

**BEFORE THE**  
**WASHINGTON UTILITIES AND TRANSPORTATION COMMISSION**

Amended Petition of	)	
	)	
PUGET SOUND ENERGY, INC.	)	
	)	
	)	Docket No. UE-070725
	)	
For an Order Authorizing the Use of the	)	
Proceeds From the Sale of Renewable	)	
Energy Credits and Carbon Financial	)	
Instruments	)	

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**REDACTED**  
**RESPONSE TESTIMONY OF DONALD W. SCHOENBECK**  
**ON BEHALF OF**  
**THE INDUSTRIAL CUSTOMERS OF NORTHWEST UTILITIES**

**January 28, 2010**

## **I. INTRODUCTION AND SUMMARY**

1   **Q.     PLEASE STATE YOUR NAME AND BUSINESS ADDRESS.**

2   **A.**     My name is Donald W. Schoenbeck. I am a member of Regulatory & Cogeneration  
3           Services (“RCS”), a utility rate and economic consulting firm. My business address is  
4           900 Washington Street, Suite 780, Vancouver, WA 98660.

5   **Q.     PLEASE DESCRIBE YOUR BACKGROUND AND EXPERIENCE.**

6   **A.**     I have been involved in the electric and gas utility industries for over 35 years. For the  
7           majority of this time, I have provided consulting services for large industrial customers  
8           addressing regulatory and contractual matters. I have appeared before the Washington  
9           Utilities and Transportation Commission (the “Commission”) on many occasions since  
10          1982. A further description of my educational background and work experience can be  
11          found in Exhibit No. DWS-2.

12  **Q.     ON WHOSE BEHALF ARE YOU APPEARING IN THIS PROCEEDING?**

13  **A.**     I am testifying on behalf of the Industrial Customers of Northwest Utilities (“ICNU”).  
14          ICNU is a non-profit trade association whose members are large industrial customers  
15          served by electric utilities throughout the Pacific Northwest, including Puget Sound  
16          Energy (“PSE” or the “Company”).

17  **Q.     WHAT TOPICS WILL YOUR TESTIMONY ADDRESS?**

18  **A.**     I will respond to PSE’s proposed use of the net revenue generated from the sale of  
19          renewable energy credits (“RECs”) and other carbon financial instruments (“CFIs”),  
20          including how the net revenue should be flowed back to PSE’s retail customers.

1 **Q. PLEASE BRIEFLY SUMMARIZE YOUR FINDINGS AND RECOMMENDATIONS**  
2 **ADDRESSED IN THIS TESTIMONY.**

3 **A.** Based on historical transactions executed to date, PSE's projected net revenue from the  
4 sale of RECs and CFIs will be about [REDACTED] through August 2015, a substantial  
5 sum. PSE is proposing to use the net revenue to: 1) offset a \$21 million receivable it  
6 continues to carry on its books from the energy crisis of 2000/2001; 2) dedicate up to \$20  
7 million to fund low income programs; and 3) credit the remaining amount to customers.  
8 PSE proposes to distribute \$10 million of existing net revenues to low income programs  
9 and distribute the net revenue received from five REC sales contracts to the three  
10 categories using allocation percentages until the receivable and low income amounts have  
11 been fully funded. Thereafter, all net revenue would be flowed through as a customer  
12 credit.

13 My testimony explains why all of the net revenue should be flowed back to  
14 customers through a separate tariff rider. PSE's claim that the substantial net revenue  
15 amount is attributable or tied to its California receivable claim is wrong, based upon  
16 publically available information. With a rate stabilization program in place during the  
17 energy crisis period, PSE's wholesale activity was solely for the benefit or detriment of  
18 its shareholders. As a result, PSE's current shareholders should not now receive a  
19 windfall profit from the REC sales. The net revenues should be returned to all the  
20 customers who paid for the renewable resources that generated the RECs and CFIs, and  
21 net revenues should not be paid to shareholders or to fund low income programs. The net  
22 revenues should be distributed to the various customer classes in the same manner the  
23 costs of the facilities providing the revenue has been assigned. In other words, the

1 Company's peak credit classification and allocation factors for production-related costs  
2 should be used to assign the net revenue credit to each class. If the Commission  
3 determines that a portion of the net revenue should be set aside to fund low income  
4 programs, then the monies should come from the amount credited to the residential  
5 customer class. ICNU recommends that a separate tariff rider should be used to track net  
6 revenues and assign a credit to each class.

