CONCERNS RAISED BY OTHER PARTIES	22
	A. Expand the PCORC To a Six Month Time Period Rather than a Five Month Period	23
	B. Formalize a Shortened Turn Around Time for Data Request Responses.....	24
	C. Provide the AURORA Model as Soon as a Confidentiality Agreement Has Been Signed	24
	D. Limit Updates to Gas Prices	24
	E. Utilize Methodologies From Last General Rate Case	25
VIII.	CONCLUSION.....	27

TABLE OF AUTHORITIES

Cases

<i>People's Org. for Wash. Energy Res. v. WUTC, 104 Wn.2d 798</i>	1
<i>POWER</i>	<i>passim</i>
<i>Puget Sound Traction, Light & Power Co. v. Publ. Serv. Comm'n, 100 Wash. 329 (1918)</i>	1

Statutes

<i>RCW 80.04.250</i>	10
<i>RCW 80.28.010(1)</i>	1
<i>RCW 80.28.020</i>	1, 10

Washington Utilities and Transportation Commission Decisions

<i>WUTC v. Puget Sound Energy, Inc., Docket Nos. UE-011570 and UG-011571, Final Order</i>	22
<i>WUTC v. Avista Corp., Docket No. UE-991606, et al., Third Supp. Order (2000)</i>	1
<i>WUTC v. Puget Sound Energy, Inc. Docket Nos. UE-060266 and UG-060267, Order 08 (Jan. 5, 2007)</i>	5, 6, 9, 17
<i>WUTC v. Puget Sound Energy, Inc., Docket No. UE-050870, Final Order (Oct. 2005)</i>	22
<i>WUTC v. Puget Sound Energy, Inc., Docket No. UE-070565, Final Order (Aug. 2007)</i>	22
<i>WUTC v. Puget Sound Energy, Inc., Docket No. UE-070565, Order 02</i>	24
<i>WUTC v. Puget Sound Energy, Inc., Docket Nos. UE-011570 and UG-011571, Twelfth Supp. Order (2002)</i>	1

I. INTRODUCTION

1. The fundamental legal question in a general rate case is whether the rates and charges proposed by the company are fair, just, reasonable, and sufficient.¹ In making these determinations, the Commission is bound by the statutory and constitutional mandate that a regulated utility is entitled to (i) reasonable and sufficient compensation for the service it provides² and (ii) the opportunity to earn “a rate of return sufficient to maintain its financial integrity, attract capital on reasonable terms, and receive a return comparable to other enterprises of corresponding risk.”³ All the parties in this proceeding have either signed or do not object to five (5) settlement stipulations that effectively resolve every issue in this case⁴ except one. The settling parties have agreed that the terms of the settlements, including the revenue requirement of \$130.2 million for electric and \$49.2 million for gas, provide for rates that are fair, just, reasonable and sufficient.

2. The single remaining issue in this general rate case is whether the power cost only rate case (“PCORC”) should continue to be available to Puget Sound Energy, Inc.’s (“PSE” or the “Company”) as a mechanism for adjusting the Company’s power costs and bringing in new resources. The PCORC is a key component of the Power Cost Adjustment (“PCA”) Mechanism, both of which were originally approved by the Commission in WUTC Docket No. UE-011570.⁵ When initially established, the parties envisioned that the PCA mechanism, which includes the PCORC, would be a long-lived mechanism and its existence today is as vital as when the mechanism was initially established in 2002.

¹ RCW 80.28.020; *People's Org. for Wash. Energy Res. v. WUTC*, 104 Wn.2d 798, 808 (1985) (“POWER”).

² See *POWER*, 104 Wn.2d at 808; *Puget Sound Traction, Light & Power Co. v. Publ. Serv. Comm'n*, 100 Wash. 329, 334 (1918); RCW 80.28.010(1).

³ *WUTC v. Avista Corp.*, Docket No. UE-991606, *et al.*, Third Supp. Order at ¶ 324 (2000).

⁴ The settlement stipulations are as follows: (1) Multiparty Settlement Re: Electric Rate Spread and Electric Rate Design, Exh. No. B-1; (2) Partial Settlement RE: Natural Gas Rate Spread and Rate Design Exh. No. B-2; (3) Multiparty Settlement Re: Emergency Response and Storm Preparedness Exh. No. B-3; (4) Partial Settlement Re: Service Quality, Meter and Billing Performance and Low Income Bill Assistance, Exh. No. B-5; and (5) Partial Settlement Re: Electric and Natural Gas Revenue Requirements, Exh. No. B-6.

⁵ See *WUTC v. Puget Sound Energy, Inc.*, Docket Nos. UE-011570 and UG-011571, Twelfth Supp. Order at ¶ 63 (2002).

3. PSE has provided evidence demonstrating the continued need for the PCORC, and Commission Staff has supported the continuation of the PCORC with some minor revisions. Since its approval by the Commission, the PCORC has been a beneficial regulatory tool that has allowed PSE to obtain timely recovery of its long term power resource needs.

4. Customers have benefited and will continue to benefit from the Company's ability to bring new cost effective resources on line as opportunities arise, in order to meet growing load and customer service demands. Under the PCORC, PSE has been able to act promptly to take advantage of new resource opportunities, such as the acquisitions of Goldendale and Fredrickson I gas generation facilities, and PSE was able to put Hopkins Ridge Wind Farm into rates as it went into service. The PCORC not only gives the Company increased flexibility but also provides assurances to counterparties that PSE will be able to deliver on its financial obligations.

5. The PCORC is important for obtaining a prudence determination for new resources on an expedited basis. Timely prudence determinations continue to be important going forward, regardless of whether the merger⁶ is approved.

6. Public Counsel and the Industrial Customers of Northwest Utilities ("ICNU") have failed to demonstrate support for their position that the PCORC is no longer needed. They do not dispute PSE's need to acquire significant long-term resources or that the PCORC provides an expedited mechanism for getting such resources into rates. They argue, incorrectly, that the PCORC circumvents the PCA. However, their explanation of the purpose of the PCA and PCORC are contrary to the evidence presented at the time these mechanisms were initially created. As discussed in more detail below, they disregard the evidence presented at the time the PCA Mechanism was created that the PCA is intended to address short-term extreme changes in power prices, while the PCORC is intended to adjust the Power Cost Rate to reflect the changes in normal power costs.

⁶ *In the Matter of the Joint Application of Puget Holdings LLC and Puget Sound Energy, Inc.*, Docket No. U-072375.

7. The PCORC does not circumvent the PCA. It sets the appropriate base line rate so that the PCA can function properly (*i.e.*, measure extreme, short-term variations from normal).

