

BEFORE THE WASHINGTON UTILITIES & TRANSPORTATION COMMISSION

Amended Petition of

PUGET SOUND ENERGY, INC.

For An Order Authorizing The Use Of The Proceeds From The Sale Of Renewable Energy

Credits And Carbon Financial Instruments

DOCKET NO. UE-070725

DIRECT TESTIMONY OF SCOTT NORWOOD (SN-1T)

ON BEHALF OF

PUBLIC COUNSEL

JANUARY 28, 2010

**REDACTED VERSION**

DIRECT TESTIMONY OF SCOTT NORWOOD (SN-1T)  
DOCKET NO. UE-070725

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**WITNESS'S EXHIBIT LIST**

Exhibit No. SN-2	Background and Experience of Scott Norwood
Exhibit No. SN-3	PSE's Response to Public Counsel Data Request No. 28
Exhibit No. SN-4HC	PSE's Highly Confidential Response to Public Counsel Data Request Nos. 30 and Confidential Response to Public Counsel Data Request No 31
Exhibit No. SN-5HC	PSE's Highly Confidential Response to Public Counsel Data Request No. 37, Rev 01
Exhibit No. SN-6C	PSE's Responses to Public Counsel Data Requests Nos. 350 and 351 and Mills' Confidential Exhibit No. DEM-11C from Docket Nos. UE-090704/UG-090705
Exhibit No. SN-7	Estimated Annual Return on Equity for PSE Wind Generation Assets
Exhibit No. SN-8	Estimated Rate Year Wind Energy Costs Paid by PSE Retail Customers
Exhibit No. SN-9	PSE's Response to Public Counsel Data Request No. 8
Exhibit No. SN-10C	PSE's Confidential Response to Public Counsel Data Request No. 10.
Exhibit No. SN-11	PSE's Response to Public Counsel Data Request No. 49
Exhibit No. SN-12	PSE's Response to Public Counsel Data Request No. 22
Exhibit No. SN-13	PSE's Response to Public Counsel Data Request No. 42
Exhibit No. SN-14HC	PSE's Highly Confidential Response to Public Counsel Data Request No. 9 and Response to Public Counsel Data Request No. 12

**I. INTRODUCTION / SUMMARY**

**Q: Please state your name and business address.**

A: My name is Scott Norwood. I am President of Norwood Energy Consulting, L.L.C. My business address is P.O. Box 30197, Austin, Texas 78755-3197.

**Q: By whom are you employed and in what capacity?**

A: I am a self-employed energy consultant specializing in the areas of electric utility regulation, resource planning and energy procurement.

**Q: On whose behalf are you testifying?**

A: I am testifying on behalf of the Public Counsel Section of the Washington Attorney General's Office (Public Counsel).

**Q: Please describe your professional qualifications.**

A: I have over 28 years of experience in the electric utility industry. After graduating from the University of Texas in 1980 with a Bachelor of Science degree in electrical engineering, I began my career as a power plant engineer for the City of Austin's Electric Utility Department where I was responsible for electrical maintenance and design projects for the City's three gas-fired power plants. In January 1984, I joined the staff of the Public Utility Commission of Texas as Manager of Power Plant Engineering. In that capacity I was responsible for addressing resource planning, fuel and purchased power cost issues presented in regulatory filings before the Texas Commission. In 1986, I joined GDS Associates, Inc., a Marietta, Georgia-based consulting firm that specializes in electric utility regulatory consulting and resource planning. I was elected a Principal of GDS in 1990 and directed the firm's Deregulation Services

1 Department until January 2004, when I left GDS to form Norwood Energy  
2 Consulting, LLC. The focus of my current consulting practice is energy planning,  
3 procurement and regulation. Exhibit No. SN-2 provides a more detailed summary  
4 of my background and experience.

5 **Q: Have you previously testified before the Washington Utilities and**  
6 **Transportation Commission or other state utility commissions?**

7 A: Yes. I recently presented testimony on behalf of Public Counsel in Puget Sound  
8 Energy, Inc.'s (PSE) pending general rate case (Docket Nos. UE-090704/UG-  
9 090705). I have also testified on behalf of consumers, government agencies, and  
10 consumer-owned utilities in numerous past regulatory proceedings before state  
11 regulatory commissions in Arkansas, Georgia, Illinois, Iowa, Louisiana,  
12 Michigan, Missouri, New Jersey, Oklahoma, Texas, Virginia, and Wisconsin.

13 **Q: What is the purpose of your testimony?**

14 A: The purpose of my testimony is to present my analysis and recommendations  
15 regarding PSE's proposed allocation and ratemaking treatment of the net proceeds  
16 from Renewable Energy Credit (REC) and Carbon Financial Instrument (CFI)  
17 sales.

18 **Q: What exhibits are you sponsoring in this proceeding?**

19 A: I am sponsoring 14 exhibits, including my testimony. A number of these exhibits  
20 are discovery responses regarding PSE's California REC sales that were provided  
21 in Docket Nos. UE-090704/UG-090705, the Company's pending general rate  
22 case.<sup>1</sup>

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<sup>1</sup> See Exhibit No. SN-3, PSE's Response to Public Counsel Data Request No. 28.

