

**EXHIBIT NO. \_\_\_\_ (RG-1HCT)**  
**DOCKET NO. UE-07 \_\_\_\_**  
**2007 PSE PCORC**  
**WITNESS: ROGER GARRATT**

**BEFORE THE  
WASHINGTON UTILITIES AND TRANSPORTATION COMMISSION**

**WASHINGTON UTILITIES AND  
TRANSPORTATION COMMISSION,**

**Complainant,**

**v.**

**PUGET SOUND ENERGY, INC.,**

**Respondent.**

**Docket No. UE-07 \_\_\_\_**

**PREFILED DIRECT TESTIMONY (HIGHLY CONFIDENTIAL) OF  
ROGER GARRATT  
ON BEHALF OF PUGET SOUND ENERGY, INC.**

**REDACTED  
VERSION**

**MARCH 20, 2007**

**PUGET SOUND ENERGY, INC.**

**PREFILED DIRECT TESTIMONY (HIGHLY CONFIDENTIAL) OF  
ROGER GARRATT**

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**PUGET SOUND ENERGY, INC.**

**PREFILED DIRECT TESTIMONY (HIGHLY CONFIDENTIAL) OF  
ROGER GARRATT**

**I. INTRODUCTION**

**Q. Please state your name, business address, and position with Puget Sound Energy, Inc.**

A. My name is Roger Garratt. My business address is 10885 N.E. Fourth Street Bellevue, WA 98004. I am the Director of Resource Acquisition within the Energy Resource Group for Puget Sound Energy, Inc. ("PSE" or "the Company").

**Q. Have you prepared an exhibit describing your education, relevant employment experience, and other professional qualifications?**

A. Yes, I have. It is Exhibit No. \_\_\_\_ (RG-2).

**Q. What are your duties as Director of Resource Acquisition within the Energy Resource Group for PSE?**

A. My present responsibilities include oversight of: (i) the acquisition of electric resources for the Company, commencing with the Request for Proposal ("RFP") process and culminating in the execution and closing of all of the definitive agreements necessary to acquire a resource; (ii) the construction and operation of the Company's wind projects; and (iii) contracts for long-term electric supply and

transmission service.

**Q. What is the nature of your testimony in this proceeding?**

A. My testimony presents, in greater detail than Mr. Eric Markell's executive summary:

- (i) The Company's evaluation of the proposals submitted in response to its RFP.
- (ii) How PSE's evaluation of resource alternatives led to the decision to acquire the 277 MW Goldendale combined cycle natural gas fired electric generation facility (the "Goldendale Generating Station" or "the Station").
- (iii) The Company's current status regarding the completion of the Wild Horse Wind Generating Project, a resource that emerged from the previous RFP process.

## **II. PSE'S EVALUATION OF RESOURCE ALTERNATIVES**

**A. Overview**

**Q. How did the Company approach its evaluation of acquiring potential resources to meet its need?**

A. Mr. Markell's testimony describes the process and analysis leading up to the Company's issuance of the RFP. The Company evaluated the proposals submitted in response to the RFP in two phases based on criteria that were designed to take into account qualitative and quantitative factors that the Company believed should be considered in deciding whether to acquire a potential resource. The quantitative analysis is described in more detail in the

1 testimony of Mr. James Elsea. My testimony focuses primarily on the qualitative  
2 analysis undertaken by the Company.

3 During Phase I of the RFP, PSE evaluated proposals based on each individual  
4 proposal's cost and on specific qualitative criteria. This process was designed to  
5 screen out proposals with high costs, unacceptable risks, or feasibility constraints  
6 with the goal of creating a "Candidate Short List" for continued evaluation in  
7 Phase II.

8 In Phase II, the Company performed more extensive due diligence on the  
9 proposals on the Candidate Short List, including but not limited to data requests,  
10 bidder presentations and site visits. The Company also evaluated a potential self-  
11 build option. Additionally, PSE quantitatively tested each project on the  
12 Candidate Short List in a variety of portfolios, scenarios and in Monte Carlo  
13 analysis. *See generally* Exhibit No. \_\_\_\_ (WJE-1HCT) at pages 29-38. In Phase II,  
14 the Company ultimately identified a "Short List" of projects that PSE would seek  
15 to acquire by reaching definitive agreements through additional negotiations and  
16 due diligence.

17 **Q. What processes did the Company put in place to organize and document its**  
18 **efforts?**

19 A. Company staff responsible for this evaluation worked extensively on the  
20 evaluation process from the time responses to the RFP were submitted in  
21 January 2006 and continue to work on the evaluation process for those projects

1 still on the Short List.

2 Personnel involved in the evaluation met weekly to review and document  
3 progress made as of that time and to discuss any issues or questions that had  
4 arisen. In addition to its own staff, PSE used outside consulting firms to evaluate  
5 the technical and environmental attributes of the proposals.

6 During the course of the evaluation process, Energy Resources staff regularly  
7 updated the Company's officers and the Commission Staff on the status of the  
8 evaluation and any preliminary conclusions through presentations documented  
9 primarily in power point slides. The Company's management, in turn, regularly  
10 apprised PSE's Board of Directors of the status of the evaluation process.

11 The Company's evaluation process and conclusions, reached at various stages of  
12 its analysis, are further explained below, and were documented in reports  
13 prepared during the course of the evaluation.

14 **B. Phase I of the RFP Evaluation**

15 **1. The Proposals.**

16 **Q. What proposals did the Company evaluate in Phase I?**

17 A. In response to the RFP, PSE received 48 unique proposals from 38 different  
18 owners/developers. Many of the proposals contained multiple options such as  
19 power purchase agreements, asset ownership, and a combination of a power

1 purchase agreement and partial ownership. Considering all the options offered  
2 under each proposal, the Company evaluated more than 120 different proposals.  
3 With respect to fuel source, 36% of the proposals were for natural gas fired  
4 facilities, 21% were for wind, 6% were for hydro, 13% were for coal, 15% were  
5 power purchase agreements that did not specify a fuel source (i.e., system power  
6 purchase agreements), and 9% were for biomass, geothermal and other  
7 renewables. *See* Exhibit No. \_\_\_\_ (RG-3HC) at page 3.

8 **Q. In addition to the proposals received from the RFP solicitation, did PSE**  
9 **receive and review any other proposals during this process?**

10 A. Yes, PSE has an ongoing obligation to look at all proposals offered. Most  
11 notably, the proposal for the Goldendale Generating Station did not originate  
12 from the RFP solicitation.

13 **2. The Criteria**

14 **Q. What criteria did the Company apply during Phase I of the evaluation**  
15 **process?**

16 A. During Phase I, PSE applied the following general criteria to the proposals:

- 17 • Compatibility with PSE Resource Need;
- 18 • Cost Minimization;
- 19 • Risk Management;
- 20 • Public Benefits; and



- Strategic and Financial.

These criteria are described in greater detail below, as well as in Exhibit No. \_\_\_\_ (RG-3HC) at pages 6-7.

**Q. What considerations were included under the “Compatibility with Need” criterion?**

A. This criterion focused on the Company’s interest in meeting its long-term energy need while reducing the risk of excess capacity. The Company was interested in projects that would come on line sooner rather than later because of its ongoing exposure to wholesale market risks. Because the Company’s loads are much higher in winter than in summer months, the Company was very interested in resources that were or could be shaped to balance the seasonality of its loads. The Company also considered its need to diversify its portfolio, pursuant to the conclusions of its 2005 Least Cost Plan.

**Q. What considerations were included under the “Cost Minimization” criterion?**

A. The Company sought to identify the lowest cost alternatives that would meet its energy and capacity needs, looking not only at prices that might be stated in proposals but at other factors that would ultimately impact the cost of the resource. Examples of such costs include the costs of transmission, emission costs, fuel transportation and energy firming.