8. These parties also ignore the plain language of the settlement stipulation that created the PCORC, which states that the PCORC was intended both to (1) true up the Power Cost Rate to *all power costs* identified in the Power Cost Rate, and (2) provide a means to incorporate new resources into the Power Cost Rate.⁷

9. Further, PSE disagrees with the assertion that the PCORC should be eliminated because it is too complex. The PCORC is intended to use the same methodologies as were used in the most recent general rate case, updated for current prices and forecast periods.⁸ As discussed in more detail later, ICNU has increased the complexity of the PCORC by introducing new methodologies in these expedited procedures.⁹

10. Notwithstanding the above, PSE has agreed to several procedural changes that should address concerns regarding the PCORC's alleged complexity and expedited time frame, including (1) increasing the procedural time frame from five months to six months; (2) shortening the turn-around time for data request responses, (3) providing AURORA models at the outset of the case, if a confidentiality agreement has been signed; (4) limiting the number of power cost updates; and (5) requiring that the methodologies from the last general rate case, as updated for current prices and forecasts, be used for a subsequent PCORC.¹⁰

11. For the reasons set forth herein, PSE respectfully requests that the Commission issue an order approving the continued existence of the PCORC with the revisions discussed herein, and rejecting the position of Public Counsel and ICNU that the PCORC should be eliminated or otherwise modified.

⁷ See "Settlement Terms For the Power Cost Adjustment Mechanism", hereinafter referred to as "PCA Settlement Stipulation", Story, Exh. No. JHS-8 at 5, ¶ 8.

⁸ See *WUTC v. Puget Sound Energy, Inc.*, Docket Nos. UE-011570 and UG-011571, Lazar, TR. 2201:8-15 (. . . "I don't think it's a difficult mechanism.").

⁹ See Mills, Exh. No. DEM-12T at 5:11-14.

¹⁰ See Harris, Exh. No. KJH-9CT at 20:7-21:18.

II. HISTORY AND PURPOSE OF THE PCA AND THE PCORC

A. Market Conditions Leading to the Establishment of the PCA and PCORC

12. In her prefiled testimony and at hearing, Kimberly Harris discussed the forces that led to the creation of the PCA and PCORC in 2002. The PCA and PCORC were created in the wake of the devastating energy crisis following California's failed experiment in deregulation and market economics (the "Western Power Crisis").¹¹ Electric utilities in California had been forced to sell their generation assets and replace them with wholesale market power acquired via short-term day-ahead and real-time ("spot market") auction systems.¹²

13. Lessons learned from the Western Power Crisis were not limited to the importance of acquiring new generation or long-term purchased power resources. They included the realization that the increasing importance of the short-term wholesale power market in the industry added significant new levels of variability and risk.¹³ The industry saw extreme price increases in the spot and day-ahead markets, and financially devastated utilities were forced to purchase power in the market to meet load at the time these high prices were in effect.¹⁴ Such utilities, having purchased the power to meet customer load, had no choice but to recover such costs from their customers.¹⁵ In addition, the Western Power Crisis was fueled in part by spikes in natural gas prices at a time of extreme drought conditions.¹⁶ Industry participants were well aware of the increase in and variability of gas prices and its impact on generation costs.¹⁷

14. It was clear to the parties involved in the 2001 general rate case, as well as the Commission, that rather than facing forced divestment of its generation assets, the Company would, for the foreseeable future, need to continue to generate power for its customers and enter

¹¹ *Id.* at 10:19-11:2.

¹² *Id.* at 11:4-6.

¹³ *Id.* at 13:6-9.

¹⁴ *Id.* at 13:10-12.

¹⁵ *Id.* at 13:12-14.

¹⁶ *Id.* at 13:17-18.

¹⁷ *Id.* at 13:18-20.

into long-term (*i.e.*, greater than two years) purchased power agreements (“PPA”).¹⁸ The Western Power Crisis had taught everyone a harsh lesson in the risks of relying too much on purchasing power in short-term wholesale markets to serve load. Because many of the Company’s generation and long-term PPA resources were expiring during the coming decade and because demand for power in the Company’s service territory was continuing to grow, the parties and Commission also knew that the Company was facing an extended period in which it would need to acquire a large number of new resources.¹⁹

B. The PCA and PCORC Were Designed To Work Together

15. In response to the concerns discussed above, several parties in PSE’s 2001 general rate case²⁰ designed the PCA Mechanism, which includes the PCORC; signed the PCA Settlement Stipulation; and recommended approval of the PCA Mechanism to the Commission. Though the PCORC and PCA serve different purposes, they were designed to work together.

16. The PCA was created to address extreme, short-term imbalances between power cost recoveries and actual power costs.²¹ These are the costs that reflect current market issues and risks such as hydro and load volatility that are largely uncontrollable by the Company. The PCA was designed to track the power costs that deviate from normal resource costs included in the Power Cost Rate²² for each 12-month PCA period. The bands in the PCA are used to determine the sharing of the over or under recovery of power costs between customers and the Company within each 12-month PCA period. The purpose of the surcharge under the PCA was

¹⁸ See Harris, Exh. No. KJH-9CT at 11:14-17; *see also* *WUTC v. Puget Sound Energy, Inc.* Docket No. UE-011570 and UG-011571, Lott, TR. 2170:2-2172-6.

¹⁹ See Harris, Exh. No. KJH-9CT at 11:17-12:3.

²⁰ The parties included PSE, the Commission’s regulatory staff, the Public Counsel Section of the Attorney General’s Office (“Public Counsel”), the Kroger Company, AT&T Wireless Services (“AT&T”), Northwest Energy Coalition (“NVEC”) jointly with Natural Resources Defense Council (“NRDC”), and Cogeneration Coalition of Washington. *See* PCA Settlement Stipulation, Exh. No. JHS-8 at 1.

²¹ *See* *WUTC v. Puget Sound Energy, Inc.*, Docket Nos. UE-011570 and UG-011571, Lott, Exh. No. 562T at 13:7-13. Additionally, as recently as 2006 the Commission reaffirmed that the PCA is intended to deal with extreme events. *See* *WUTC v. Puget Sound Energy, Inc.* Docket Nos. UE-060266 and UG-060267, Order 08 at ¶ 20 (Jan. 5, 2007).

²² For a definition of the PCA Power Cost Rate, *see* PCA Settlement Stipulation, Story, Exh. No. JHS-8 at 3, ¶ 5.

to either collect or refund to the customer any over or under recovery of power costs when the cumulative ending balances of the PCA periods reached \$30 million.²³ The surcharge was created in this manner to address power costs deferrals over time. The parties expected that the over and under balances would offset each other, over time, and the deferrals would be minimized.²⁴ In fact, this balancing has occurred, and the surcharge has never been triggered.²⁵

17. In contrast to the short-term imbalances captured by the PCA, the PCORC was intended to adjust rates for long-term trends in production related costs. The PCORC was intended to adjust both fixed and variable power costs in addition to allowing for the timely inclusion of resource acquisitions in rates.²⁶ The settling parties designed the PCORC to adjust the normalized production related power costs used to determine the PCA Power Cost Rate. In turn, the Power Cost Rate is used in the PCA to determine the over or under collection of actual power costs during a PCA period.²⁷ When the Company's portfolio changes, or when costs currently included in the Power Cost Rate change due to contractual agreements or market prices, it is necessary to have a PCORC so that there is a proper measurement of normalized power costs during the future PCA period.²⁸ In the Company's last general rate case, the Commission confirmed the importance of resetting the baseline rate to reflect normalized power costs. "The Commission's goal is to set the Power Cost Baseline Rate as close as possible to what is expected to be experienced in the rate year and expect this to continue going forward."²⁹

18. Another key component of the PCA Mechanism, when it was established, was the Least Cost Plan ("LCP"), also referred to as the "Integrated Resource Plan" ("IRP")), Section E

²³ See PCA Settlement Stipulation, Story, Exh. No. JHS-8 at 2-3.