**II. SUMMARY OF TESTIMONY**

**Q: Please summarize your testimony and recommendations.**

A: Through November of 2009, PSE earned approximately [BEGIN HIGHLY CONFIDENTIAL] XXXXXXXX [END HIGHLY CONFIDENTIAL] from the sale of Renewable Energy Credits (RECs) and Carbon Financial Instruments (CFIs).<sup>2</sup> The Company forecasts that it will earn an additional [BEGIN HIGHLY CONFIDENTIAL] XXXXXXXX [END HIGHLY CONFIDENTIAL] over the next six (6) years from the sale of RECs under existing contracts with California utilities and other parties.<sup>3</sup> PSE requests that it be allowed to retain approximately \$21.1 million of the net proceeds from REC sales to offset unpaid amounts it claims to be owed by California utilities (California Receivable) for power sold by PSE during 2000 and 2001. However, PSE has not demonstrated why it is entitled to retain \$21.1 million of REC proceeds or that its California Receivable claim is even valid or recoverable. Moreover, PSE's retail customers pay all costs of the generating facilities from which RECs and CFIs are derived and therefore are entitled to receive 100 percent of related REC and CFI sales proceeds as a matter of basic equity, just as such customers currently receive all revenues earned from off-system energy sales supplied from PSE's generating assets.

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<sup>2</sup> See Exhibit No. SN-4HC, PSE's Highly Confidential Responses to Public Counsel Data Requests Nos. 30 and 31.

<sup>3</sup> See Exhibit No. SN-5HC, PSE's Highly Confidential Response to Public Counsel Data Request No. 37, Rev. 01.

1 I have several recommendations regarding the calculation of net proceeds  
2 from PSE's REC and CFI sales, the allocation of proceeds from such sales, and  
3 the ratemaking treatment of such proceeds. First, I recommend that 100 percent  
4 of net proceeds from REC and CFI sales, along with any energy sales margins  
5 associated with the off-system energy sales component of these transactions, be  
6 credited to PSE's ratepayers and reflected in a manner that provides immediate  
7 customer benefits to the extent possible. In this regard, I recommend that the  
8 **[BEGIN HIGHLY CONFIDENTIAL] XXXXXXXX [END HIGHLY**  
9 **CONFIDENTIAL]** of accumulated REC and CFI revenues and energy sales  
10 margins, plus associated interest, that existed as of the end of November 2009, be  
11 immediately applied to reduce the rate base of PSE's Hopkins Ridge and Wild  
12 Horse wind generation facilities and that this adjustment be reflected in PSE's  
13 approved rates resulting from the Company's pending general rate case (Docket  
14 Nos. UE-090704/UG-090705).

15 While I do not support or oppose the proposal by PSE and the Joint Parties  
16 that 20 percent of REC and CFI sales proceeds, up to a cumulative total amount of  
17 \$20 million, be allocated to help fund low-income renewable energy and energy  
18 efficiency programs, I do recommend that, should the Commission approve this  
19 proposal, such amounts be derived from net REC proceeds collected after  
20 November 2009. I further recommend that all other REC and CFI sale proceeds  
21 and any related energy sales margins collected later than November 2009, after  
22 any designated monthly allocation to low-income programs is made, be

1 immediately credited to all PSE retail customers through a non-general rate tariff,  
2 similar to the Company's Production Tax Credit (PTC) Tracker mechanism.

3 Finally, I recommend that PSE's calculations of REC and CFI proceeds  
4 and related energy margins be subject to review and final reconciliation in the  
5 Company's next general rate case, and that the Commission establish terms for  
6 reporting and monitoring of PSE's management and accounting for REC sales  
7 proceeds on an ongoing basis, consistent with the method approved by the  
8 Commission in PacifiCorp's most recent general rate case, Docket No. UE-  
9 090205.

10 The bases for these recommendations are explained in the remaining  
11 sections of my testimony.

### 12 13 **III. OVERVIEW OF PSE'S PROPOSALS**

14 **Q: What is PSE proposing in this case?**

15 A: PSE is requesting approval to defer the net proceeds from its past and future sales  
16 of RECs and CFIs.<sup>4</sup> The Company is requesting that it be allowed to use up to  
17 \$20 million of the REC and CFI proceeds to fund low-income energy efficiency  
18 measures and energy-related repairs and renewable energy systems for low-  
19 income residential locations.<sup>5</sup> PSE further requests that it be allowed to retain  
20 \$21,062,800 of REC sale proceeds to offset its California Receivable for power  
21 sold by PSE during 2000 and 2001.<sup>6</sup> Finally, PSE proposes to use the remainder

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<sup>4</sup> Amended Petition, page 1.

<sup>5</sup> *Id.*, page 7.

<sup>6</sup> *Id.*, page 8.