## **II. PSE NET REVENUE PROJECTION**

7 **Q. PLEASE EXPLAIN AND DESCRIBE THE SOURCES OF THE SUBSTANTIAL**  
8 **PROJECTED NET REVENUES.**

9 **A.** Since August 2007, PSE has been selling RECs to various entities, as shown by PSE's  
10 response to Public Counsel Data Request ("DR") 30, attached to this testimony as Exhibit  
11 DWS-3HC. In total, this exhibit indicates net proceeds through November 2009 of [REDACTED]  
12 [REDACTED] attributable to these sales. PSE's response to Public Counsel DR 31, attached to  
13 this testimony as exhibit DWS-4C, shows the proceeds from CFI sales. From March  
14 2009, through November 2009, the net proceeds from these transactions were [REDACTED].  
15 Finally, since December 2008, PSE has executed five REC sales contracts, which account  
16 for most of the net revenue projection. PSE has executed three contracts with Southern  
17 California Edison Company ("SCE"), one contract with Pacific Gas and Electric  
18 Company ("PG&E"), and one contract with Shell Energy North America ("Shell").  
19 PSE's response to Public Counsel DR 37, attached to this testimony as Exhibit DWS-  
20 5HC, shows the projected revenue from these five agreements. In aggregate, these  
21 transactions provide for deliveries of power from September 2009, through August 2015,  
22 with a projected net value of [REDACTED].

1 **Q. ARE THE AMOUNTS SHOWN IN THESE THREE DATA RESPONSES**  
2 **ADDITIVE?**

3 **A.** No. A substantial portion of the net revenue included in Exhibit DWS-3HC ([REDACTED])  
4 ([REDACTED]) is associated with two of the REC sales contracts set forth in Exhibit DWS-5HC.  
5 Eliminating this “double counting” results in a projected net revenue amount of about  
6 [REDACTED].

7 **Q. AS MOST OF THE PROJECTED NET REVENUE IS ASSOCIATED WITH THE**  
8 **FIVE CONTRACTS EXTENDING THROUGH 2015, HOW LIKELY IS IT THAT**  
9 **PSE WILL ACTUALLY REALIZE THESE REVENUES?**

10 **A.** It is highly likely PSE will realize revenue close to this estimate. The pricing under all  
11 five contracts is based [REDACTED] Three of the contracts  
12 also specify a fixed amount of energy to be delivered under the agreement. These  
13 contracts are the agreement executed with SCE, effective December 31, 2008 (“SCE1”),  
14 the contract, dated April 16, 2009 with PG&E, and the second SCE contract, effective  
15 May 28, 2009 (“SCE2”). The contract with Shell has a limited term calling for deliveries  
16 from [REDACTED] Accordingly, the associated energy  
17 deliveries and margin revenue will be realized and known by the conclusion of this  
18 proceeding for the Shell contract. The third contract with SCE (“SCE3”) requires the  
19 exclusive sale of PSE’s portion of the Klondike III wind resource to SCE. The projected  
20 deliveries under this contract are [REDACTED]. Consequently,  
21 only under this last contract (SCE3) are the energy deliveries uncertain and dependent  
22 upon the actual amount of power that will be produced from this resource. The following  
23 table presents the required or projected energy deliveries, associated margin and resulting  
24 net revenue for each of these five agreements.

### Summary of Energy Agreements

Contract	Energy (GWhs)	Margin (\$/MWh)	Margin Revenue (Millions)
SCE1	2,000	████	████
PG&E	1,000	████	████
SCE2	2,560	████	████
Subtotal:	5,560		████
SCE3	████	████	████
Shell	████	████	████
Total:	████		████

As shown by the table, the three fixed energy contracts account for █████% of the projected energy deliveries and █████% of the net revenue from all five agreements. Taking the bundle of contracts together, PSE should realize an amount of revenue relatively close to the estimate shown in the above table.