²⁴ See *WUTC v. Puget Sound Energy, Inc.*, Docket Nos. UE-011570 and UG-011571, Lazar, Exh. No. 551T at 3:1-20.

²⁵ See Story, TR. 593:24-25; see also Story, Exh. No. JHS-14T at 35:20-36:4; see Exh. Nos. JHS-27 and JHS-28 (showing deferral balance moved from \$25 million to \$5 million in 2006, and a credit of \$3.2 million in 2007 leaving the customer deferral balance at \$1.8 million).

²⁶ See PCA Settlement Stipulation, Exh. No. JHS-8 at ¶ 8; Lott, Exh. No. 562T at 14.

²⁷ See Story, Exh. No. JHS-1CT at 61:8-62:4.

²⁸ See *id.* at 61:8-62:4; see also *WUTC v. Puget Sound Energy, Inc.*, Docket Nos. UE-011570 and UG-011571, Lott, Exh. No. 562T at 14:1-6.

²⁹ See *WUTC v. Puget Sound Energy, Inc.* Docket Nos. UE-060266 and UG-060267, Order 08 at ¶ 22 (2006) .

of the PCA Settlement Stipulation. In this section of the Settlement Stipulation, the parties emphasized that the Company was expected to increase its capability of reviewing long term resource development and move away from a short-term, market purchase type of portfolio.³⁰

This is further discussed by Commission Staff witness Mr. Lott at the settlement hearing:

One of the parts of this mechanism is . . . the integrated resource planning process, and that new resources should be coming out of the integrated resource planning process. And in other words, there should be discussion about and the company should be following that process. . . .

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

If that's a direction that does not come out of least cost planning, if least cost planning moves more toward short-term portfolio, then this portion of this will have to be looked at again to make sure that we're still consistent with the intent of costs flowing through this mechanism.³¹

19. The purpose of the PCA, including the IRP and the PCORC, therefore, was to develop and approve some regulatory means by which the Company could better deal with the financial pressures associated with changing market prices and bringing new resources into PSE's power portfolio to move from a short-term market purchase type of portfolio to a utility-type portfolio. The PCORC complements traditional rate making by aligning the goals of PSE and customers to move to long-term resources.³² The PCORC also resolves issues of prudence in a timely fashion, and it minimizes the cash flow constraints the Company experiences both during acquisitions and long-term changes to its power costs.

³⁰ See Story, Exh. No. JHS-8 at 7.

³¹ See *WUTC v. Puget Sound Energy, Inc.*, Docket Nos. UE-011570 and UG-011571, Lott, TR. 2170:15-2171:21.

³² See *WUTC v. Puget Sound Energy, Inc.*, Docket Nos. UE-011570 and UG-011571, Lazar, TR: 2175:24-2177:8 and Lott, TR. 2175:16-20.

C. The Settling Parties Anticipated a Long-Term Need for the PCORC and the Need For the PCORC Remains

20. Commission Staff, in the 2001 settlement hearing, explained that the PCA Mechanism, including the PCORC, would be a long-lasting process, subject to occasional modifications, and a process that would be long-lived: “This mechanism would hopefully last for a long period time, with modifications that take care of unintended consequences....”³³ Commission Staff explained that if unintended consequences do occur, the intent was to modify the process rather than eliminate it.³⁴ Mr. Lazar, Public Counsel’s witness supporting the PCA Settlement, agreed that the PCA Mechanism should be long-lived: “My guess is that unless there’s some egregious problem with it, that [a general rate case] will be the time that the parties would look to fine-tune it.”³⁵ As recently as the 2006 general rate case, no party identified any “egregious problem” that would warrant substantial changes to the process, much less its elimination.

D. PSE Customers Have Benefited From Timely Acquisition of Resources through the PCORC

21. Customers have benefited from PSE’s ability to timely acquire resources and obtain regulatory approval of such resources through the PCORC.³⁶ Despite the risk factors PSE faces, including low internal cash flow and inability to actually earn the return on equity that has been authorized, as described by Mr. Markell,³⁷ PSE’s customers have benefited by the addition of low cost resources through the PCORC, including Fredrickson I in 2003, Hopkins Ridge in 2005 and Goldendale in 2007. The shortened regulatory process allowed the Company to bring these resources into its portfolio without exacerbating these risk factors. The Company and its

³³ *WUTC v. Puget Sound Energy, Inc.*, Docket Nos. UE-011570 and UG-011571, Lott, TR:2205:5-8. In fact, PSE has agreed to certain modifications of the PCORC and to review the PCA sharing bands. *See* Partial Settlement Re: Electric and Natural Gas Revenue Requirements at 9:9-18.

³⁴ *See WUTC v. Puget Sound Energy, Inc.*, Docket Nos. UE-011570 and UG-011571, Lott, TR:2205:9-11.

³⁵ *See WUTC v. Puget Sound Energy, Inc.*, Docket Nos. UE-011570 and UG-011571, Lazar, TR. 2209:4-7.

³⁶ *See* Story, Exh. No. JHS-1CT at 63:1-17.

³⁷ *See* Markell, Exh. EMM-1CT at 12:3-15:4.

customers benefited by PSE's opportunistic acquisition of these resources at a cost below the then-current-build costs through the PCORC.³⁸

E. The PCORC Is Not the Reason the PCA Over or Under Recovers Power Costs

22. It is not surprising that the Company has at times over recovered and at times under recovered under the PCA. As Mr. Story pointed out at hearings, this was contemplated in the design of the PCA Mechanism.³⁹ Indeed, at the time of the PCA settlement hearing in the 2001 general rate case, Mr. Lazar testified that the parties anticipated such variations in the deferral, and that the goal was for such variations to offset one another:

[T]he amount of deferred power cost must reach \$30 million before a surcharge is triggered. . . . This is likely to be relatively infrequent. . . . In most cases a "bad" year or group of years would be followed by one or more "good" years that would erase some or all of the deferred power costs before a surcharge would be triggered.⁴⁰

23. Mr. Lazar was accurate in his prediction that there would be groups of years in which the Company under earned and groups of years in which the Company over earned and that the two would balance one another to limit the triggering of the surcharge. That is precisely what PSE has experienced. The reasons for the variations from normal power costs are provided in each of the Company's annual PCA compliance filings. Typically they related to hydro runoff, temperature, natural gas and power prices, and increased loads. Thus, it is not the changing of the Power Cost Rate that causes the over or under earning. It is necessary to change the Power Cost Rate to reflect the expected power costs during a PCA period so that the PCA measures the appropriate power cost variations.⁴¹

³⁸ PSE built Hopkins Ridge, and it was able to take advantage of relatively low cost wind turbines that were then available on the market. *See WUTC v. Puget Sound Energy, Inc.* Docket No. UE-050870, Garratt, Exh. No. 54HCT at 58:13-16 and Story, Exh. No. 13 at 12.