1 of the REC proceeds to offset regulatory assets that are currently recovered  
2 through its base rates.<sup>7</sup>

3 **Q: What are Renewable Energy Credits?**

4 A: Washington's Energy Independence Act defines Renewable Energy Credits under  
5 Section RCW 19.285.030 as:

6 . . .a tradable certificate of proof of at least one megawatt-  
7 hour of an eligible renewable resource where the generation  
8 facility is not powered by fresh water, the certificate  
9 includes all of the non-power attributes associated with that  
10 one megawatt-hour of electricity, and the certificate is  
11 verified by a renewable energy credit tracking system  
12 selected by the department.

13  
14 In essence, RECs represent the right to claim environmental attributes or benefits  
15 associated with energy produced by a renewable generation facility.<sup>8</sup> RECs are  
16 characterized by the energy generated from renewable resources; one REC equals  
17 one megawatt-hour (MWh) produced from an eligible renewable resource.<sup>9</sup>  
18 Importantly, RECs can be used to demonstrate compliance with Renewable  
19 Portfolio Standards (RPS).<sup>10</sup>

20 **Q: What are Carbon Financial Instruments (CFI)?**

21 A: A CFI is a commodity sold on the Chicago Climate Exchange which is equivalent  
22 to a 100 metric ton reduction of CO<sub>2</sub> emissions.<sup>11</sup>

23 **Q: What are the total net proceeds from PSE's sales of RECs and CFIs to date?**

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<sup>7</sup> *Id.*

<sup>8</sup> *Id.*, page 2.

<sup>9</sup> *Id.*

<sup>10</sup> *Id.*, page 3.

<sup>11</sup> *Id.*, page 4.

1 A: From August of 2007 through November of 2009, PSE sold [BEGIN HIGHLY  
2 CONFIDENTIAL] XXXXXX [END HIGHLY CONFIDENTIAL] RECs and  
3 earned total net proceeds of [BEGIN HIGHLY CONFIDENTIAL] XXXX  
4 XXXXX [END HIGHLY CONFIDENTIAL] from such sales.<sup>12</sup> Through  
5 November of 2009, PSE recorded total net proceeds of [BEGIN  
6 CONFIDENTIAL] XXXXXX [END CONFIDENTIAL] from sales of CFIs.<sup>13</sup>

7 **Q: What is PSE's forecast of REC sales revenues over the next several years?**

8 A: PSE's forecast of REC sales proceeds over the next several years is summarized  
9 below in Table 1. This forecast reflects the REC sales volumes and prices  
10 specified under PSE's sales contracts with Southern California Edison (SCE),  
11 Pacific Gas and Electric Company (PG&E), and other parties, which were  
12 executed during 2008 and 2009.<sup>14</sup>

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<sup>12</sup> See Exhibit No. SN-4HC, PSE's Highly Confidential Response to Public Counsel Data Request No. 30.

<sup>13</sup> See Exhibit No. SN-4HC, PSE's Confidential Response to Public Counsel Data Request No. 31.

<sup>14</sup> Legislation currently being considered in Washington state may expand the generation facilities from which RECs may be derived, and thus may increase the number of excess RECs PSE may claim and sell. See e.g. H.B. 3034 and S.B. 6672, 61st Leg., §1 (Wash. 2010).

[BEGIN HIGHLY CONFIDENTIAL]

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[END HIGHLY CONFIDENTIAL]

#### IV. ENTITLEMENT TO REC AND CFI PROCEEDS

**Q: How are PSE's RECs and CFIs created?**

A: The majority of PSE's RECs are created as a result of the generation of renewable energy from the Company's Wildhorse and Hopkins Ridge wind farms, and Klondike III Wind Power Purchase Agreement (PPA). The CFIs referenced in this case were created as a result of PSE reducing the level of carbon emissions on its system from a baseline level established during the 1998 to 2001 period. The reduction in carbon emissions has been accomplished primarily by the Company's acquisition of renewable resources and by the acquisition of gas-fired, combined cycle generating resources that have low carbon emissions.

1       **Q:     Who pays for the capital and operating costs of the renewable resources and**  
2               **other generating resources from which RECs and CFIs sold by PSE are**  
3               **derived?**

4       A:     PSE's retail customers in Washington pay all of the costs for the Hopkins Ridge  
5               and Wild Horse wind generation facilities, and the Klondike III Wind PPA (from  
6               which the majority of PSE's RECs are derived) through charges embedded in  
7               PSE's base rates. PSE's retail customers also pay for other generating resource  
8               additions to PSE's system that have resulted in the creation of the CFIs (and  
9               related revenues) that are at issue in this case.

10      **Q:     How much do PSE's ratepayers pay annually for energy generated from the**  
11               **Hopkins Ridge, Wild Horse, and Klondike III PPA wind resources?**

12      A:     The total annual revenue requirement for the Hopkins Ridge, Wild Horse, and  
13               Klondike III PPA paid by ratepayers is approximately [BEGIN  
14               CONFIDENTIAL] XXX [END CONFIDENTIAL] million per year.<sup>15</sup>

15      **Q:     What cost is incurred by PSE's shareholders for the Hopkins Ridge, Wild**  
16               **Horse, and Klondike III PPA wind resources?**

17      A:     PSE's shareholders do not incur any costs for the Hopkins Ridge, Wild Horse, or  
18               Klondike III PPA wind resources; in fact, the Company's shareholders earn  
19               approximately \$27.3 million per year in equity return for the Hopkins Ridge and  
20               Wild Horse wind projects.<sup>16</sup>

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<sup>15</sup> See Exhibit No. SN-6C, PSE's Responses to Public Counsel Data Requests Nos. 350 and 351 and Mills' Exhibit DEM-11C from Docket No. UE-090704/UG-090705.