1 **Q. What considerations were included under the “Risk Management” criterion?**

2 A. The Company considered many risks, particularly those that could threaten the  
3 feasibility of a project or the timing of completion. Such risks included  
4 environmental and permitting risks. The Company also evaluated risks associated  
5 with whether a potential counterparty would actually be able to perform its  
6 obligations related to a project proposal. Other considerations included the  
7 desirability of long-term flexibility in order to better respond to future changes in  
8 the industry or PSE’s portfolio.

9 **Q. What considerations were included under the “Public Benefits” criterion?**

10 A. The Company considered whether projects would contribute to regional energy  
11 adequacy and contribute to environmental and efficiency interests such as  
12 reducing portfolio emission levels. Community impacts were also considered.

13 **Q. What considerations were included under the “Strategic and Financial”**  
14 **criterion?**

15 A. These considerations included potential exposure to future environmental  
16 regulations and future state wholesale market restructuring. They also included  
17 balance sheet impacts and potential degradation of the Company’s credit quality  
18 or ability to fund ongoing operations due to factors such as credit support  
19 requirements and imputed debt.

20 /////

1           **3.     PSE's Initial Screening and Application of the Criteria.**

2     **Q.     How did the Company apply these criteria?**

3     A.     The Company first screened the 120 proposals to identify any that appeared  
4           clearly unsatisfactory because the project lacked viability. Several proposals  
5           were identified as clearly not feasible for a variety of reasons. PSE sent 18  
6           projects that involved short-term opportunities to the Energy Risk Management  
7           Department for consideration. Jim Elsea discusses the analysis of these short-  
8           term projects in his prefiled direct testimony, Exhibit No. \_\_ (WJE-1HCT).

9           The Company then performed quantitative analysis using the Company's  
10          Portfolio Screening Model, to develop a cost ranking for each individual resource  
11          proposal. These results are presented as Exhibit No. \_\_\_\_ (WJE-7HC) and Exhibit  
12          No. \_\_\_\_ (WJE-8HC). For further description of the quantitative process, please  
13          see generally the testimony of Mr. W. James Elsea.

14    **Q.     Did the Company do anything in addition to this initial Portfolio Screening**  
15    **Model analysis?**

16    A.     The Company also conducted an extensive evaluation of qualitative factors  
17           related to its evaluation criteria. Such factors included availability and potential  
18           problems regarding fuel supply and transmission. The Company also evaluated  
19           whether the bidders' projections regarding their proposal appeared to be realistic,  
20           as the Company had concerns regarding the likely ability of bidders to actually

1 deliver what they proposed. Subject matter experts within the Company were  
2 assigned to closely review various project proposals or aspects of proposals with  
3 which they were familiar. After each team performed their evaluations, positive  
4 and negative comments were documented. Then, through the weekly evaluation  
5 meetings, the teams summarized their evaluations by assigning a qualitative  
6 evaluation rating for each of the proposals using a rating system of “Low,”  
7 “Medium,” and “High,” with “High” being considered more favorable and “Low”  
8 being considered less favorable. This qualitative rating system was applied in  
9 order to identify the most favorable proposals. See Exhibit No. \_\_\_\_ (RG-4HC) for  
10 the evaluations from Phase I.

11 **Q. Please describe the evaluation teams.**

12 A. In both Phase I and Phase II of the evaluations, subject matter experts within the  
13 Company were assigned to review project proposals and perform due diligence in  
14 order to assess the proposals or aspects of proposals within their specialized area.  
15 PSE’s RFP evaluation process was a cooperative effort involving 40-50  
16 individuals across the Company that were grouped in the following sixteen teams:  
17 (i) Business / Commercial Issues; (ii) Fuel Supply; (iii) Transmission;  
18 (iv) Technology; (v) Quantitative; (vi) Environmental; (vii) Real Estate;  
19 (viii) Community Relations; (ix) Operations; (x) Credit/Finance/Tax/Accounting;  
20 (xi) Regulatory; (xii) Insurance; (xiii) Legal; (xiv) Human Resources;  
21 (xv) Government Relations (Federal); and (xvi) Government Relations (State).  
22 See Exhibit No. \_\_\_\_ (RG-3HC) at page 173 for the subject matter teams.

1 **Q. Would you please provide some examples of the teams' evaluation process**  
2 **and analysis?**

3 A. Some examples of the work, process and results of the evaluation teams are:

- 4 • The community affairs team visited the local community where a  
5 proposed project was located or potentially would be located. The team  
6 talked with community stakeholders and assessed local support.  
7 Information was gathered from public, local, state and federal government  
8 entities and Native American nations. The team collected local newspaper  
9 editorials and letters to the editor that discussed project proposals. This  
10 allowed PSE to understand and address the concerns of the local  
11 community regarding a potential project and helped position PSE for  
12 further development of the project.
- 13 • The real estate team engaged in extensive review of the site control  
14 documents presented in the proposals. As additional information was  
15 needed, particularly in the Phase II evaluations, the real estate team visited  
16 project proposal sites, walked or drove the sites, and "ground truthed" the  
17 representations contained in the proposals. This helped PSE identify  
18 potential issues that were not described in the proposal documents.
- 19 • The environmental team researched the web sites of local, state, and  
20 federal agencies in order to determine whether there were any  
21 environmentally sensitive issues and to uncover any assessment  
22 documents that had been produced. This allowed PSE to more fully  
23 evaluate environmentally sensitive issues that needed to be addressed  
24 within the proposals.
- 25 • On the permitting side of the environmental team, local, state, and federal  
26 permitting processes were outlined in order to ascertain the status of the  
27 project proposals' permits. An evaluation of the process and risks of  
28 acquiring such permits were also address by the team's efforts.

29 **Q. Would you please provide some examples of how the Company applied these**  
30 **qualitative factors?**

31 A. As one example, as described above, Company personnel with real estate  
32 experience reviewed the proposals with an eye toward the status and

1 documentation of real estate rights related to a project. Projects at the earliest  
2 stages of real estate execution or with no real estate documentation provided for  
3 review received a “low” ranking with respect to this factor; proposals containing  
4 plans and/or discussion of real estate rights but with incomplete or insufficient  
5 documentation received a “medium” ranking, and those with fee ownership  
6 and/or signed real estate documentation (or where a plant was operational and  
7 assumed to have valid operating rights) received a “high” ranking.

8 Transmission issues provide another example. Company personnel evaluated the  
9 location of proposed projects in relation to PSE’s system as well as transmission  
10 paths and known transmission constraints. Proposals that were not to be  
11 delivered directly to PSE’s system were reviewed to determine whether the  
12 developer had already submitted a request for transmission rights and the status of  
13 that request in the transmission provider’s queue.

14 Company engineers also evaluated the technologies proposed to be used for each  
15 project. They noted positive attributes such as the reliability or efficiency of a  
16 type of turbine as well as negative attributes such as lack of information on the  
17 type of equipment proposed to be used for a project, and ultimately assigned high,  
18 medium or low ratings to each project with respect to the technology evaluation.

19 **Q. Did the Company do all of the Phase I evaluation in-house?**

20 A. No. The Company retained Global Energy Concepts to perform an in-depth  
21 evaluation of the wind proposals that PSE received in the RFP. The report

1 prepared by Global Energy Concepts is provided as Exhibit No. \_\_\_\_ (RG-5HC).  
2 Additionally, PSE hired Altera Energy to assist in the RFP process.

3 **Q. Why did the Company hire Global Energy Concepts?**

4 A. The Company sought external assistance in evaluating wind projects because of  
5 its lack of technical experience with wind energy, especially meteorological  
6 expertise. Global Energy Concepts is recognized internationally as a leading  
7 authority on all aspects of wind energy. Global Energy Concepts has acted as  
8 project engineer on behalf of lenders, insurers and owners on numerous projects.  
9 As part of this work, it has performed due diligence with respect to wind turbine  
10 technology and wind resource assessment, and it has consulted with respect to  
11 various aspects of project design and construction including economic modeling.  
12 Global Energy Concepts maintains its independence by taking no equity stake in  
13 any development or technology and works purely on a consultancy basis.