³⁹ Story, TR. 594:7-12.

⁴⁰ *WUTC v. Puget Sound Energy, Inc.*, Docket Nos. UE-011570 and UG-011571, Lazar, Exh. No. 551T at 3:7-14.

⁴¹ *See WUTC v. Puget Sound Energy, Inc.*, Docket Nos. UE-060266 and UG-060267, Order 08 at ¶ 22 (Jan. 5, 2007).

III. THE COMPANY NEEDS TO ACQUIRE SIGNIFICANT RESOURCES OVER THE NEXT SEVERAL YEARS, AND THE PCORC IS ESSENTIAL TO THIS PROCESS

A. The Company's Need To Acquire Significant Resources Is Undisputed

24. The external forces that were the drivers behind creating the PCORC⁴² remain today. PSE is still faced with expiring generation and long-term PPA resources, as it faces increased load due to customer growth.⁴³ PSE also still faces increasing fixed and variable power costs. The PCORC is a tool proven useful to mitigate these challenges, and it continues to be a valuable regulatory tool for resource acquisition, planning, and financing.⁴⁴

25. An electric utility is obligated to meet the public's continuing demand for power, and this requires that the company continue to seek supply sources.⁴⁵ In PSE's 2003 PCORC, 2004 general rate case, 2005 PCORC, 2006 general rate case, and 2007 PCORC, the Company extensively documented its need to acquire additional power resources now and well into the future. No party contested PSE's need to acquire additional resources in any case in the past six years, and this proceeding is no exception. The Company has a continuing need to acquire additional generation resources amounting to 480 aMW by winter of 2010, growing to 1,650 aMW by 2015 and to 2,125 aMW by 2020.⁴⁶ The Company's IRP illustrates that this need will continue. "The combination of economic growth and expiring supply contracts means that PSE faces large electric resource needs in the years ahead."⁴⁷

26. Acquiring additional resources is complicated by the difficult planning environment that exists today. PSE must acquire additional resources in an environment in which new laws and rules have been and are being adopted, the demand for renewable resources and energy efficiency is rising, regional transmission access is constrained, and intermittent

⁴²See *WUTC v. Puget Sound Energy, Inc.*, Docket Nos. UE-011570 and UG-011571, Lazar TR. 2161:9-12 (discussing PSE's need to acquire significant resource needs).

⁴³ See Harris, Exh. No. KJH-1HCT at 12:2-6.

⁴⁴ See Harris, Exh. No. KJH-1HCT at 12:15-18; see also Exh. No. KJH-5 at 8.

⁴⁵ RCW 80.04.250 and RCW 80.28.020. See also *WUTC v. Puget Sound Power & Light Co.*, Docket Nos. U-89-2688-T and U-89-2955-T, Third Supplemental Order (January 1990).

⁴⁶ See Harris, Exh. No. KJH-1HCT at 12:11-13.

⁴⁷ Harris, Exh. No. KJH-5 at 8.

resources must be integrated.⁴⁸ These factors all lead to substantial uncertainty in resource planning and acquisition.

27. Specifically, PSE witness Kimberly Harris describes in detail the following challenges that PSE faces in resource acquisition:

- (i) a new renewable energy portfolio standard, also known as the Energy Independence Act, which requires the Company to meet 15% of customers' needs by 2020 with renewable energy resources, as defined in RCW Chapter 19.285;
- (ii) increasing cost pressures as a result of high demand for renewable and gas resources, price increases in the commodities markets, and a marked decline in the Dollar exchange rate with the Euro and other currencies; and
- (iii) increasing financial pressures, as the Company must invest approximately \$1.9 billion to acquire the necessary energy resources to meet our customers' needs. This significant amount of financial investment will strain the Company's ability to make such investments.⁴⁹

28. PSE must navigate these challenges in order to pay cash to asset sellers, contractors or vendors engaged in the sale or construction of a facility. Any enterprise with which the Company partners or from which the Company purchases a resource will be concerned about the Company's ability to make such payments in a timely manner. The PCORC process was designed to ease the effects of this cash requirement.

B. The PCORC Is Necessary to Timely Recover the Incremental Cost of PSE's Power Portfolio and to Send a Proper Price Signal to Customers

29. The PCORC is an essential regulatory mechanism to ensure rates reflect the costs of power utilized by the customers. It is critical to ensuring that the customers receive proper price signals. In order to minimize cash flow constraints, it is important that the Company have

⁴⁸ See Harris, Exh. No. KJH-5 at 22.

⁴⁹ Harris, Exh. No. KJH-9CT at 4:14-5:5.

the capabilities to include new resource acquisitions in rates at the same time (or very shortly after) the new resources are placed into service.⁵⁰

30. Investors also rely on the PCORC process for assurance that PSE will be able to repay borrowed capital in a timely manner. This is especially important in this extreme financial market. If rating agencies and the capital markets view the Company as a risky investment because the Company may have trouble raising cash or recovering its investments in a consistent and timely manner, investors will demand more return for their investment (*i.e.*, in the form of higher interest rates on debt). This will only make investments more costly for customers.⁵¹ The PCORC is an important risk-mitigating cost-recovery mechanism that investors depend on to provide some level of security and consistency.

C. The Alternatives Suggested by Public Counsel Are Insufficient

31. Throughout Ms. Smith's testimony there are discussions that increased revenue and load growth have the ability to offset the Company's under earnings due to increased costs. It is implied in her testimony that the Company would have the capability to earn its allowed rate of return without a PCORC through other mechanisms such as deferral accounting, filing of general rate cases, etc. But, as pointed out by Mr. Markell, the Company has failed to earn its authorized rate of return even with the PCORC and occasional deferrals of resource-type costs (*i.e.*, Goldendale).⁵² The insufficient alternatives suggested by Ms. Smith will only exacerbate the Company's under earning.

⁵⁰ See *WUTC v. Puget Sound Energy, Inc.*, Docket Nos. UE-011570 and UG-011571, Lazar, TR. 2177 and Lott, TR. at 2178.

⁵¹ See Harris, Exh. No. KJH-9CT at 6.

⁵² See Markell, Exh. No. EMM-CT at 12:4-15:4.

1. The PCORC Was Created To Complement Traditional Ratemaking By Aligning the Company and Customers Goals to Move From a Market Purchase Portfolio To a Utility Portfolio Where the Company Owns and Operates Resources

32. For the past six years, the PCORC has provided regulatory certainty and stability that is critical for the Company as it moves from a utility with a market purchase portfolio to a utility that owns and operates its resources. The challenges PSE faced six years ago as it began this transformation continue today, and it is imperative that the Company continue to have the PCORC available to complement other traditional ratemaking tools and allow PSE to move quickly and opportunistically to acquire needed resources.