<sup>16</sup> See Exhibit No. SN-7.

1       **Q:     What portion of the net proceeds from REC and CFI sales should be**  
2       **returned to PSE's ratepayers?**

3       A:     PSE's ratepayers should receive 100 percent of the net proceeds derived from  
4       sales of RECs and CFIs because ratepayers pay all costs of the generating  
5       resources from which such RECs and CFIs are derived, including an equity return  
6       paid to PSE's shareholders for the investment in such projects. Moreover, it is  
7       important to recognize that, even after receiving 100 percent of the credit for REC  
8       and CFI sales proceeds, PSE's ratepayers will likely still be paying significantly  
9       more for wind energy than they would otherwise pay if PSE had purchased such  
10      energy from the market. For example, PSE's projected cost of energy from the  
11      Hopkins Ridge, Wild Horse, and Klondike III Wind PPA in its pending base rate  
12      case is approximately \$98/MWh, which is approximately 115 percent higher than  
13      PSE's forecasted average market price of energy during this same period.<sup>17</sup> Even  
14      after 100 percent of the net proceeds from RECs and CFIs sales are credited to  
15      customers as I have recommended, the net cost of energy paid by ratepayers for  
16      energy delivered from these wind energy projects during the rate year ending  
17      March 30, 2011 would be approximately \$88/MWh, which is approximately 95  
18      percent higher than PSE's forecasted average price of market energy purchases  
19      during the rate year.<sup>18</sup>

20      **Q:     Does PSE credit other benefits of wind generation to its retail customers?**

21      A:     Yes. PSE presently credits 100 percent of the wind production tax credits to  
22

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<sup>17</sup> See Exhibit No. SN-8.

<sup>18</sup> *Id.*

1 ratepayers through its Production Tax Credit (PTC) Tracker mechanism.

2 **Q: Does PSE credit 100 percent of the net proceeds from the off-system sales of**  
3 **energy supplied from other generating assets to its native retail customers?**

4 A: Yes. The net proceeds from PSE's REC sales are analogous to off-system energy  
5 sales margins which are also credited entirely to customers by reducing the level  
6 of system fuel expense included in PSE's power cost rate.

7 **Q: Why does PSE believe it is entitled to retain \$21.1 million of REC sales**  
8 **proceeds when the Company does not contribute any amount to the cost of**  
9 **wind generation from which such RECs sales are supplied?**

10 A: PSE has indicated that it is appropriate for it to retain approximately \$21.1 million  
11 of REC sales proceeds to satisfy the California Receivable that the Company  
12 claims it is owed by California utilities, because "the tremendous increase in  
13 benefits that customers will receive would not have been available absent the  
14 settlement" with such utilities.<sup>19</sup> As discussed in the next section of my  
15 testimony, PSE has not demonstrated the basis for its \$21.1 million claim nor has  
16 it proven that its native retail customers will receive a tremendous increase in  
17 benefits as a result of its settlements with California utilities.

18 **Q. Please summarize your conclusions regarding the appropriate allocation of**  
19 **REC and CFI sale proceeds.**

20 A. PSE's retail customers pay all costs of the generating facilities from which RECs  
21 and CFIs are derived, and therefore are entitled to receive 100 percent of related  
22 REC and CFI sales proceeds as a matter of basic equity, just as such customers  
23

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<sup>19</sup> See Exhibit No. SN-9, PSE's Response to PC Data Request No. 008.

1 currently receive 100 percent of wind production tax credits and 100 percent of  
2 revenues earned from off-system energy sales supplied from PSE's generating  
3 assets. PSE has not demonstrated why it is entitled to retain approximately \$21.1  
4 million of REC sales proceeds or whether its California Receivables claim is even  
5 valid or recoverable.

6  
7 **V. PSE'S REQUEST TO RETAIN REC SALE PROCEEDS**

8  
9 **Q: What information has PSE provided to support its request to retain \$21.1**  
10 **million of REC proceeds for its California litigation claim?**

11 A: PSE has presented certain information prepared by the California Independent  
12 Systems Operator (ISO) that details the price and payments received for power it  
13 sold into the California market, and which shows that the net balance owed to the  
14 Company was approximately \$21.1 million.<sup>20</sup> The Company has stated that this  
15 amount represents "the discounted amount that PSE had a reasonable expectation  
16 that it would be able to collect from California, before interest, if the litigation ran  
17 its course."<sup>21</sup> However, after more than eight years of litigation and failed  
18 attempts at mediation and settlement, the Company admits that central issues of  
19 the litigation remained far from resolution.<sup>22</sup> Therefore, there was significant

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<sup>20</sup> See Exhibit No. SN-10C, PSE's Response to PC Data Request No. 10.