14 **Q. What did Global Energy Concepts do?**

15 A. Global Energy Concepts undertook its own evaluation of the wind projects. It  
16 applied PSE's Phase I criteria to the projects based on its knowledge of the wind  
17 generation industry. Its most significant contribution to the evaluation process  
18 was to look at each proposed project from the perspective of an independent  
19 engineer. By providing PSE feedback on the engineering and financial viability  
20 of the proposal (i.e., determining whether the information presented in the

1 proposal was sufficient for a lender or equity investor to proceed), Global Energy  
2 Concepts provided PSE with expert advice to supplement the Company's own  
3 judgment. Global Energy Concepts also employed its proprietary software for  
4 analyzing topographic and wind turbine wake effects on project output.

5 Additional detail regarding the Company's analysis of issues specific to the wind  
6 power proposals is discussed below.

7 **Q. Why did the Company hire Altera Energy?**

8 A. Altera Energy was retained to assist the PSE resource evaluation team with the  
9 review and evaluation of the business and commercial issues of the proposals.

10 **Q. What did Altera Energy do?**

11 A. Altera participated in evaluation meetings to discuss key findings, provided data  
12 analysis support in the evaluation of the proposals and to help document the  
13 process. In addition, they provided an outside and fresh expertise on the RFP  
14 process and evaluation. For example, Altera suggested that PSE use a new  
15 quantitative metric--the Portfolio Benefit Ratio--to better provide parity among  
16 projects of all sizes. Please see the prefiled direct testimony of Mr. W. James  
17 Elsea, Exhibit No. \_\_\_\_ (WJE-1HCT), for a description of the Portfolio Benefit  
18 Ratio.

19 /////



1           **4.     The “Most Favorable Proposals” List and Ultimate Phase I**  
2           **“Candidate Short List”.**

3     **Q.     How did the Company then proceed?**

4     A.     The qualitative evaluation and rating, combined with the Portfolio Screening  
5           Model ranking, eliminated certain proposals with high costs, unacceptable risks,  
6           and/or feasibility constraints and showed others as favorable. PSE then selected  
7           sixteen proposals for a Candidate Short List.

8     **Q.     How did the Company proceed with respect to the Candidate Short List?**

9           The sixteen proposals on the Candidate Short List appeared to offer the lowest  
10          cost and lowest acceptable risk for obtaining additional electric supply. The  
11          proposals selected for the Candidate Short List included a diverse mix of  
12          ownership types and fuel sources, specifically: Five natural gas-fired projects,  
13          four wind projects, three system power purchase agreements, two coal projects,  
14          one geothermal project and one hydropower facility. The proposals on the  
15          Candidate Short List and their ratings under the Phase I evaluation criteria are  
16          provided in Exhibit No. \_\_\_\_ (RG-3HC) at pages 220-231. The Company  
17          presented the Phase I analyses and the Candidate Short List to Commission Staff.  
18          See Exhibit No. \_\_\_\_ (RG-6HC).

19          ////

20          ////

1 **C. Phase II of the RFP Evaluation**

2 **1. The Criteria.**

3 **Q. Did the projects evaluated in Phase II differ from the original Candidate**  
4 **Short List?**

5 A. Yes. Early in Phase II, PSE was notified by three of the respondents whose  
6 projects had been selected for the Candidate Short List that their project  
7 conditions had changed. The first respondent indicated that the project was being  
8 sold to another entity. The second respondent withdrew its proposal due to  
9 redeployment of turbines originally earmarked for the project proposed to PSE.  
10 The third respondent indicated a delay until 2008 due to recent permitting  
11 challenges, which imposed significant cost and Production Tax Credit risk on the  
12 proposal. To ensure strong comparative analysis, the next best projects were  
13 added to the Candidate Short List and evaluated in Phase II.

14 **Q. What criteria did the Company apply during Phase II of the evaluation**  
15 **process?**

16 A. During Phase II, PSE continued to apply the Phase I evaluation criteria and placed  
17 further emphasis on the following qualitative factors:

- 18 • Transmission and Integration Alternatives;
- 19 • Comparison of power purchase agreements and Ownership Alternatives;
- 20 • Ability to Deliver;

- Experience of Developers;
- Guarantees and Security; and
- Environmental and Public Benefit.

The Phase II criteria are described in further detail in Exhibit No. \_\_\_\_ (RG-7HC).

**Q. How did the Company apply these criteria**

A. The Company reevaluated the proposals on the Candidate Short List against each other by combining quantitative cost rankings with extensive evaluation of qualitative criteria, which were again summarized in “High,” “Medium,” and “Low” qualitative ratings. The Company based this evaluation on information that had been provided in the initial proposals as well as on responses to information requests that PSE sent to the owners and developers of the projects on the Candidate Short List. The Company also considered information discovered through its due diligence efforts.

**Q. What additional information did the Company request?**

A. PSE requested information such as copies of existing permits or applications for permits, a list of agreements contemplated between PSE and the developer, information about contingency plans in the event certain assumptions did not materialize, and preliminary information about the commercial agreements and terms the bidder anticipated requesting of PSE. PSE also inquired as to certain projects whether the bidder would be willing to agree to terms such as price

1 guarantees or date certainty to the extent such terms were not addressed in the  
2 original proposal.

3 **2. PSE's Quantitative Evaluation of the Proposals.**

4 **Q. Did the Company quantitatively evaluate proposals on the Candidate Short**  
5 **List during Phase II?**

6 A. Yes. Please see the prefiled direct testimony of Mr. W. James Elsea, Exhibit  
7 No. \_\_\_\_ (WJE-1HCT), for a description of the quantitative evaluation process  
8 utilized by the Company in Phase II.

9 **3. PSE's Qualitative Evaluation of Proposals.**

10 **Q. What qualitative evaluation did the Company undertake in Phase II?**

11 A. The Company's qualitative evaluation included continuing efforts such as those  
12 described above for Phase I. See Exhibit No. \_\_\_\_ (RG-8HC) for the qualitative  
13 evaluations from Phase I. In addition, the Company conducted the due diligence  
14 described below and considered information regarding qualitative factors that  
15 resulted from those investigations. The Company also evaluated the  
16 creditworthiness of the bidders as potential counterparties to long-term  
17 transactions, for the reasons described below.

18 ////

19 ////

1           **4.     Due Diligence.**

2       **Q.     Please explain what is meant by “due diligence”?**

3       A.     Due diligence is the process by which a party investigates and evaluates a  
4             potential investment. This often involves the examination of business operations,  
5             engineering design, equipment performance, environmental conditions, permit  
6             status, real estate and other necessary property rights status, and the verification  
7             of other material facts. Due diligence may also assess factors that affect the  
8             future operation of a potential acquisition and the prospects that the acquisition  
9             will perform as expected.

10      **Q.     What due diligence did the Company perform with respect to the potential**  
11       **projects?**

12      A.     The Company conducted due diligence with respect to environmental issues and  
13             concerns, permitting status and conditions, real estate matters, counterparty credit,  
14             the wind resource projections made by project developers, legal agreements and  
15             technical matters associated with the engineering, construction and operation of  
16             potential projects that were asset based.

17      **Q.     How did the Company go about performing this due diligence?**

18      A.     PSE conducted much of this review in-house, through personnel experienced in  
19             legal, environmental and real estate matters, but also relied upon outside expertise

1 on environmental and permitting matters, real estate issues, and technical matters.  
2 With respect to wind projections, wind project feasibility, and technical  
3 compatibility, the Company continued to work with Global Energy Concepts, as  
4 described above.

5 The Company's due diligence efforts began during the Phase I evaluation process  
6 and continued thereafter as to projects that ultimately were selected to the  
7 Phase II Candidate Short List, as well as projects on the continuing evaluation  
8 list.