33. Ms. Smith's argument that traditional ratemaking is sufficient for PSE and provides incentive to control costs misses the point of why the PCORC was created in 2002. As discussed previously, in the wake of the Western Power Crisis, the Commission and parties to PSE's general rate case realized that traditional ratemaking could not timely or proactively address the Company's challenges with respect to the volatility of market prices nor could it support the Company's efforts to acquire electric generation resources.⁵³ As new resources are generally more expensive in the first few years than the market power they are replacing, a mechanism needed to be put in place that would provide the Company a timely prudence determination and recovery in rates. That mechanism was the PCORC.

34. It is over the life of the plant that these new resources save money for customers. As shown in the chart provided by Ms. Smith, the revenue deficiency for Fredrickson I in the 2003 PCORC was \$18.3 million,⁵⁴ in contrast to the \$84.8 million net present value savings over 20 years.⁵⁵ For Hopkins Ridge, the 2005 PCORC showed a revenue deficiency of \$38.5 as compared to the net present value savings of approximately \$30 million over 20 years.⁵⁶ For Goldendale, the 2007 PCORC listed a revenue deficiency of \$31.4 million as compared to the

⁵³ See *WUTC v. Puget Sound Energy, Inc.*, Docket Nos. UE-011570 and UG-011571, Lott, Exh. No. 562T at 13:10-14:9 and Lazar, Exh. No. 551T at 3.

⁵⁴ See Smith, Exh. No. LS-1CT at 24:3.

⁵⁵ See *WUTC v. Puget Sound Energy, Inc.* Docket No. UE-031725, Markell, Exh. No. 148HC at 7.

⁵⁶ See *WUTC v. Puget Sound Energy, Inc.*, Docket No. UE-050870, Elsea, Exh. No. 38T at 53.

benefit associated with adding Goldendale to the portfolio which was in excess of \$100 million over the remaining life of the project.⁵⁷

35. Ms. Smith would have the Company absorb the fixed costs of operating and financing the resource (as well as the variable costs of operating the resource) by eliminating the PCORC and thus delaying the recovery of such resources.

2. Accounting Petitions Serve a Different Purpose Than a PCORC

36. Contrary to arguments made by Public Counsel and ICNU, the availability of accounting petitions to defer costs related to resource acquisitions does not support elimination of the PCORC. In the short term, accounting petitions serve the limited purpose of protecting the income statement from expenses that should be borne by the customer and protect the Company from additional under earnings; however, they provide for no cash flow until a prudence determination has been made and resources are included in rates.

37. There are many uncertainties associated with accounting petitions. There is no guarantee that the parties will support an accounting petition when taken before the Commission or that the Commission will grant a petition for such an accounting order.⁵⁸ Moreover, there is no statutory time frame by which the Commission must rule on an accounting petition, and petitions have, at times, languished for many months without resolution.

38. Even if the accounting petition is approved, the additional delay of several months or more before an acquisition is determined to have been prudent, which would only be done in a general rate case under Public Counsel and ICNU proposal, is perceived as an additional risk to PSE's recovery of invested funds. Such delay and uncertainty are unsettling to financial markets, and as discussed previously, will only lead to increased credit costs.

39. Further, deferral of costs does not cure the cash flow problems that would be created by elimination of the PCORC. The recovery of costs deferred through an approved

⁵⁷ See *WUTC v. Puget Sound Energy, Inc.*, Docket No. UE-070565, Story, Exh. No. 91T at 18:7-13.

⁵⁸ See *Harris*, Exh. No. KJH-9CT at 7:13-15

accounting petition only begins at the completion of the next PCORC or general rate case. In the meantime, the Company has to allocate or borrow cash to fund the resource acquisition. Until revenues are collected to repay the investment, the Company has to turn to other sources of cash for its operations or for acquiring additional resources.

3. General Rate Case Takes Twice As Long As a PCORC

40. A general rate case process takes at least twice as long as a PCORC to prepare and litigate to conclusion. As Commission Staff witness Mr. Parvinen points out, past PCORCs have resulted in a time savings of about six months to bring new resources into rates.⁵⁹ “This savings in months helps the Company match more closely the in-service date of new resources with retail rates.”⁶⁰

41. If the PCORC were eliminated, PSE would experience longer, more difficult cash flow constraints because it can take up to a year and a half to two years before an investment that has been acquired and put into service for customers can be included in rates through a general rate case.

D. Elimination of the PCORC Would Only Exacerbate the Company’s Chronic Under earning

42. The Company has provided undisputed evidence of its chronic under earning over the past several years.⁶¹ As Mr. Markell testified, “[t]he Company suffers from chronic under-earnings in its regulated business. Since 2003, the Company has under-earned its authorized rate of return every year.”⁶² Elimination of the PCORC in this period of heavy resource acquisition would exacerbate regulatory lag, worsen already existing financial pressures,⁶³ and take away PSE's opportunity to earn a sufficient rate of return.⁶⁴

⁵⁹ See Parvinen, Exh. No. MMP-1T at 5:10-17.

⁶⁰ *Id* at 5:16-17.

⁶¹ See Markell, Exh. No. EMM-1CT at 12:2-15:4; *see also* Markell, Exh. No. EMM-5C.

⁶² Markell, Exh. No. EMM-1CT at 12:4-6; *see also* Markell, Exhibit No. EMM-5C.

⁶³ See Markell, Exh. No. EMM-1CT at 30:6-7.

⁶⁴ See *POWER* 104 Wn.2d at 808.

43. Public Counsel would have the Commission believe that the Company has the opportunity to earn its return under “traditional ratemaking” methodologies;⁶⁵ however Public Counsel ignores the fact that even with the PCORC the Company has not been able to earn its allowed rate of return. Public Counsel's own analysis shows that without the PCORC “overall customers would have paid somewhat less”, yet Public Counsel argues that “the Company would not have suffered major financial losses.”⁶⁶ Even if the Company did not suffer “major financial losses,” any loss due to customers paying less would create further under earnings for the Company.

44. Public Counsel also does not explain how revenue growth between general rate cases has the potential to offset increases in costs when the revenue growth is already included in Mr. Markell’s analysis and when revenue growth associated with 23.7%⁶⁷ of power cost recoveries are credited back to customers in the PCA.⁶⁸ Public Counsel’s argument that “traditional ratemaking allows an opportunity for the recovery of all costs” rings hollow based on Public Counsel's attempt to eliminate the ability of the Company to update its resource costs, yet keep the benefit of crediting sales growth back to customers.⁶⁹

IV. THE PCORC WAS DESIGNED TO UPDATE ALL POWER COSTS

45. Public Counsel and ICNU incorrectly claim that the main objective of the PCORC is to provide a timely inclusion of the costs of new resources as opposed to updating all production related costs. They claim that the PCORC is being misused because in the three PCORC proceedings the amount of revenue requirement needed to recover the new resource was only a fraction of the total revenue deficiency requested in each PCORC filing.⁷⁰ These arguments ignore the fact that resources are only one part of the power cost calculation. The

⁶⁵ See Smith, Exh. No. LS-1CT at 32:5-7.

⁶⁶ See Smith, Exh. No. LS-1CT at 19:12-13.