<sup>21</sup> *Id.*

<sup>22</sup> See Exhibit SN-9, PSE's Response to PC Data Request No. 08.

1           uncertainty as to whether PSE would ever have recovered the \$21.1 million it now  
2           claims that it is entitled to collect for its California Receivable.<sup>23</sup>

3       **Q:   Does the \$21.1 million claimed by PSE represent costs actually incurred by**  
4       **the Company to supply the energy sales at issue, the price of such sales, or**  
5       **some other amount?**

6       A:   PSE indicates that the \$21.1 million it seeks to retain is neither the incurred cost  
7           nor the price of the energy sales under dispute.<sup>24</sup> In fact, the Company states that  
8           it does not have information on either the cost or the volume of the energy sales  
9           related to this claim.<sup>25</sup>

10      **Q:   Has PSE presented any evidence to demonstrate that the Company's**  
11      **proposal to retain \$21.1 million of the net proceeds from REC sales is**  
12      **justified by the price it received for RECs sold to SCE and PG&E?**

13      A:   No. The Company has stated that its customers will receive a tremendous  
14           increase in benefits due to the prices for RECs that were negotiated and obtained  
15           as a result of the settlement.<sup>26</sup> PSE has not provided any testimony or other  
16           evidence that demonstrates the value or probability of recovery of its California  
17           Receivable claim or to otherwise support its position that the prices it obtained for

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<sup>23</sup> It is my understanding as a non-attorney that, as a general matter, costs must be known and measurable to be recoverable under normal regulated ratemaking practices. The party seeking to recover a cost must offer factual or other showings to this effect. A cost is “known” when the effect of the related event will be in place when rates will likely be in effect.<sup>23</sup> A cost is generally “measurable” when documented by an “actual expenditure, invoice, contract, or other specific obligation,” while costs from estimates and projections are generally not measurable. *See WUTC v. Avista Corporation d/b/a/ Avista Utilities*, WUTC Docket No. UE-090134/UG-090135 (*consolidated*), Final Order (Order 10), ¶45. In this case, PSE has not offered any showing of known or measurable costs.

<sup>24</sup> *See* Exhibit No. SN-10C, PSE's Response to PC Data Request No. 10.

<sup>25</sup> *Id.*

<sup>26</sup> *See* Exhibit No. SN-9, PSE's Response to PC Data Request No. 08.



1 RECs sold to SCE and PG&E could not have been obtained without the  
2 settlement.<sup>27</sup>

3 **Q: Was PSE able to negotiate similar REC sales prices under agreements which**  
4 **were not conditioned upon approval of the California litigation settlement?**

5 A: Yes. The price of RECs obtained by PSE under a subsequent sale agreement with  
6 SCE that was executed in May 2009 and was not conditioned upon approval of  
7 the California litigation settlement agreement, was only approximately 13 percent  
8 lower than the REC sales prices negotiated under the "settlement agreements"  
9 with SCE and PG&E.<sup>28</sup> Moreover, PSE's REC sales agreement with PG&E,  
10 which had slightly *higher* pricing than the REC sale agreement with SCE, also  
11 was not conditioned upon approval of the California litigation settlement  
12 agreement. The fact that PSE was able to obtain similar pricing for REC sales  
13 that were negotiated in the same general timeframe but without linkage to the  
14 California litigation settlement appears to refute PSE's claim that customers could  
15 not have achieved a similar level of benefits without the litigation settlement.

16 **Q: Is PSE seeking to retain a portion of the net revenues from REC sales limited**  
17 **only to proceeds from sales that are related to its California litigation**  
18 **settlement?**

19 A: No. It appears that PSE is requesting that it be allowed to retain 40 percent of all  
20 REC proceeds up to \$21,062,800, including proceeds from REC sales unrelated to  
21 its California litigation settlement.<sup>29</sup> I see no apparent basis for the Company's

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<sup>27</sup> See Exhibit No. SN-14HC, PSE's Responses to PC Data Request Nos. 09 and 12.

<sup>28</sup> See Exhibit No. SN-10C, PSE's Response to PC Data Request No. 10.

<sup>29</sup> Amended Petition, page 8, and Direct Testimony of Tom De Boer, pages 3-4.

1 claim to retain 40 percent of REC proceeds, particularly those REC proceeds  
2 which are unrelated to its California litigation settlement.

3 **Q: Absent the REC sales and this Petition, would PSE be entitled to recover**  
4 **costs associated with the California litigation through its Washington retail**  
5 **rates?**

6 A: No. All costs associated with the California Receivable and subsequent litigation  
7 relate to non-regulated wholesale power sales. Only in the event that PSE  
8 received revenue from such sales that it shared with its Washington retail  
9 customers would these litigation costs even be something that the Commission  
10 should consider for recovery through retail rates. This is not the case here.