9 **Q. What were some of the results of these due diligence efforts?**

10 A. These efforts caused PSE to decide not to pursue certain projects on the  
11 Candidate Short List and also confirmed the attractiveness of certain projects.  
12 For example, based on the Phase II analysis, PSE determined that there was too  
13 much uncertainty and risk around the complexity of a transmission solution for a  
14 storage hydroelectric project located in Southeast Alaska.

15 **5. Credit and Balance Sheet Issues With Respect to Power**  
16 **Purchase Agreements.**

17 **Q. Do you have additional comments on other factors considered in the**  
18 **Company's evaluation?**

19 A. Yes. Creditworthiness, credit support and credit quality issues continue to be of  
20 importance in evaluating power purchase agreements as compared to ownership

options.

**Q. What were the Company's concerns about creditworthiness and credit support?**

A. The Company's concerns regarding the financial condition of potential counterparties and the credit required to support long-term, fixed price energy contracts were extensively documented in the Company's prior rate proceedings.

It is very common for companies to include in power purchase agreements a requirement that credit assurances be provided to better protect a party from the risk that the other will not perform its obligations under the contract. Credit provisions are generally reciprocal, that is, the counterparty or PSE would provide to the other contractual access to immediately available funds in the form of a letter of credit or cash to cover the daily market-to-market exposure (above a certain threshold level).

**Q. Did bidders of power purchase agreements request such credit support from PSE?**

A. Yes. Among various proposed terms and conditions, bidders of power purchase agreements requested that the Company post credit support to secure its obligations to pay for purchased power under the long-term power purchase agreements. Potential counterparties requested credit support from PSE in the form of a demand letter of credit or cash.

1 **Q. Did the Company have concerns about the creditworthiness of any**  
2 **counterparties?**

3 A. Yes, the Company had creditworthiness concerns with entities not financially  
4 rated or of speculative grade. Further, project companies held as a special  
5 purpose entity, such as a limited liability company, wherein the project is the only  
6 asset, were of particular concern. In those cases, the Company requested credit  
7 support, generally in the form of a parental guarantee.

8 **Q. Did the Company seek to address these concerns without rejecting the**  
9 **resource proposal?**

10 A. Proposals are selected based on their ability to meet the established criteria that  
11 PSE has outlined in its RFP solicitation, and that are offered at the lowest  
12 reasonable cost with the lowest reasonable risk. In Phase I, no project was  
13 eliminated based on credit. Once the selection of the Candidate Short List is  
14 identified at the conclusion of Phase I, credit becomes significant to the analysis  
15 and evaluation of the proposal.

16 **Q. Did the Company have other concerns about power purchase agreements?**

17 A. Yes. Credit rating agencies view electric utility power purchase agreements as  
18 debt-like in nature and, in their analysis of the Company's financial strength and  
19 risk factors, treat a portion of the Company's obligation under such contracts as  
20 debt. This "imputed debt" is a significant concern for the Company because of its



1 impact on the Company's credit quality. Moreover, the Commission's 1994  
2 prudence order expressly instructed the Company to consider "rating agencies'  
3 views of purchased power" and "to quantify the impact of future resource  
4 acquisitions on capital cost and capital structure."<sup>1</sup>

5 **Q. Did the Company consider the impact of imputed debt when comparing**  
6 **power purchase agreements to ownership options?**

7 A. Yes. The Company's quantitative analysis of the competing resource proposals  
8 took into account costs related to debt that would be imputed to the Company if it  
9 entered into various proposed power purchase agreements, as described in the  
10 prefiled direct testimony of Mr. W. James Elsea, Exhibit No. \_\_\_\_ (WJE-1HCT).

11 **D. PSE Also Considered a Self-Build Option**

12 **Q. Did the Company analyze a self-build option in addition to the projects**  
13 **proposed in response to the RFP?**

14 A. Yes. The responses to PSE's 2005 All-Source RFP included several self-build  
15 alternatives. The self-build proposals can be divided into two types—each  
16 requiring different levels of PSE involvement in both the development activities  
17 and the construction build-out. The two types of proposals offered are those in  
18 which:

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<sup>1</sup> *WUTC v. Puget Sound Power & Light Co.*, Docket No. UE-921262, *et al.*, Nineteenth Supplemental Order (September 27, 1994) at 35-36.

- 1           i)       PSE plays a key role in the remaining development activities and funds  
2                   the cost of completing the project with the developer; or
- 3           ii)       PSE purchases the existing development assets from the developer and  
4                   PSE completes the project on its own.

5           Both types of self-build proposals result in PSE ownership of the project. In some  
6           cases project ownership is transferred to PSE early in the development stage and  
7           in other cases the ownership transfer occurs at the completion of the project.

8   **Q.     Please describe the self-build analysis that was performed.**

9   A.     As defined by the RFP evaluation criteria, the self-build proposals were evaluated  
10           in the same manner as all other proposals. However, greater diligence was  
11           observed when analyzing the costs of the remaining development activities and  
12           construction build-out. PSE relied on costs supplied by the developer. Where  
13           costs were not defined, PSE solicited pricing from the original equipment  
14           manufacturers. Where feasible, PSE used costs based on its existing operational  
15           experience from recent asset purchases including a half interest in EPCOR's  
16           combined cycle gas plant, Frederickson I, and more recently, PSE's acquisition of  
17           two wind farms. Also, additional costs that PSE would be required to fund in  
18           order to self-build the project were added to the project economics during the  
19           quantitative evaluation.

Of the thirteen projects that were included on the Candidate Short List, nine of the projects could be considered self-build.

REDACTED  
VERSION

**E. Results of the Phase II Evaluation**

**Q. What did the Company do with the qualitative, quantitative, and due diligence analyses discussed in your preceding testimony?**

A. Combining the qualitative, quantitative, and due diligence analyses led PSE to develop a Short List of proposals that combined low projected levelized costs (as compared to other proposals) with acceptable evaluations with respect to qualitative factors.

**Q. What did the Company conclude as a result of the Phase II evaluation?**

A. PSE ultimately selected the following resources for inclusion on the Short List of potential acquisition opportunities.

Project Name Owner/Developer	Size (MW)	Fuel	Proposal Type
██████████	██████	Geothermal	PPA
██████████	██████	Wind	Ownership
██████████	██████	Gas	PPA
Goldendale	277	Gas	Ownership
██████████	██████	Gas	Ownership
██████████	██████	System Power	PPA



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4. Goldendale – Goldendale is among the most efficient plants in the Pacific Northwest, has transmission and gas transportation solutions, and could be purchased at a steep discount.

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The Company presented the Phase II Analyses and the Short List to Commission Staff. *See* Exhibit No. \_\_\_\_ (RG-9HC) and Exhibit No. \_\_\_\_ (RG-10HC).

16

17

**Q. Did the Company reject those proposals that were not placed on the Short List?**

18

19

A. No. PSE determined that promising proposals that did not make the Short List

1 should be placed on a “continuing investigation” list so that PSE could continue  
2 to monitor their status and potentially reconsider whether any of these proposals  
3 should be pursued.

REDACTED  
VERSION

4 **F. PSE’s Efforts to Finalize Contracts**

5 **Q. How did the Company proceed with respect to the potential acquisitions that**  
6 **made the Phase II Short List?**

7 A. PSE is in various stages of negotiations with the seven short-listed projects. The  
8 status of each of the negotiations is briefly outlined below.

- 9 1. [REDACTED]  
10 [REDACTED].
- 11 2. [REDACTED]  
12 [REDACTED]  
13 [REDACTED].
- 14 3. [REDACTED].
- 15 4. Goldendale – PSE has purchased the Goldendale Generating Station.
- 16 5. [REDACTED]  
17 [REDACTED].

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6. [REDACTED]
- [REDACTED]
7. [REDACTED]
- [REDACTED]

**Q. Does the Company anticipate that it will acquire any of these Short List resources while this case is pending before the Commission?**

A. It is possible that PSE will acquire some of these resources while this case is pending. It is difficult to predict at this time.