### **III. PSE PROPOSED DISTRIBUTION OF NET REVENUE**

#### **Q. HOW IS PSE PROPOSING TO USE THESE PROCEEDS?**

**A.** The Company is proposing to allocate the net funds into three categories. First, the Company proposes that \$21.1 million be used to offset the receivable it has maintained on its books since the California energy crisis of 2000 and 2001. Second, the Company is proposing that up to \$20 million be used for low income programs and that all remaining monies go to ratepayers. More specifically, the Company is proposing that the existing net revenue associated with the CFIs and historic non-contract REC sales go toward the first \$10 million of support for the low income programs. Then, the remaining net revenue from the five contracts would be distributed as the revenue is realized with 40% going to the receivable obligation until the \$21 million amount is offset, 20% to low

1 income until the \$20 million ceiling level is achieved and 40% going to ratepayers. The  
2 likely result from this proposal is that the \$20 million low income distribution will be  
3 fully funded by [REDACTED]. PSE will have received the full \$21.1 million receivable  
4 amount by [REDACTED], but ratepayers will not receive all their credits until [REDACTED]  
5 [REDACTED]. The following table compares the expected net revenue distribution with the net  
6 present value for each category as of August 2010 and using a 10% discount rate. The  
7 table shows that on a net present value (“NPV”) basis, PSE’s “front end loaded” funding  
8 of the receivable and low income categories essentially penalizes ratepayers versus the  
9 other two categories. In order to equitably share the NPV loss from the extended  
10 contractual arrangements, the percentages should be 8.5% for the receivable and low  
11 income categories and 83% for the ratepayer category applied to all net revenue.

Net Revenue Comparison

Category	Net Revenue (Millions)	NPV (Millions)	Difference (Millions)
Receivable	\$21.1	\$21.1	\$0.0
Low Income	\$20.0	\$20.0	\$0.0
Ratepayers	[REDACTED]	[REDACTED]	[REDACTED]
Total:	[REDACTED]	[REDACTED]	[REDACTED]

12 **Q. PLEASE EXPLAIN HOW PSE INTENDS TO CREDIT THE REMAINING**  
13 **AMOUNT TO CUSTOMERS?**

14 **A.** PSE is not proposing a specific methodology to credit the remaining net revenues to  
15 customers. In response to Public Counsel DR No. 20, PSE stated that it “has not made a  
16 proposal as to how the underlying tariff would credit customers.” DWS-19 at 1.

1 **IV. ICNU RECOMMENDATIONS**

2 **Q. DOES ICNU SUPPORT PSE'S PROPOSED DISTRIBUTION OF THE**  
3 **PROJECTED NET REVENUES?**

4 **A.** No. ICNU recommends that all of the net revenue should be flowed back to PSE's  
5 ratepayers, who have paid the cost of the renewable resources that generate the RECs and  
6 CFIs.

7 **Q. WHY DO YOU DISAGREE WITH THE COMPANY'S PROPOSAL TO USE A**  
8 **PORTION OF THE MONIES TO OFFSET THE CALIFORNIA RECEIVABLE?**

9 **A.** PSE alleges the sales contracts and the associated prices would not have occurred but for  
10 its claim of \$21.1 million from various California entities including SCE and PG&E.  
11 This assertion reflects a poor understanding of the California REC requirements and the  
12 associated market. Several years ago, California legislation was enacted requiring all  
13 California load serving entities ("LSEs") to use renewable resources to meet 20% of their  
14 sales by 2010 and arguably 33% by 2020. As there were not enough existing renewable  
15 resources to satisfy this requirement, LSEs (including SCE and PG&E) have been  
16 conducting numerous bid solicitations and entering in to bilateral contracts to achieve the  
17 2010 requirement and to avoid the \$50/MWh shareholder penalty for non-compliance.  
18 With each renewable contract execution, entities regulated by the California Public  
19 Utilities Commission ("CPUC") must submit the contract for approval in an "advice  
20 letter filing." The CPUC will then issue a "resolution" either approving or denying the  
21 advice letter.