11 **Q: Would PSE's retail customers have benefitted from the past California**  
12 **energy sales which resulted in the California Receivable claim that the**  
13 **Company seeks to recover in this case?**

14 A: No. The California energy sales which are the basis for PSE's claim were  
15 speculative, market-based, off-system power sales that the Company pursued in  
16 an effort to produce additional profits for its shareholders. PSE was under no  
17 obligation to pursue such sales and should have recognized the inherent risk of  
18 selling energy into the (then) new California wholesale power market. The  
19 extremely high prices for energy sold in the California market during this period  
20 were in-part reflective of the high risk of sales into this market. In any event, the  
21 proceeds from PSE's energy sales to California during 2000 and 2001 would not

1 have been shared with PSE's retail customers because the Company was under a  
2 five-year rate freeze during this period.<sup>30</sup>

3 **Q: Did PSE include the off-system sales revenues associated with its California**  
4 **REC sales contracts in its updated electric baseline power forecast in its**  
5 **pending general rate case (Docket No. UE-090704)?**

6 A. No. PSE did not reflect the off-system energy sales associated with the REC sales  
7 agreements in the proposed baseline power cost forecast in the Company's  
8 pending general rate case. It is likely that there will be opportunities for PSE to  
9 realize significant profits on sales of energy under these agreements which are  
10 priced based on Mid-C on-peak indices, since PSE currently has surplus energy  
11 on its system and has energy resources whose variable costs are forecasted to be  
12 below Mid-C market prices in certain on-peak periods.<sup>31</sup> Under PSE's proposals,  
13 these energy sales profits would flow to the Company and its shareholders and  
14 therefore would provide another source of compensation for PSE's California  
15 Receivables claim. For example, if PSE was able to deliver energy to SCE and  
16 PG&E for a cost of only \$2/MWh below the Mid-C on-peak index energy price  
17 reflected in such contracts, the Company would earn approximately \$30 million  
18 of profits under these transactions, which is \$11.1 million more than its California  
19 Receivables claim. These off-system energy sales profits also should be returned  
20 entirely to customers who pay all non-fuel costs of the generating resources from

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<sup>30</sup> See Exhibit No. SN-11, PSE's Response to PC Data Request No. 49.

<sup>31</sup> See Mills' Exhibit No. DEM-11C from Docket Nos. UE-090704/UG-090705, which is contained in Exhibit No. SN-6C.

1 which such energy would be supplied. Returning these profits is also consistent  
2 with normal treatment of all such off-system sales.

3 **Q: Are you aware of any other reasons why PSE should be allowed to retain**  
4 **\$21.1 million of REC sales proceeds to offset its California Receivables**  
5 **claim?**

6 A: No. As a matter of basic equity, PSE's ratepayers are entitled to all REC proceeds  
7 since ratepayers pay all costs of the wind generation facilities which supply  
8 RECs, including an equity return of approximately \$27.3 million per year on such  
9 wind facilities to PSE's shareholders, as a component of the Company's regulated  
10 retail rates.

11 **Q: Please summarize your conclusions regarding PSE's claim to retain \$21.1**  
12 **million of REC sales proceeds in this case.**

13 A: It is not reasonable to allow PSE to retain \$21.1 million, or any amount, of the  
14 REC sales proceeds, particularly without evidence as to the basis for the amounts  
15 claimed, and without demonstration that the price PSE received for the RECs sold  
16 to the California utilities could not have been obtained without the settlement. I  
17 recommend that 100 percent of PSE's REC sales proceeds be returned to its retail  
18 customers who pay 100 percent of the cost of wind generation resources from  
19 which such RECs are supplied. In addition, all profits from the off-system energy  
20 sales made under the contracts negotiated with California utilities should be  
21 returned entirely to customers.

**VI. CALCULATION AND RATEMAKING TREATMENT  
OF REC AND CFI PROCEEDS**

**Q: What are the remaining issues regarding PSE's proposed treatment of REC and CFI revenues?**

**A:** Beyond what I discussed earlier, there are three additional issues that must be addressed:

- What is the appropriate method of calculating net proceeds from REC and CFI sales?
- How should the amount of REC and CFI sale proceeds be reflected in rates?
- What regulatory review process should be employed to ensure that the REC and CFI sales proceeds are properly calculated and returned to ratepayers in the future?

**Q: How does PSE propose to calculate the net proceeds from REC and CFI sales?**

**A:** PSE proposes to calculate the net proceeds from REC and CFI sales by subtracting the total costs and credits associated with such sales, or required to facilitate such sales, from the total sales revenues.<sup>32</sup> The Company indicates that these costs would include:

expenses incurred in negotiating the transactions, finalizing the sales agreements and fulfilling the obligations under such agreements, including, but not limited to, . . . attorney fees, broker commissions, royalty payments or other third party fees

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<sup>32</sup> Amended Petition, ¶12.