**III. THE GOLDENDALE GENERATING STATION**

**A. Facility Description**

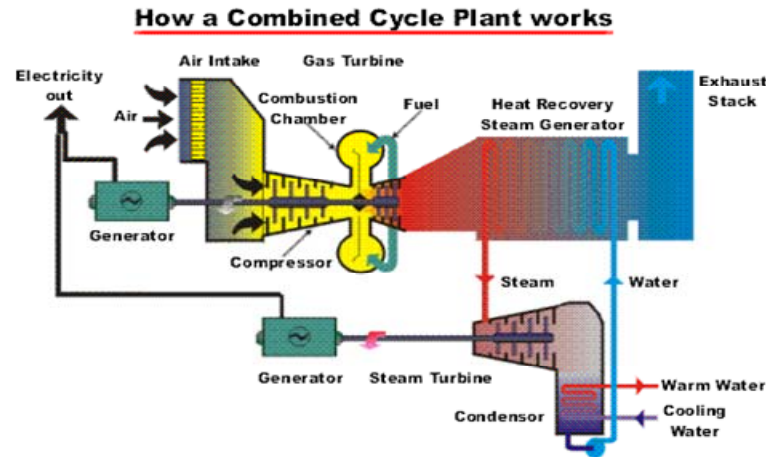
**REDACTED  
VERSION**

**Q. Please describe the Goldendale Generating Station.**

A. The Goldendale Generating Station is a 277 MW natural gas-fired combined cycle generating facility (252 MW “nominal” plus 25 MW duct firing) located on an approximately 42-acre site within the Goldendale Industrial Park and the City of Goldendale, Washington. The Station was developed and constructed by Calpine on a greenfield site and achieved commercial operation in September 2004.

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The following diagram depicts the combined cycle process.



The primary components of the plant consist of (i) a General Electric (“GE”) Frame 7FA model combustion turbine and generator, (ii) a Babcock-Hitachi heat recovery steam generator, (iii) a Hitachi steam turbine, and (iv) a Siemens generator. Goldendale’s low heat rate makes it one of the most efficient generating facilities in the Western Energy Coordinating Council (“WECC”) region.

The GE 7FA is a mature technology, proven and well understood. GE’s 7FA dominates the F-class combustion turbine market with the largest installed base of any manufacturer. GE’s F-class fleet includes more than 900 units in operation worldwide and has compiled more than ten million hours of commercial operation. Independent operating data confirms that fleet average reliability is about 98% with an availability of 93%. The availability of parts and service is excellent.



1 The plant was originally designed for baseload operation. The Babcock-Hitachi  
2 heat recovery steam generator has a number of design features that allow for  
3 improved operating profiles compared to a conventionally designed heat recovery  
4 steam generator, such as its improved readiness capability and reduced tendency  
5 to trip the steam generator. Although supported by a smaller installed base, the  
6 Hitachi steam turbine and Siemens generator are each recognized as reliable  
7 equipment. The availability of parts and service is considered good.

8 **Q. Please describe the electric transmission arrangements for the Goldendale**  
9 **Generating Station.**

10 A. As part of the Station acquisition, PSE acquired long-term, firm, point-to-point  
11 transmission service agreements with Klickitat County Public Utility District  
12 (“KPUD”) and the Bonneville Power Administration (“BPA”). The Project is  
13 interconnected at the E.E. Clouse Substation, which is owned and operated by  
14 KPUD. The substation is located on a 4.04 acre parcel owned by KPUD within  
15 the Station’s borders, but exclusive of the Station’s 41.65 acres. KPUD provides  
16 approximately ten miles of 230 kV transmission access to the interconnection  
17 point with the BPA transmission system at the Harvalum Substation. KPUD also  
18 provides station service power for the Station. The cost of this power has been  
19 included in the quantitative analysis.

20 Under the Station’s point-to-point transmission agreement with BPA, the power  
21 received at the Harvalum Substation is then delivered to the Mid-Columbia

trading hub (“Mid-C”). While Mid-C provides the greatest liquidity for wholesale trading in the Pacific Northwest, particularly for a merchant generator, PSE’s need, as a load-serving entity, is to have power delivered directly to its system. Moving power from Mid-C across the Cascades can pose constraint problems in the winter.

BPA has completed its public process to reassess and evaluate its transmission capability across its system. As a result, PSE expects to receive a redirect from the Station’s Mid-C point of delivery directly to PSE’s load centers at Covington and Maple Valley in April, 2007. The transmission costs included in this case assumes this redirect will occur. This redirect provides both enhanced reliability and significant financial benefits to PSE customers of an estimated \$30 million net present value savings over 20 years or a \$5.35/MWh reduction on a levelized cost basis, and was taken into consideration when establishing PSE’s bidding strategy. See Exhibit No. \_\_\_\_ (WJE-1HCT) for further details.

**Q. Please describe the gas transportation arrangements for the Goldendale Generating Station.**

A. The Company will enter into a contract with a third party to acquire [REDACTED] [REDACTED] additional long-term pipeline transportation capacity to serve the Goldendale Generating Station on Northwest Pipeline Company.

Although the primary delivery point for this pipeline is not at Goldendale, PSE will reassign (or “Flex”) the delivery point to the Goldendale Generating Station

1 when possible. Northwest Pipeline is required to accommodate requests to flex  
2 delivery points if operationally feasible. There may be times when Northwest  
3 Pipeline may not be able to accommodate requests to flex the delivery points.  
4 Such conditions could occur if Sumas gas prices are trading at a significant  
5 discount to Rockies, in the event of maintenance or if some unforeseen physical  
6 event should occur.

7 As a backup, for times when Northwest Pipeline may not be able to accommodate  
8 PSE's request to flex the delivery point [REDACTED], PSE proposes  
9 to physically exchange natural gas between the electric generation fuel book and  
10 the gas customer (or PGA) book. Under such exchange, gas from Sumas will be  
11 delivered over the acquired capacity to meet gas customer loads, and an  
12 equivalent amount of gas from the Rockies will be delivered over Northwest  
13 Pipeline transport capacity to meet the generation fuel needs for the Goldendale  
14 Generating Station. (This practice is generally referred to as "displacement" in  
15 the gas industry.) To compensate gas customers for this flexibility, PSE proposes  
16 an annual transfer of a \$250,000 compensation payment from the electric  
17 generation fuel book to the PGA book. This will help ensure that gas customers  
18 are fully compensated for such service.

19 As part of the Goldendale Generating Station, PSE also acquired the rights for gas  
20 transportation on a 5.1 mile lateral from Northwest Pipeline Company's mainline  
21 facilities to the Goldendale Generating Station.

1 **Q. Please describe the fuel supply arrangements for the Goldendale Generating**  
2 **Station.**

3 A. Natural gas is the primary and only fuel supply for the Goldendale Generating  
4 Station. The Station is not capable of dual fuel use (without equipment retrofit)  
5 and has no distillate storage capability or an air permit that allows distillate use.

6 Such limitations are common to almost all gas-fired facilities of recent vintage.

7 The fuel supply requirements for the Goldendale Generating Station will be  
8 managed in a manner consistent with the Company's well-documented and  
9 established hedging strategies. PSE's operations and trading group closely  
10 monitors and continuously evaluates the need for additional fuel supplies based  
11 on daily updates of its dispatch models.

12 **Q. Please describe the water supply arrangements for the Goldendale**  
13 **Generating Station.**

14 A. Raw water supply is provided by the City of Goldendale under a 30-year  
15 agreement. To reduce the consumption of water, the plant employs an advanced  
16 condensing system that includes a conventional condenser and an air-cooled  
17 condenser operating in parallel. Two water storage tanks hold about 2.2 million  
18 gallons each; a smaller tank holds de-mineralized water that has been treated to  
19 protect the equipment.

