EXHIBIT NO. ___(JHS-1T)
DOCKET NO. ____________
2006 PCA 4 COMPLIANCE
WITNESS: JOHN H. STORY

BEFORE THE
WASHINGTON UTILITIES AND TRANSPORTATION COMMISSION

In the Matter of the Petition of **PUGET SOUND ENERGY, INC.** **For Approval of its 2006 Power Cost Adjustment Mechanism Report**	**Docket No. UE-_______**

PREFILED DIRECT TESTIMONY OF
JOHN H. STORY (NONCONFIDENTIAL)
ON BEHALF OF PUGET SOUND ENERGY, INC.

AUGUST 31, 2006

PUGET SOUND ENERGY, INC.

PREFILED DIRECT TESTIMONY OF JOHN H. STORY

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PUGET SOUND ENERGY, INC.

PREFILED DIRECT TESTIMONY OF JOHN H. STORY

I. INTRODUCTION

Q. Please state your name, business address and present position.

A. My name is John H. Story. My business address is 10885 N.E. Fourth Street, P.O. Box 97034, Bellevue, Washington 98009-9734. I am the Director of Cost and Regulation for Puget Sound Energy, Inc. ("PSE" or "the Company").

Q. What is your educational and professional experience?

A. Exhibit No. ___(JHS-2) describes my educational and professional experience.

Q. What are your duties as Director of Cost and Regulation for Puget Energy?

A. As Director of Cost and Regulation, I am responsible for the Revenue Requirement department at PSE.

Q. What is the purpose of this filing?

A. In accordance with the Commission's Twelfth Supplemental Order in Docket No. UE-011570, the Company must file an annual report detailing the power costs included in its deferral calculation under the Power Cost Adjustment Mechanism. Through its Petition, the Company is requesting approval of PSE's

Power Cost Adjustment Mechanism Annual Report for the Twelve Months Ended June 30, 2006 ("2006 PCA Report").

II. BACKGROUND REGARDING THE PCA MECHANISM

Q. Please provide a brief summary of the Power Cost Adjustment Mechanism.

A. As authorized by the Commission, the Company's PCA Mechanism accounts for differences in PSE's modified actual power costs relative to a power cost baseline. This mechanism accounts for a sharing of costs and benefits that are graduated over four levels of power cost variances, with an overall cap of $40 million (+/-) for the four year period July 1, 2002 through June 30, 2006. If the cap is exceeded, costs and benefits in excess of $40 million would be allocated 99% to the customers and 1% to the Company. *See*, the Stipulation associated with the Commission's Twelfth Supplemental Order in Docket No. UE-011570, attached as Exhibit A to the Accounting Petition, which defines the specific sharing levels and conditions.

Q. Please describe the categories of power costs that are included in the PCA mechanism.

A. The following fixed and variable power costs are included. These costs are adjusted as described below.

Fixed Costs:

For PCA calculation purposes, fixed costs are power production related costs and rate of return. Power production related costs from the most recent general rate case or power cost only rate case are included and do not change during the PCA period except for special treatment of Hopkins Ridge as noted below. These costs include depreciation, property taxes for production plant, and specifically identified transmission plant. Other fixed costs include FERC Accounts 557 Other production expense, Hydro and Other Production O&M, and 500 KV O&M. Regarding the rate of return, the rate from the most recent general rate case is applied in the PCA period. Pursuant to the Settlement Agreement in the 2005 PCORC, WUTC Docket No. UE-050870, return on ratebase and depreciation expense for Hopkins Ridge has been included at actual amounts from it's in-service date of November 27, 2005 through March 31, 2006, rather than at the forecasted amount established in Exhibit A-1. The difference between the actual and forecasted amounts is considered to be included in Purchased Power, a variable cost component in the PCA mechamism, thus resulting in no net impact on the overall power cost baseline rate used in the PCA mechamism calculations.

Variable Costs:

Actual monthly amounts recorded in FERC Accounts 501 – Steam generation fuel, 547 – Other power generation fuel, 555 – Purchased power, 447 – Sales for resale, 565 – Transmission of electricity by others. In addition, variable costs and credits for sales of non-core gas, Transmission Revenue for Colstrip 1-4 lines, Third AC and Northern Intertie are included. Allowed regulatory return on amounts associated with Tenaska, Cabot, Bonneville Exchange Power Agreement ("BEP"), White River Relicensing and CWIP, White River Plant Costs, CanWest and the Hopkins Ridge Prepaid Transmission regulatory assets and liabilities are also included in variable costs.

Adjustments per the 2001 General Rate Case Settlement:

The following are adjustments as determined in Docket UE 011570:

1) Prudence disallowance from UE-921262, disallowing a portion of the power costs associated with March Point 2 (3%) and Tenaska (1.2%);

2) Contract price adjustments to limit the rate or total cost to the most recently approved contract rate;

3) Colstrip Availability adjustment if the actual availability factor for the four plants at Colstrip falls below a 70% equivalent availability factor; and

4) New long-term resource pricing adjustment to bring the variable cost of the new resource to the lower of actual unit cost or the average embedded cost.