1 (such as WREGIS-related fees, the Center for Resource  
2 Solution fees and audit fees) and the net costs of the energy  
3 component of the transaction, if any.<sup>33</sup>  
4  
5

6 **Q: What amount of the above expenses has PSE recorded to-date in conjunction**  
7 **with its past REC and CFI sales?**

8 **A:** As shown in Table 2, PSE has recorded approximately **[BEGIN HIGHLY**  
9 **CONFIDENTIAL]** **XXXXXXX** **[END HIGHLY CONFIDENTIAL]** in total  
10 expenses associated with its REC and CFI sales through November of 2009.  
11

12 **[BEGIN HIGHLY CONFIDENTIAL]**  
13

14 XX  
15 XX  
16 XX  
17 XX  
18 XX  
19 XX  
20 XX  
21 XX  
22 XX  
23 XX  
24 XX  
25 XX  
26 XX  
27 XX  
28 XX  
29 XX  
30 XX  
31

32 **[END HIGHLY CONFIDENTIAL]**

<sup>33</sup> *Id.*

1       **Q:     Do you have any concerns with PSE's proposed calculation of net proceeds of**  
2       **RECs and CFIs?**

3       A:     Yes; I have two basic concerns. My first concern is that the definition of costs  
4       that PSE proposes is vague and could allow the Company to recover amounts that  
5       may be only peripherally related to the sales or are already recovered through  
6       PSE's base rates. For example, PSE has not directly stated whether its calculation  
7       of the net proceeds of REC and CFI sales may include labor or other costs that  
8       have also been reflected in its retail base rates.

9             My second concern relates to PSE's proposal to include "net costs of the  
10       energy component of the transaction" as a component of the costs considered in  
11       determining net proceeds from REC and CFI sales.<sup>34</sup> PSE indicates that these  
12       costs represent any difference between the contract price for energy and the cost  
13       incurred in supplying the energy transaction.<sup>35</sup> There is no apparent relationship  
14       between the cost of energy sold and the contract price of RECs under PSE's REC  
15       sale agreements. Therefore it would be unreasonable to adjust the net proceeds  
16       from RECs to reflect any such energy cost differences.

17       **Q:     What is your recommendation to address the concern regarding the potential**  
18       **for double-recovery or recovery of unrelated costs through the REC net**  
19       **proceeds calculation?**

20       A:     The Commission should require regular reporting of REC revenues and costs so  
21       that the Commission Staff and other interested parties can monitor the level of  
22

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<sup>34</sup> *Id.*

<sup>35</sup> See Exhibit No. SN-12, PSE's Response to Public Counsel Data Request No. 22.

1 REC proceeds reflected in rate credits to customers on an ongoing basis. In  
2 addition, I recommend that any costs reflected in PSE's REC proceeds  
3 calculations be subject to review and reconciliation in future PSE general rate  
4 proceedings.

5 **Q. What is PSE's proposed ratemaking treatment of REC and CFI proceeds**  
6 **that are allocated to customers under the Company's proposal in this case?**

7 A. PSE proposes to allocate the \$20 million of REC and CFI proceeds to low-income  
8 renewable energy and energy efficiency programs over a seven year period.<sup>36</sup>  
9 PSE is proposing that the remaining 40 percent of total REC proceeds that would  
10 be allocated to customers would be used to offset an approved regulatory asset,  
11 such as the storm damage regulatory asset associated with the December 2006  
12 wind storm.<sup>37</sup>

13 **Q: Would customers realize immediate benefits from REC and CFI sales**  
14 **proceeds under PSE's proposal?**

15 A: I cannot determine when the effect of PSE's proposed treatment of REC and CFI  
16 sales proceeds would be reflected as an offset to the Company's retail rates since  
17 PSE did not present a proposed tariff or other details of its proposed rate credits  
18 for such proceeds in its direct testimony. However, the Commission indicated in  
19 paragraph 11 of its January 10, 2010 Order Granting Motion to Strike Testimony  
20 regarding REC proceeds in Docket Nos. UE-090704/UG-090705, that it expected  
21 any final determination in this proceeding could be effective simultaneously with,  
22

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<sup>36</sup> Amended Petition, page 7.

<sup>37</sup> *Id.*, page 8.



1 or shortly following, the conclusion of the general rate case. Moreover, PSE has  
2 acknowledged that it expects the Commission will order that benefits from REC  
3 sales proceeds be passed through to customers immediately and that use of a non-  
4 general rate tariff would provide such immediate customer benefit.<sup>38</sup> Again, PSE  
5 has not proposed such a non-general rate tariff in its testimony in this case.

6 **Q: What is your recommendation regarding the appropriate methods to ensure**  
7 **that benefits of REC and CFI sales proceeds are immediately passed through**  
8 **to PSE's customers?**

9 A: I recommend that 100 percent of REC and CFI sales proceeds be credited to  
10 PSE's ratepayers and reflected in a manner that provides immediate customer  
11 benefits to the extent possible. In this regard, I recommend that the \$31.3 million  
12 of accumulated REC and CFI benefits, plus associated interest, that existed as of  
13 the end of November 2009 be immediately applied to offset the approved rate  
14 base for PSE's Wild Horse and Hopkins Ridge wind generation facilities, and that  
15 this adjustment be reflected in the compliance filing for PSE's approved rates  
16 resulting from the Company's pending general rate case.