20 /////

1     **B.     Additional Due Diligence**

2     **Q.     Did PSE evaluate the Goldendale Generating Station prior to the RFP?**

3     A.     In June 2005, through an informal solicitation, Calpine solicited potential bidders  
4           in a reverse auction process for sale of its Northwest generation assets, including  
5           the Goldendale Generating Station. Previously, Calpine had publicly announced  
6           that as part of its strategic plan to meet its debt reduction, it would divest assets  
7           that were no longer strategic to its core markets, which it defined as California  
8           and Texas.

9           PSE submitted an indicative non-binding bid on June 29, 2005, and was selected  
10          by Calpine in early July 2005. PSE and Calpine first negotiated and then entered  
11          into a non-binding Letter of Intent at the end of August 2005. At the conclusion  
12          of the Company's exclusive 90-day due diligence period set forth in the Letter of  
13          Intent, Calpine's much publicized deteriorating credit condition caused PSE to  
14          suspend negotiations. On December 20, 2005, Calpine and its affiliate companies  
15          filed for a reorganization bankruptcy under Chapter 11 of the U.S. Bankruptcy  
16          Code. PSE's interest in the Station remained as a potential purchase out of  
17          bankruptcy.

18          In early January 2006, after the ground rules of the Calpine bankruptcy were set  
19          by the court and Calpine commenced the process of selling some of its generation  
20          assets, PSE and Calpine restarted discussions for the potential purchase of the  
21          Station. Throughout those discussions, PSE evaluated the acquisition of the

Goldendale Generating Station against the other resource alternatives revealed in PSE's RFP solicitation and against other resources apparent in the marketplace.

**Q. What additional due diligence did PSE conduct with respect to the Goldendale Generating Station?**

A. The Company conducted a comprehensive review of legal, commercial, environmental, real estate, insurance, operations and maintenance, and technical concerns related to the Goldendale Generating Station.

**1. Commercial and Legal Due Diligence**

**Q. Please describe the commercial and legal due diligence conducted by the Company.**

A. The Company and its outside counsel reviewed the various contracts pertaining to the ownership and operation of the Goldendale Generating Station, with a particular focus on identifying potential liabilities and provisions that could be implicated in the acquisition, such as consents, assignments and accrued liabilities, and taking into account the special rules that apply to sales in bankruptcy. These included, for purposes of illustration, interconnection, transportation, operating and maintenance, water supply and similar types of agreements. The Company considered the application of the bankruptcy rules to the treatment of these agreements and the Company's obligations thereunder. In the course of these investigations, PSE discovered that Goldendale Energy

Center LLC (the previous owner of the Goldendale Generating Station) owed significant payments to a variety of business partners. Goldendale Energy Center LLC satisfied these obligations during negotiations with PSE.

**2. Real Estate Due Diligence**

**Q. Please describe the real estate due diligence conducted by the Company.**

A. The real estate due diligence included title review and a survey of the entire site to confirm the site is contiguous, without significant encroachments, and that there were not any additional real property interests needed for the Goldendale Generating Station.

The Goldendale Generating Station is located within the Goldendale Industrial Park in Klickitat County, Washington, on previously undeveloped land. The property consists of four contiguous parcels of land that total 41.65 acres.

Within the borders of, but exclusive of the 41.65 acre plant property, KPUD owns and occupies a 4.04 acre site which is improved with an electrical switchyard.

Easements for ingress and egress, overhead and underground electrical systems in favor of KPUD encumber the property. Additional easements granted to the City of Goldendale for a flood control channel and utility infrastructure, which includes Pacific Telephone and Telegraph for a telephone line and Northwest Pipeline for a 100 foot by 100 foot metering station and related gas delivery pipeline, occupy portions of the plant property.

1 The plant property is bordered on the north and east by industrial zoned lands.  
2 Property to the south is owned by Calpine Corporation and is General Rural  
3 residential zoned vacant land. West of the plant property is rural residential  
4 housing.

5 The property south and adjacent to the Plant Property is a 141.5 acre parcel,  
6 which PSE acquired from Calpine Corporation as part of the Goldendale  
7 acquisition. The north border of the 141.5 acre parcel borders the south property  
8 line of the plant property as noted above as well as other industrial zoned lands.  
9 South, east and west of the 141.5 acre parcel is rural residential and agricultural  
10 property. While vacant of any formal structures, the 141.5 acre property is  
11 occupied with easements for telephone, natural gas pipelines and overhead and  
12 underground electric and transmission and distribution lines. PSE acquired this  
13 adjacent property as part of the transaction. The 141.5 acre property is currently  
14 zoned General Rural (5 acre minimum) and is currently used for agricultural  
15 purposes under a farming lease. PSE expects to continue this lease.

16 **3. Environmental Due Diligence**

17 **Q. Please describe the environmental due diligence conducted by the Company.**

18 A. The environmental due diligence review consisted of a site visit, interviews with  
19 facility employees, review of all available environmental documentation  
20 (including environmental agency correspondence, permit applications, final  
21 permits, environmental plans and policies, etc.) at the plant, review of Department



1 of Ecology files pertaining to the Station and interviews with an Ecology  
2 representative and a Goldendale Fire Department representative by PSE staff  
3 and/or its agents.

4 No significant environmental issues were identified during the environmental due  
5 diligence. The Station appears to be properly sited and constructed and in good  
6 condition. There are comprehensive programs in place to address air emissions,  
7 wastewater discharge, stormwater discharges, solid waste management, hazardous  
8 materials handling and hazardous waste management. Although no sampling was  
9 performed, there is no indication of any groundwater, surface water or noise  
10 issues associated with the Station.

11 **4. Insurance Due Diligence**

12 **Q. Please describe the insurance due diligence conducted by the Company.**

13 A. PSE hired a property insurance engineer for an assessment of the Goldendale  
14 Generating Station. The comments from PSE's property insurance engineer were  
15 generally good and included the following findings: 1) All equipment and systems  
16 are fully commissioned and the installed fire protection systems are at industry  
17 standard or better; 2) the plant management and operators are considered highly  
18 competent; and 3) the water supply for the existing fire protection systems is  
19 excellent.

1 In addition, there are four loss control recommendations requiring action, and any  
2 one of the identified exposures could result in a significant fire loss. The  
3 recommendations include: (i) extending CO2 protection to additional  
4 components of the gas turbine generator; (ii) adding fire protection, oil  
5 containment and drainage piping for the combustion turbine; (iii) upgrading the  
6 fire protection, oil containment, and drainage for the steam turbine; and  
7 (iv) confirming the generator building has a class 1 roof, or installing fire  
8 sprinklers. PSE has included these costs in its assessment and pro forma and  
9 plans to make these improvements.

10 PSE will add the Station to its permanent property insurance program with a  
11 \$1,000,000 deductible and an insured replacement value of \$260 million. PSE  
12 projects a \$10,000 increase in premium by its excess general liability carrier  
13 associated with the new facility.

14 **5. Operations and Maintenance Due Diligence**

15 **Q. Please describe the operations and maintenance due diligence conducted by**  
16 **the Company.**

17 A. The Company reviewed the operating reports, maintenance inspection records,  
18 software being used at the project and conducted site visits to the Station and  
19 found no significant problems.

20 /////

1 PSE developed an Asset Management Plan to transition Calpine employees, all  
2 software and vendor contracts, as well as the operations and maintenance policies  
3 and procedures of the Station. PSE worked with Calpine Operating Services  
4 Company, Inc., a Calpine subsidiary, which operated and maintained the Calpine  
5 Generating Station. Staffing at the Station is similar to the Frederickson I project,  
6 with approximately 19 employees. Staff size is projected to remain constant over  
7 the life of the Station. Nearly all of the personnel at the Station have become PSE  
8 employees.