⁶⁷ See Partial Settlement Agreement Re: Electric and Natural Gas Revenue Requirements, Attachment 4, at 1. (\$15.611 (L40 Fixed Rate Component)/\$65.74 (L41 Power Cost Rate) = 23.7%)

⁶⁸ See Story, Exh. No. JHS-14T at 41:7-42:13.

⁶⁹ See Smith, Exh. No. LS-1CT at 33:5-8.

⁷⁰ See, e.g., Smith, Exh. No. LC-1CT at 13:11-14:17, Schoenbeck, Exh. No. DWS-1T at 6:16-21.

purpose of the PCORC is to update all power costs so that the PCA Mechanism measures the difference between actual unanticipated or uncontrollable power costs as compared to the normal, expected power costs for the rate year. In order to measure this difference, it is necessary to know the normal, expected power costs, which the PCORC provides. The Commission has recognized the importance of updating the Power Cost Rate:

The Commission has reset the Power Cost Baseline Rate on several occasions The Commission’s goal has been to set the baseline as close as practicable to what is likely to be experienced during the rate year. We expect that practice to continue and we also expect the parties to continue to refine the method and improve the data upon which we act.⁷¹

46. The Company’s portfolio will change with the inclusion of a new resource and the Company must reflect the impact of that new resource on all of the costs of providing power to customers. This was contemplated when the PCORC was established. As noted by Commission Staff witness Merton R. Lott in testimony supporting the PCA Settlement Stipulation, “these single issue rate cases [PCORC] will look at *all costs* included within the PCA mechanism.”⁷² It is not feasible to bring in new resources and ignore their impacts on the overall power portfolio.

47. It is hard to understand how parties can argue that known and measurable changes in the forecast costs of providing power that electric customers consume should not be reflected in their rates. There are real limits to what the Company can do to hold down its power costs. Preventing the Company from passing through the basic costs of providing electric service to customers is inconsistent with the fundamental regulatory compact that a regulated utility be given the opportunity to recover its costs.⁷³

48. Public Counsel also errs in claiming that because of the PCORC filings, the Company is not incented to hold down costs and that the customers and the Company are not treated symmetrically. As Ms. Harris testified, the Company has significant incentive to control

⁷¹ *WUTC v. Puget Sound Energy, Inc.*, Docket Nos. UE-060266 and UG-060267, Order 08 at ¶ 22.

⁷² *WUTC v. Puget Sound Energy, Inc.*, Docket Nos. UE-011570 and UG-011571, Lott, Exh. No. 562T at 14:7-9 (emphasis added).

⁷³ *POWER v. WUTC* 104 Wn.2d at 808 (1985).

its power costs and the historical evidence shows that the Company has reasonably controlled its power costs:

Because of the sharing bands and the uncontrollable nature of much of the financial risk to which the Company is exposed, the Company is absolutely incented to control its power costs (as well as its other costs) to the greatest extent reasonably possible. . . . In addition, PSE's operations and hedging strategies, which are reflected in PSE's short-term power costs, were deemed prudent in each of PSE's five PCA Compliance filings that have been completed to date—proof that PSE is properly and reasonably addressing the costs of the power to meet customer demand.⁷⁴

49. Public Counsel witness Ms. Smith ignores testimony and evidence in the 2001 general rate case in reaching her conclusion that “the addition of new resources would be the major driver behind PCORC filings.”⁷⁵ The testimony of Commission Staff witness Merton R. Lott at the time the PCORC was established demonstrates the intent that the PCORC would be available both to update power costs to reflect increased costs due to existing resources and to update costs associated with new resources:

[I]n the collaborative PSE expressed the need to deal with increased costs associated with adding new resources for growth or replacing old low-cost resources. Thus, new resources will not be recovered directly through the PCA, *but the Company may periodically update its general rates to reflect increased power supply costs associated with new resources or increased costs of existing resources.*⁷⁶

(Emphasis added). Mr. Lott's testimony is consistent with the PCA Settlement Stipulation, which states that in paragraph 8 that the PCORC would true up the Power Cost Rate to *all power costs* and would also be used to add new resources to the Power Cost Rate. It should also be noted that under the PCORC process and the PCA compliance filing, all parties have the ability to review any power costs (long term or short term) for prudence.

⁷⁴ Harris, Exh. No. KJH-9CT at 16:15-17:1.

⁷⁵ Smith, Exh. No. LS-1CT at 23:16-18.

⁷⁶ *WUTC v. Puget Sound Energy, Inc.*, Docket Nos. UE-011570 and UG-011571, Lott, Exh. No. 562T, 14:1-3.

V. THE PCORC SHOULD CONTINUE TO BE AVAILABLE TO UPDATE POWER COSTS AS WELL AS TO INCORPORATE NEW RESOURCES INTO THE POWER COST RATE

50. The PCORC is important for obtaining a prudence determination for new resources on an expedited basis. Timely prudence determinations continue to be important going forward, regardless of whether the merger is approved. The Company cannot recover its investment in a new resource until it obtains a prudence determination in a general rate case or PCORC. Until the revenues are collected to repay the investment, the Company has to turn to other sources of cash for its operations or for acquiring additional resources. This could place serious financial constraints on the Company⁷⁷ at a time when the Company is facing the need to acquire significant resources over the next decade.

51. PSE and Commission Staff have provided evidence demonstrating the continued need for the PCORC.⁷⁸ Since its approval by the Commission, the PCORC has been a beneficial regulatory tool that has allowed PSE to obtain timely recovery of its long term power resource needs, and provide benefits to customers as explained in more detail below. Through its Integrated Resource Plan, PSE has estimated the need to acquire resources for 2,125 average megawatts (“aMW”) by 2020.⁷⁹ PSE faces challenges in acquiring these resources due to increasing cost pressures associated with financing acquisitions and, in addition, the increase in the cost of the available resources themselves. Over the past five years the Company has been very successful in taking advantage of resource acquisition opportunities as they have arisen, to obtain low cost resources and put them into service for its customers' benefit. Now is not the

⁷⁷ Harris, Exh. No. KJH-9CT at 8:5-10.

⁷⁸ See Parvinen, Exh. No. MPP-1T at 5:13-17. Mr. Parvinen discussed the time savings that results from the use of a PCORC rather than a general rate case:

[R]ates from PCORCs have gone into effect an average of 7 months earlier than general rate cases. PCORCs are designed currently to be completed within 5 months of the filing and general rate cases within 11 months of filing, hence a time savings of 6 months. This savings in months helps the Company match more closely the in-service date of new resources with retail rates.

Id.

⁷⁹ See Harris, Exh. No. KJH-1HCT at 12:11-13.

time to change the regulatory environment under which the Company can adjust its power cost portfolio in a relatively timely and simplified manner.

52. The framers of the PCORC mechanism expressly stated that the purpose of the PCORC was twofold: (1) it would be a periodic proceeding specific to power costs that “would true up the Power Cost Rate to *all power costs* identified in the Power Cost Rate.” (emphasis in original); and (2) it would be a means to incorporate new resources into the power cost rate.⁸⁰ Thus, the PCORC has always been as much about updating the level of all power costs recovered in rates generally as about bringing the costs of new resources into rates on an expedited basis.