17 While I do not take a position on the proposal to allocate a portion of  
18 revenues to low-income renewable energy and energy efficiency programs, I  
19 recommend that, should the Commission approve this allocation, any such  
20 funding be made from REC sale proceeds and any CFI proceeds collected after  
21 November 2009.

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<sup>38</sup> See Exhibit No. SN-13, PSE's Response to Public Counsel Data Request No. 42.

1                   Finally, I recommend that the remainder of REC and CFI sale proceeds  
2                   collected each month after November 2009 (subsequent to any allocations to low-  
3                   income renewable and efficiency programs) be immediately applied to reduce rate  
4                   base associated with PSE's Wild Horse and Hopkins Ridge wind generation  
5                   resources, and that the associated reduction in revenue requirements be credited to  
6                   all PSE retail customers through a non-general rate tariff, similar to the  
7                   Company's PTC tracker. It is my understanding that PSE does not expect to make  
8                   CFI sales after November 2009, so future funding may be derived solely from  
9                   REC sale proceeds.

10                  I further recommend that this REC Proceeds Tracker mechanism be  
11                  implemented as soon as this case is concluded, and that monthly credits used in  
12                  designing the initial tracker be based on REC revenue forecast provided by PSE  
13                  in its highly confidential response to Public Counsel Data Request No. 37.<sup>39</sup> I  
14                  recommend that this REC Proceeds Tracker remain in effect until all future REC  
15                  sales by PSE have been completed and the associated wind generation rate base  
16                  credits have been fully reflected in PSE's base rates.

17       **Q:    How do you recommend that REC proceeds be allocated among customers**  
18       **under your proposed REC Proceeds Tracker?**

19       **A:**    I recommend that the REC Proceeds Tracker be designed to allocate REC  
20                  proceeds among retail customers in the same manner that PSE wind generation  
21                  costs are currently treated, so that the REC tracker credits are allocated to  
22                  customers in the same manner that as are wind generation costs. In this way,

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<sup>39</sup> See Exhibit No. SN-5HC.

1 customers who pay for PSE's wind generation facilities will receive their fair  
2 share of the REC proceeds derived from such wind generation assets.

3 **Q: Why do you recommend that REC and CFI sale proceeds which have been**  
4 **realized through November of 2009 be credited to PSE's base rates instead of**  
5 **through your proposed REC Proceeds Tracker mechanism?**

6 A: As discussed earlier in my testimony, the Commission has indicated a desire to  
7 immediately pass through benefits of PSE's REC and CFI sales to customers.  
8 However, it is unknown how long it will take following the conclusion of this  
9 case for PSE to prepare, file, and obtain approval to implement its initial REC  
10 Proceeds Tracker mechanism. My recommendation to credit the REC and CFI  
11 proceeds collected through November 2009 to PSE's base rates recognizes that the  
12 amounts collected to date are sufficiently known and measurable to be included in  
13 PSE's base rates, and is further intended to meet the Commission's stated desire to  
14 pass through the credits as soon as reasonably possible. However, if it is not  
15 feasible to reflect the REC and CFI proceeds that have already been collected in  
16 PSE's base rates due to time limitations or other factors, I recommend that these  
17 proceeds from past REC and CFI sales instead be included as credits in PSE's  
18 initial REC Proceeds Tracker mechanism.

19 **Q: Do you have other recommendations regarding the regulatory review process**  
20 **that should be used to administer your proposed REC Proceeds Tracker**  
21 **mechanism and to provide oversight of PSE's management and accounting**  
22 **for REC sales in the future?**

1       A:     Yes. I recommend that PSE be required to adjust its REC Proceeds Tracker  
2             mechanism once every 12 months to reflect forecasted REC proceeds over the  
3             next 12-month cycle and to adjust for any differences between the forecasted REC  
4             proceeds used in the design of the REC Proceeds Tracker during the previous 12-  
5             month period and the actual REC sale proceeds recovered during that same  
6             period. As discussed earlier in my testimony, I recommend that PSE's  
7             calculations of REC and CFI proceeds be subject to review and final  
8             reconciliation in the Company's next general rate case.

9       **Q:     Do you have any other recommendations regarding future regulatory**  
10       **treatment of PSE's REC sales?**

11      A:     Yes. In light of questions raised in this case regarding PSE's past handling of  
12             REC sales, I believe that it would be beneficial for the Commission to increase  
13             oversight of PSE activities related to the sale of RECs to ensure that the benefits  
14             of such transactions are maximized for customers who are funding the costs of the  
15             facilities from which RECs are supplied. A recently approved settlement  
16             stipulation in Docket No. UE-090205, PacifiCorp's most recent general rate case,  
17             establishes terms for reporting and monitoring of REC sales activities by the  
18             utility on an ongoing basis. I recommend that the Commission adopt similar  
19             requirements for PSE to ensure that information is available to monitor PSE's  
20             REC sales and that customer benefits from such sales are being maximized.

21      **Q:     Does that conclude your testimony?**

22      A:     Yes.

23