9 **6. Technical Due Diligence**

10 **Q. Please describe the technical due diligence conducted by the Company.**

11 A. The Goldendale Generating Station is a conventional one-on-one combined cycle  
12 power plant. The plant achieved commercial operation in September 2004 and is  
13 rated at approximately 252 MW base load and approximately 277 MW with duct  
14 firing. A General Electric ("GE") Frame 7FA+e Model 7241 combustion turbine  
15 provides electrical power via a GE generator and exhaust heat to a Babcock-  
16 Hitachi heat recovery steam generator, which is used to generate high,  
17 intermediate, and low pressure steam. Steam generated by the heat recovery  
18 steam generator drives a triple pressure Hitachi steam turbine, similar in design to  
19 a GE AT10 steam turbine but with better vibration characteristics. A Siemens  
20 generator converts the mechanical energy from the steam turbine into electrical  
21 energy.

1 The GE 7FA gas turbine is a mature, well-understood machine with hundreds of  
2 units installed around the world amassing more than five million operating hours.  
3 The availability of parts and service is considered to be excellent with both  
4 original equipment manufacturer and third party after-market support. The plant  
5 does not require fuel gas compression as gas is delivered at sufficient pressure for  
6 use in the combustion turbine. Although supported by a smaller installed base,  
7 the Hitachi steam turbine and Siemens generator are recognized as reliable  
8 equipment.

9 Raw water supply is provided by the City of Goldendale. To reduce the  
10 consumption of water, the plant employs a condensing system that includes a  
11 conventional condenser and an air-cooled condenser operating in parallel. The  
12 manufacturer of this system has five other similar condenser cooling systems in  
13 operation around the world. The level of maintenance for the parallel condensing  
14 system is believed to be minimal.

15 The electrical equipment on-site appears to originate from reputable  
16 manufacturers and be in good operating order. KPUD owns and operates the  
17 substation on the Station site. KPUD ownership begins at the high voltage side of  
18 the generator step-up transformer. The power plant is controlled by a system of  
19 local control panels, local instrumentation, and a central distributed control  
20 system supplied by ABB Bailey.

21 /////

1 In general, the plant has a high level of equipment redundancy, (2 x 100% pumps,  
2 fans, etc.) so the number of spare parts required on site can be minimized.

3 The overall conclusion of PSE's technical due diligence team is that the plant is  
4 clean, quiet, and well-designed. The plant has the latest emission controls that  
5 meet or exceed regulations. Operations and maintenance at the plant appear to  
6 have been carried out by conscientious and experienced personnel guided by good  
7 procedures.

8 **C. Board Approval of the Acquisition**

9 **Q. Was PSE able to finalize contracts for acquisition of the Goldendale**  
10 **Generation Station?**

11 A. Yes. Negotiations with Calpine produced definitive agreements for PSE's  
12 acquisition of the Station. At the November 3, 2006, meeting of PSE's Board of  
13 Directors, PSE management recommended that the Board approve the acquisition  
14 as set forth in the summary documentation to the Board of Directors. *See* Exhibit  
15 No. \_\_\_\_ (EMM-5HC) and Exhibit No. \_\_\_\_ (EMM-6). The Board approved the  
16 recommendation, and PSE executed the necessary agreements and closed on the  
17 transaction on February 21, 2007.

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19 ////

1 **Q. Does the Company's acquisition of the Goldendale Generating Station satisfy**  
2 **the evaluation criteria set out in the Company's RFP?**

3 A. Yes, it does.

4 (i) The Station is compatible with PSE's need. The Station provides  
5 up to 277 MW of winter capacity, has significant operational  
6 flexibility and has the lowest heat rate in PSE's fleet.

7 (ii) The project will minimize PSE's costs. PSE was able to acquire  
8 the Station from a distressed seller and achieve extreme savings  
9 from the costs required to build the Station three years ago. PSE  
10 was also uniquely suited to utilize pipeline capacity and expects to  
11 secure a transmission redirect to PSE's service territory.

12 (iii) The project minimized PSE's risks. Goldendale represented the  
13 lowest risk of any proposal in the Phase II Monte Carlo analysis.  
14 In addition, by purchasing an existing facility, PSE was able to  
15 avoid construction and financing risk.

16 (iv) The project includes public benefits. The Station is the most  
17 efficient gas fired generation available and has NOx and SO<sub>2</sub>  
18 controls to limit emissions.

19 (v) The Project met PSE's strategic and financial needs. By acquiring  
20 100% ownership of the Station, PSE increased its flexibility with  
21 respect to future dispatch of the Station and eliminated costs  
22 associated with providing credit support for a power purchase  
23 agreement and debt that would have been imputed to PSE by  
24 ratings agencies if the transaction had been a power purchase  
25 agreement.

26 **D. Project Acquisition Process**

27 **Q. Please describe the process resulting in PSE's acquisition of the Goldendale**  
28 **Generating Station.**

29 A. PSE and Calpine entered into a non-binding Letter of Intent and Term Sheet,

1 which was executed on August 22, 2006. *See* Exhibit No. \_\_\_\_ (RG-11). This  
2 Letter of Intent and Term Sheet formed the basic terms upon which PSE would be  
3 willing to proceed to negotiate Definitive Agreements, pursuant to which PSE  
4 would act as a “stalking horse” bid for the sale of the Station, as part of Calpine’s  
5 bankruptcy auction process.

6 PSE and Calpine executed the Definitive Agreements on November 3, 2006,  
7 following Board consideration for each of the respective companies and Calpine’s  
8 review of the Definitive Agreements with the Calpine Creditors Committee.  
9 Copies of the Definitive Agreements are provided as Exhibit No. \_\_\_\_ (RG-12).

10 A motion for approval of the bidding procedures with the bankruptcy court was  
11 filed by Calpine on November 14, 2006. *See* Exhibit No. \_\_\_\_ (RG-13). The  
12 bidding procedures established, among other things, the minimum bidding  
13 increments, the qualification of the bidders, and approval of the break-up fee  
14 payable to PSE.

15 The bankruptcy court approved the bidding procedures on December 6, 2006.  
16 *See* Exhibit No. \_\_\_\_ (RG-14). The public auction occurred on February 5, 2007.  
17 *See* Exhibit No. \_\_\_\_ (RG-15) for a transcript of the auction. The court approved  
18 the transaction on February 7, 2007. *See* Exhibit No. \_\_\_\_ (RG-16).

1 **Q. What does it mean to be the “Stalking Horse Bidder” and why did PSE seek**  
2 **to establish itself as such?**

3 A. The Stalking Horse Bidder is the bidder that sets the floor price for an auction.  
4 PSE offered a Stalking Horse Bid of \$100,000,000. By establishing itself as the  
5 Stalking Horse Bidder, PSE was able to negotiate the terms and conditions of the  
6 sale and help shape the bidding procedures and conditions applicable to the  
7 bankruptcy auction. In addition, by being the Stalking Horse Bidder, PSE was  
8 entitled to a “break-up fee” of \$2,500,000 if another qualifying party cast the high  
9 bid at the auction. Likewise, PSE received a credit equal to the “break-up fee” for  
10 all bids the Company submitted in the auction. A “break up fee” essentially  
11 provides an advantage to the stalking horse bidder since it is entitled to “credit”  
12 such fee against its purchase price.

13 **Q. What concessions was PSE able to secure from the seller of the Goldendale**  
14 **Generating Station?**

15 A. Through negotiations, PSE was able to win concessions that included, payment of  
16 only 50% of the Real Estate Excise Tax, (whereas in most bankruptcy sales the  
17 purchaser typically assumes all transaction taxes like this); the allocation to  
18 Calpine of most of the risk of so-called “Cure Costs” under Calpine contracts with  
19 third parties (which essentially need to be paid to assign contracts); and various  
20 contractual provisions in favor of the Company designed to protect the Company  
21 in the event unexpected Cure Costs arose prior to the closing for which it would



1 have been responsible. In addition, PSE negotiated the inclusion of a 141.5 acre  
2 parcel in the acquisition.