53. ICNU has proposed that a PCORC should be filed only when PSE acquires a new resource. Mr. Schoenbeck testified on behalf of ICNU stating, “In my view, the main objective of the PCORC was to provide a timely inclusion of the costs of new resource [sic] in rates.”⁸¹ Please note, however, that ICNU was not a signatory to the PCA Settlement Stipulation that instituted the PCORC mechanism.⁸² Mr. Schoenbeck's “view” of the process does not reflect the way the PCORC was intended or the way it has operated ever since it was initiated. But most importantly, it does not reflect the expressed terms of the settlement agreement. Further, Mr. Schoenbeck himself points out that PSE *has* limited every PCORC proceeding to those instances when it has acquired new resources.⁸³ Accordingly, ICNU proposes restrictions on the PCORC to correct a “problem” that does not exist.

54. Commission Staff articulated its view of the objective of the PCA and PCORC mechanisms in testimony supporting the PCA Settlement in WUTC Docket No. UE-011570.

The Company may periodically update its general rates to reflect increased power supply costs associated with new resources *or increased costs of existing resources*. These Power Cost Only rate proceedings are an exception to the general rule that a company should not be allowed to file single issue rate cases. . . . Further, these single issue rate cases will

⁸⁰ PCA Settlement Stipulation, Story, Exh. No. JHS-8 at 5.

⁸¹ Schoenbeck, Exh. No. DWS-1T at 5:15-16.

⁸² *See id.* at 3:6-8.

⁸³ Schoenbeck, Exh. No. DWS-1T at 6:15-17.

look at all costs included within the PCA mechanism. And, the Company will be required to support these rate proposals in the same detail it must support power supply costs in a general rate proceeding.⁸⁴

55. Under both ICNU and Public Counsel's proposals, they would modify the PCA to recover power costs that would be recovered under a normalized scenario—rather than using the PCA to track extremes.

VI. THE PCORC SCOPE IS LIMITED

A. The PCORC Deals With Power Costs

56. While a PCORC deals with a complex subject--the forecast of future power costs for a future load--the process is intended to be narrow in scope and can be completed in an expedited time frame. This was expressed well by Public Counsel witness Jim Lazar at the time of the 2001 settlement hearing:

Our goal here was to have a narrow process and a tight time frame. . . .
[O]ur goal was . . . to have a narrow set of issues addressed and have it addressed in a very efficient fashion. . . .⁸⁵

57. Such topics are reserved for general rate cases. Company witness David Mills also testified that while a PCORC proceeding does involve thorough and complete review of projected power costs, it excludes many other cost components that are addressed in a general rate case.⁸⁶ A PCORC does not deal with cost of money or changes in non production-related expenses or ratebase. Given this, it is appropriate that a PCORC proceeding be relegated a shorter time frame.

58. The Company has completed three PCORC proceedings since the Commission approved the PCA mechanism in 2002.⁸⁷ The parties have been able to work together during these proceedings to complete the expedited review of power costs in the timely manner

⁸⁴ *WUTC v. Puget Sound Energy, Inc.*, Docket Nos. UE-011570 and UG-011571, Lott, Exh. No. MRL-2T at 14:1-9 (emphasis added).

⁸⁵ See *WUTC v. Puget Sound Energy, Inc.*, Docket Nos. UE-011570 and UG-011571 Lazar, TR. 2158:10-17.

⁸⁶ Mills, TR. 522:18-523:4.

⁸⁷ Docket Nos. UE-031725, UE-050870 and UE-070565.

anticipated by the parties to the PCA Settlement. In addition, two of the three PCORC proceedings were successfully resolved through Commission-approved settlements.⁸⁸

B. The PCORC Does Not Pose an Unreasonable Regulatory Burden

59. Ms. Smith laments that the PCORC poses an unreasonable regulatory burden on all parties and the Commission.⁸⁹ However, the Commission expressly authorized the PCORC as an exception to the rule governing general rate increases

We established on the record, and conclude, that the Power Cost Only Rate Review provisions do fall within the exception to this rule governing general rate increase filings⁹⁰

60. As discussed above, the PCORC serves an important purpose of implementing PSE's Integrated Resource Plan as an element of the PCA Mechanism and transforming PSE's portfolio from a short-term, market power portfolio to a portfolio with owned resources.

61. Given the Commission's express authorization of the PCORC and the PCORC's limited scope, Ms. Smith's characterization of this approved regulatory mechanism as a "regulatory burden" is puzzling. The Commission should not penalize the Company by eliminating an established and well-functioning regulatory mechanism because an intervenor finds it burdensome.

VII. THE COMPANY HAS AGREED TO REVISIONS TO THE PCORC THAT ADDRESS THE CONCERNS RAISED BY OTHER PARTIES

62. The argument of ICNU and Public Counsel that the PCORC is too complex should be rejected. During cross examination ICNU used the example of a new load forecast as an indication of how the PCORC did not allow enough time to review the validity of a new power cost proposal. However, the PCORC is not the only venue that presents this type of

⁸⁸ See *WUTC v. Puget Sound Energy, Inc.*, Docket No. UE-050870, Final Order (Oct. 2005); see also *WUTC v. Puget Sound Energy, Inc.*, Docket No. UE-070565, Final Order (Aug. 2007).

⁸⁹ See Smith, Exh. LS-1CT at 9:8-9.

⁹⁰ *WUTC v. Puget Sound Energy, Inc.*, Docket Nos. UE-011570 and UG-011571, Final Order at ¶ 27.

updated information. New forecasts such as load and current market prices are routinely discussed in other venues—such as the IRP process—prior to being used in the PCORC.

63. To the extent these parties find the PCORC too complex, it may be because they have elected not to participate in these processes,⁹¹ or they are trying to bring in new theories or methodologies during the PCORC process to change the way power costs are set in rates.⁹² The Commission should require that only the methodologies used in setting power costs in the most recent general rate case, updated for current prices and forecasts, should be used in determining the power costs for a subsequent PCORC.

64. Notwithstanding the above, in response to parties' concerns expressed through the PCORC collaborative and settlement negotiations and response testimony in this proceeding, PSE has agreed to revisions to the PCORC that will respond to concerns about the expedited time frame and allow for increased time to review PSE's proposed power cost adjustments while streamlining and further improving the efficiency of the PCORC process.

A. Expand the PCORC To a Six Month Time Period Rather than a Five Month Period

65. In order to serve its fundamental purposes, and also considering the single issue of production related costs, the PCORC process must be significantly shorter than a general rate case. PSE and other parties have settled or litigated three PCORC proceedings since the PCORC mechanism was initiated in 2002. It is clear that interested parties are now very familiar with the PCORC process, the Company's resource acquisition process and the methodologies underlying rate year power cost projections, such that the process is efficient and focused.

66. Nonetheless, in response to parties' concerns that more time is needed for these cases, PSE has agreed to extend the time period of the PCORC proceeding from five months to six months.

⁹¹ See Mills, TR. 549:3-550:6.

⁹² See Mills, Exh. No. DEM-12T at 5:11-14.