No adjustment was required during the July 1, 2005 through June 30, 2006 period ("PCA Period 4") for either item 3 or 4 above. Adjustments under items 1 and 2 are shown in the Company's work papers relating to this filing.

Q. Are there other adjustments to be considered along with those determined in UE-011570?

A. Yes, per the Commission orders issued in Docket UE-031725, PSE is subject to the disallowance of costs associated with the Tenaska Benchmark Disallowance.

III. PCA PERIOD 4 ACCOUNTING

Q. Please explain how the Company has tracked its PCA Period 4 power costs.

A. The Company has detailed accounting instructions, which are provided in the supporting workpapers to this filing, that track PCA Mechanism activity. Each month the Company calculates the power costs subject to PCA sharing using the same methodology shown in Exhibit B from the original PCA Mechanism filing. Allowed power costs include the fixed and adjusted variable costs, net of the adjustments discussed above. Total allowable costs are then compared to the baseline power cost rate from Exhibit A-1 times the actual delivered load and any difference is allocated to the Company or customers based on the different levels of sharing defined in the PCA Mechanism. Any difference allocated to the customers is recorded in FERC Account 182.3, Other regulatory assets or Account 254, Other regulatory credits depending on whether the accumulated balance is a debit or credit.

Under the PCA Mechanism, the deferred amount at the time of the next PCA annual true-up filing, along with the projected variable and fixed costs through the next proposed rate year, could be considered in the determination of any rate change for the subsequent PCA period. Amounts deferred, when authorized, will be amortized to FERC Account 407.3, Regulatory debits or 407.4, Regulatory credits as they are recovered or refunded by the Company to customers.

The Company accrues interest monthly on any deferred balance (debit or credit) at the interest rate calculated in accordance with WAC 480-90-233(4).

Q. Did the Baseline power cost rate change within PCA Period 4?

A. Yes. From July 1, 2005 through October 31, 2005, the baseline rate was $49.132 as established in Docket No. UG-040640, *et al.*, the Company's 2004 general rate case. Attached in Exhibit No.___(JHS-3C), 2006 PCA Report, pages 5 through 16, is the calculation of this Baseline rate and supporting schedules for this period.

For the remainder of PCA Period 4, November 1, 2005 through June 30, 2006, the Baseline rate was $52.503 as established in Docket No. UE-050870, the Company's 2005 power cost only rate case. Attached in Exhibit No.____(JHS-3C), 2006 PCA Report, pages 17 through 26, is the calculation of this Baseline rate and supporting schedules for this period.

Q. What is the effective baseline rate at the end of PCA Period 4 when changes in the variable power cost components are considered?

A. As shown on Exhibit No.___(JHS-3C), 2006 PCA Report, page 4, Exhibit A-1 Power Cost Rate Updated, when changes in variable components of the PCA Mechanism plus the change in Baseline rate that occurred in November 2005 are considered, the baseline rate for the twelve month period ended June 30, 2006 is $51.004. The baseline rate exceeded actual power costs by $10,522,768 (after adjustment for Firm Wholesale). Major contributors to the increase are discussed by Mr. David Mills in his prefiled direct testimony.

Q. What is the resulting deferral balance for PCA Period 4?

A. As of June 30, 2005 the Company had deferred $5,101,727 of under-recovered power costs. There were no additional deferrals required at the end of PCA Period 4. Therefore, the deferred balance remains at $5,101,727. Interest of $407,644 had been accrued at the end of PCA period 3. $736,238 of interest relates to PCA Period 4 as allowed for under the PCA Mechanism. Adding the total accrued interest of $1,143,882 to the deferred balance of $5,101,727, results in a total customer deferral balance under the PCA mechanism at June 30, 2006 of $6,245,609. *See* attached Exhibit No.___(JHS-3C), 2006 PCA Report, page 3.

Q. Will there be a rate increase as a result of this filing?

A. No. The deferral balance is not at a level where an increase is warranted.

IV. ADJUSTMENT OF COSTS OUTSIDE OF THE PCA PERIOD

Q. Please describe the need for "Adjustments of Costs Outside of the PCA Period".

A. In the Company's PCA Period 1 compliance filing, Docket No. UE-031389, a procedure entitled "Methodology for Adjustments of Costs Outside of the PCA Period" was agreed to by the parties and approved by the Commission for the treatment of such adjustments in that and future PCA periods. *See* Exhibit No.___(JHS-4).

Q. Were there any such adjustments in PCA Period 4?

A. There were no material accounting adjustments made during the PCA period.

Q. Does this conclude your testimony?

A. Yes, it does.