3 **Q. Please describe the Company's bidding strategy for the auction.**

4 A. PSE sought to establish a clear guidance from its Board of Directors as to a  
5 maximum bid price, and pursue the purchase of the Goldendale Generating  
6 Station up to this value in the auction. PSE sought to [REDACTED]  
7 [REDACTED] to avoid over bidding. PSE further had a strategy  
8 of [REDACTED]  
9 [REDACTED].

REDACTED  
VERSION

10 **Q. How did the auction proceed?**

11 A. In the bankruptcy auction, PSE, as the Stalking Horse Bidder, submitted the first  
12 bid, which was rounded up to make future bids easy to compute. Another  
13 qualified bidder emerged and submitted a qualifying bid. Several topping bids  
14 were offered, and PSE made counter bids. Ultimately PSE cast the highest bid  
15 [REDACTED]. A transcript of the  
16 auction is presented as Exhibit No. \_\_\_\_ (RG-15). Please see Exhibit  
17 No. \_\_\_\_ (WJE-1HCT) for further details on the calculation of the maximum bid  
18 price.

19 ////

20 ////

1 **Q. Has the Federal Energy Regulatory Commission approved the disposition of**  
2 **the Goldendale Generating Station?**

3 A. Yes, the Federal Energy Regulatory Commission issued its “Order Authorizing  
4 Disposition of Jurisdictional Facilities and Acquisition of Generating Facilities”  
5 on February 1, 2007. *See* Exhibit No. \_\_\_\_ (RG-17).

6 **Q. Have PSE and Goldendale closed the sale of the Goldendale Generating**  
7 **Station?**

8 A. Yes, the transaction closed on February 21, 2007.

9 **E. Project Acquisition Costs**

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10 **Q. Please describe the acquisition costs for the Goldendale Generating Station.**

11 A. The Company’s total purchase price for the Goldendale Generating Station was  
12 \$120,000,000 or approximately \$433 per kW. In addition, there were additional  
13 acquisitions costs as indicated in the following table, which resulted in a total  
14 acquisition cost of \$ [REDACTED]:

Goldendale Generating Station	Project Costs
Facility Purchase Price	\$120,000,000
Real Estate Excise Tax (50%)	\$ [REDACTED]
Facility Improvements	\$ [REDACTED]
Transaction & Due Diligence	\$ [REDACTED]
Property Taxes	\$ [REDACTED]

Goldendale Generating Station	Project Costs
AFUDC	\$ [REDACTED]
<b>Total Project</b>	<b>\$ [REDACTED]<sup>3</sup></b>

**Q. Please describe the line item “Facility Purchase Price.”**

A. The Facility Purchase Price represents the Company’s auction bid price less the “break-up fee.”

**Q. Please describe the line item “Real Estate Excise Tax.”**

A. The Real Estate Excise Tax (“REET”) is a Washington State tax levied on the portion of property classified as “real” in which a controlling interest of the property is transferred. The combined tax rate for Klickitat County and Washington State is 1.53%. The seller will bear 50% of this cost.

**Q. Please describe the line item “Facility Improvements.”**

A. Facility improvements include funds (1) to bring the roof into insurance compliance and provide adequate fire protection, and (2) for a computer maintenance and management system, security upgrades and integration with PSE’s IT infrastructure.

**REDACTED  
VERSION**

<sup>3</sup> PSE is also seeking rate recovery for an estimated \$ [REDACTED] in capitalized parts for a major maintenance overhaul required for Goldendale in 2007. This brings the total estimated plant cost to \$130,952,698, as described in the testimony of John Story. For a description of the major maintenance required for the Goldendale Generating Station and treatment of the related costs, please see Exhibit No. \_\_\_\_ (EMM-5HC) at page 103.

1 **Q. Please describe the line item “Transaction & Due Diligence.”**

2 A. Transaction and due diligence costs are PSE’s internal costs for due diligence and  
3 negotiations, title insurance, third party expert consultants and legal fees  
4 associated with the transaction.

5 I described above the concept of due diligence and the due diligence efforts  
6 undertaken by the Company with respect to the Goldendale Generating Station.

7 The category “Transaction & Due Diligence Costs” reflects (i) the costs paid by  
8 PSE to third parties who assisted in PSE’s due diligence efforts for the Station  
9 and (ii) the legal fees paid to the law firm LeBoeuf, Lamb Greene & McRae,  
10 L.L.P. for negotiating, drafting and documenting the definitive agreements for the  
11 Station.

12 **Q. Please describe the line item “Property Taxes.”**

13 A. In Washington State, property is assessed at the end of each calendar year with  
14 taxes paid in April and October of the following year, in arrears. It is customary  
15 in real estate transactions in Washington for property taxes to be prorated based  
16 on taxes payable in the year of closing. Since PSE utilizes accrual accounting, the  
17 property taxes paid by it subject to the proration as well as that portion of the  
18 property taxes incurred in the current calendar year attributable to the time period  
19 that the Goldendale Generation Station was owned by Goldendale Energy  
20 Center, LLC, that would have been accrued for payment next year are capitalized.

1 **Q. Please describe the line item “AFUDC.”**

2 A. Allowance for funds used during construction (“AFUDC”) is applicable in this  
3 acquisition to all funds expended prior to closing, which include the deposit,  
4 payable into escrow and transaction and due diligence costs.

5 **F. Operations and Maintenance Expenses**

6 **Q. What arrangements has the Company made with respect to ongoing**  
7 **operations and maintenance for the Goldendale Generating Station?**

8 A. PSE will perform all routine operations and maintenance for the Goldendale  
9 Generating Station. During periods of major maintenance, specialists from the  
10 equipment manufacturers will be brought in to perform the work. Major  
11 maintenance overhauls are expected at intervals over the life of the Station, based  
12 on the number of hours the plant operates. The first major maintenance overhaul  
13 is expected to be performed in June of 2007.

14 **Q. What does the Company project its expenses will be for the Goldendale**  
15 **Generating Station during the rate year?**

16 A. Mr. Story’s Exhibit No. \_\_\_\_ (JHS-5) at page 6 shows the costs associated with the  
17 Goldendale Generating Station. Exhibit No. \_\_\_\_ (RG-18) presents a more detailed  
18 proforma of the costs associated with the Goldendale Generating Station.

1     **G.     Power Costs**

2     **Q.     What does the Company project its power costs will be for the Goldendale**  
3     **Generating Station during the rate year?**

4     A.     In the Facility Description section above, I discuss the Goldendale Generating  
5             Station, and the related power transmission, gas transportation arrangements. The  
6             fuel, transmission and transportation costs for the Goldendale Generating Station  
7             during the rate year is forecast to be \$91,279,291, as shown in Exhibit  
8             No. \_\_\_\_ (JHS-5) at page 6. These costs are included in the rate year power costs  
9             discussed in Mr. Mills' testimony.

10                   **IV.     WILD HORSE WIND PROJECT UPDATE**

11    **Q.     What is the current status of the Wild Horse Wind Project?**

12    A.     The Wild Horse Wind Project began commercial operation as scheduled on  
13             December 21, 2006. Remaining minor construction items (punch list items) are  
14             currently being completed and power performance tests are being performed.  
15             These activities are scheduled to be completed in the first quarter of 2007.

16    **Q.     Is the Wild Horse Wind Project on budget?**

17    A.     The project is currently projected to come in under budget by \$6 million, for a  
18             total cost of approximately \$377 million. Exhibit No. \_\_\_\_ (RG-19) summarizes  
19             (i) the budget; (ii) actual amounts as of January 31, 2007; (iii) the forecast to

1 completion; and (iv) the forecast at completion amounts for the project.

2 **Q. How has the Wild Horse Wind Project performed since it was placed into**  
3 **service?**

4 A. Since December 21, 2006, the Wild Horse Wind Project has operated at a  
5 capacity factor of [REDACTED]%, below its projected capacity factor of [REDACTED]% due to  
6 lower winds in the first quarter of 2007.

7 **V. CONCLUSION**

8 **Q. Does that conclude your testimony?**

9 A. Yes, it does.