B. Formalize a Shortened Turn Around Time for Data Request Responses

67. In response to parties' concerns that there is not adequate time to fully evaluate the data provided by the Company in the PCORC's expedited timeframe, PSE has agreed to shorten the turn around time for data request responses from ten days to five days for PCORC proceedings.⁹³ This will provide parties more time to evaluate the data provided by the Company.⁹⁴

C. Provide the AURORA Model as Soon as a Confidentiality Agreement Has Been Signed

68. PSE witness David Mills testified at hearing that the sole trigger for PSE providing intervenors with copies of the AURORA model is the intervenors' filing of a confidentiality agreement. "First, the date that the Aurora files are provided to the counterparties is not a random exercise. It has everything to do with when we get the signed confidentiality agreements back from parties."⁹⁵ In PSE's 2007 PCORC proceeding, Docket No. UE-070565, intervenors signed a confidentiality agreement and received the AURORA model even before a prehearing conference had been held.⁹⁶ PSE agrees to follow this practice in all future PCORC proceedings, further increasing the efficiency of the PCORC proceeding.⁹⁷

D. Limit Updates to Gas Prices

69. Commission Staff has proposed that PSE limit updates to power costs to one update with an additional power cost update if the Commission determines the update is necessary due to increased gas costs and orders that such update be made as part of the compliance filing.⁹⁸ PSE has agreed to such proposal with the modification that the power cost update should be available if gas prices decrease as well as if they increase.⁹⁹

⁹³ See Harris, Exh. No. KJH-9CT at 18:5-8.

⁹⁴ It should be noted that the Commission routinely shortens the response time for data requests in PCORC proceedings. See e.g., *WUTC v. Puget Sound Energy, Inc.*, Docket No. UE-070565, Order 02 at ¶ 6.

⁹⁵ Mills, TR. 538:22-539:1.

⁹⁶ See Exh. No. B-8 (PSE's Response to Bench Request No. 7).

⁹⁷ See Mills, TR. 550:21-551:1.

⁹⁸ See Buckley, Exh. No. APB-1T at 5.

⁹⁹ See Harris, Exh. No. KJH-9CT at 20:7-23.

70. When the Company updates its power costs with new gas prices, this typically causes other elements of the power cost projection to change.¹⁰⁰ For example, when the power cost model is updated for gas prices, AURORA-modeled rate year resource costs and generation change.¹⁰¹ For consistency, power costs are also updated to include rate year short-term power and gas for power contracts at the date of the gas price forecast. Thus, the update for more recent gas prices should include all changes in power costs that are triggered by changes in gas prices. The methodology for updating power costs with new gas prices is discussed in Mr. Mills' prefiled direct and rebuttal testimonies.¹⁰² As clarified at hearing, these updates involve only a change to the input, not a change in methodology.¹⁰³ When such updates are made, the Company provides to other parties the model runs and detailed work papers that compare the updated to the earlier version. The Company will continue this practice.¹⁰⁴

E. Utilize Methodologies From Last General Rate Case

71. The complexity of the PCORC can be minimized if the parties use the same methodologies for updating power costs as were used in the preceding general rate case, updated for current prices and forecasts. As noted by Mr. Story, the PCORC was meant to be simplified in that it is based on approved power cost methodologies from the most recent general rate case plus the prudence of new resources. It does not deal with the cost of money or changes in non production related expenses or ratebase. Also new methodologies for determining power costs were intended to be limited to the general rate case filing. Unfortunately, parties have veered from the course and have proposed new methodologies during PCORC proceedings.

72. As discussed by Mr. Mills, some of the same parties who complain about the complexity of the PCORC are the ones who contribute to its alleged complexity:

¹⁰⁰ See *id.* at 21:9-10.

¹⁰¹ See *id.* at 21:10-12.

¹⁰² See Mills, Exh. No. DEM-1T at 29:2-32:7; see also Exh. No. DEM-12T at 16:13-19:16.

¹⁰³ See Mills, TR. 546:15-547:8.

¹⁰⁴ See Mills, TR. 547:9-23.

I think part of the challenge . . . that we're facing is not only from the Industrial Customers but potentially from other interveners, there's typically new proposals that are suggested in rebuttal testimony, things having to do with adjusting the forced outage rate or the availability of the Colstrip coal plant, how to model and impute a value for sales and resale as opposed to using the Aurora model, recommendations for how to provide gas supplies to . . . the Goldendale combustion turbine, how to provide gas supply from what inherently was an asset that belonged to the core gas book, how to swing that back, core gas transportation to provide raw heat gas to the Goldendale plant. Those types of proposals take everybody a significant amount of time to dial in and to try to understand one another in terms of the assumptions and the data points that are used.

Another problem that we typically have that kind of finds its way into the Aurora process is people focus—interveners come in with different suggestions or recommendations about changing either the availability or the total capacity factors of various units that . . . are dispatched in the Aurora model.

So all of that combined, that makes it a more challenging process.¹⁰⁵

73. To address this concern, Mr. Story had proposed in his rebuttal testimony a slight revision to the sixth bullet point of C.8 of the Settlement Stipulation¹⁰⁶:

- A calculation of proforma production cost schedules that are consistent with the Company's most recent general rate case, including power supply and other adjustments impacting then current production costs.

74. The intent of this revision is to emphasize that new methodologies for determining normalized power costs should not be brought into a PCORC. The parties should use the same methodologies used in the most recent general rate case, updated for new forecasts and resource prices.

75. By prohibiting the introduction of new methodologies in a PCORC proceeding, while still allowing updates for current prices and forecasts, the complexity of a PCORC is minimized.

¹⁰⁵ See Mills, TR. at 539:4:-540:4.

¹⁰⁶ See Story, Exh. No. JHS-14T at 34:13-35:4.

VIII. CONCLUSION

76. PSE has demonstrated an ongoing need for the PCORC. The PCORC was created through the PCA Settlement Stipulation in 2002 to address needs that continue to exist today. The PCORC aligns the interests of PSE and its customers in transforming the Company from a short-term, market power utility to a utility that owns and manages its resources.

77. PSE has done what it was asked to do in 2002 when the PCORC was created. PSE has worked diligently to acquire cost effective resources to meet its load. It has been successful in using the PCORC to acquire these low cost resources when opportunities have arisen. It has actively engaged in the least cost plan/integrated resource plan process. Even so, the conditions that led to the creation of the PCORC continue today, including PSE's need to still acquire significant new resources to meet its growing load and to replace expiring contracts.

78. The arguments raised by Public Counsel and ICNU misconstrue the intent of the PCA and PCORC and demonstrate that they do not grasp the policy reasons for the creation of the PCORC. Their suggested solutions to replace the PCORC are short sighted and do not provide any reason to eliminate the PCORC, which has been functioning as planned.

79. For the reasons set forth herein and based on the evidence submitted in this case, PSE respectfully requests that the Commission approve the ongoing existence of the PCORC, with the modifications agreed to by the Company.

DATED this 26th day of September, 2008.

Respectfully submitted

PERKINS COIE LLP

By _____
Sheree Strom Carson, WSBA # 25349
Jason Kuzma, WSBA #31830

Attorneys for Puget Sound Energy, Inc.