22 Attached to this testimony as Exhibits DWS-6, DWS-7, DWS-8, DWS-9, DWS-  
23 10 and DWS-11 are portions of the advice letter filings made to date with regard to four  
24 of the five contacts. Exhibits DWS-7 and DWS-8 are portions of the advice letter filings



1 associated with the SCE1 agreement. Exhibits DWS-9 and DWS-10 are portions of the  
2 advice letter filings for the SCE2 agreement. Exhibit DWS-11 is a part of the advice  
3 letter filing for the SCE3 agreement, and Exhibit DWS-6 is the advice letter filing for the  
4 PG&E agreement. While all these agreements are the results of bilateral contracting by  
5 the California entities, each advice letter filing explains how the associated price is  
6 comparable to the prices for contracts entered into as a result of the utility solicitations.  
7 Of particular relevance to this instant docket is Exhibit DWS-8. This supplemental  
8 advice letter filing by SCE addresses the Federal Energy Regulatory Commission  
9 settlement agreement and the release of claims by the associated parties. In particular, it  
10 includes the following sentences:

11 The Puget Contract's pricing is not dependent on the Settlement  
12 Agreement and SCE would have chosen to enter into the Puget  
13 Contract independent of the Settlement Agreement. The Puget  
14 Contract should be evaluated on its own merits as a market  
15 transaction for the purchase of renewable energy, irrespective of  
16 the Settlement Agreement.

17 **Q. DID THE CPUC APPROVE THIS AGREEMENT?**

18 **A.** Yes. The CPUC approved the SCE1 contract on June 18, 2009, with the issuance of  
19 Resolution E-4244. The resolution (without the attachments) is attached to this testimony  
20 as Exhibit DWS-13. The discussion regarding the contract price is on page 17 of the  
21 resolution. It states that the contract price is reasonable as compared to the shortlisted  
22 resources from the 2008 solicitation for the same period of deliveries.

23 **Q. HAS THE CPUC ISSUED OTHER RESOLUTIONS REGARDING PSE**  
24 **CONTRACTS?**

25 **A.** Yes. Resolutions E-4278 issued on October 15, 2009, and E-4300 issued on December  
26 17, 2009, approved the PG&E and SCE3 agreements. Portions of these documents are

1 provided as Exhibits DWS-14 and DWS-12. Both resolutions note the contract price is  
2 reasonable as compared to the respective utility's 2008 renewable solicitation.  
3 Consequently, based on publically available information, the prices under these  
4 agreements are not due to PSE's California receivable claim, but rather the supply and  
5 demand factors facing LSEs in California to achieve the state mandated renewable energy  
6 procurement levels.

7 **Q. IS PSE'S SITUATION UNIQUE?**

8 **A.** No. SCE made similar filings with the CPUC with regard to a PacifiCorp Renewable  
9 Portfolio Standard contract in July 2009. These were not attributable to the litigation  
10 regarding the power crisis of 2000-01, because PacifiCorp had settled with the California  
11 parties in June 2007. Exhibit Nos. DWS-16, DWS-17 and DWS-18.

12 **Q. WHY HASN'T THE CPUC ISSUED A RESOLUTION WITH REGARD TO THE**  
13 **SCE2 CONTRACT?**

14 **A.** I believe it simply has to do with the tasks or workload of the Energy Division of the  
15 CPUC. Deliveries under the SCE2 agreement do not commence until 2012, and SCE  
16 filed a relatively recent supplement to the original advice letter regarding this contract.  
17 So, there is still a good deal of time between now and when this contract needs to be  
18 approved.

19 **Q. ARE THERE ANY OTHER REASONS WHY PSE'S SHAREHOLDERS SHOULD**  
20 **NOT BE GIVEN A PORTION OF THE NET REVENUE PROCEEDS?**

21 **A.** Yes. Pursuant to the Commission order approving the merger of Washington Natural  
22 Gas Company and Puget Sound Power & Light Company, a five year rate stabilization  
23 plan was in place from January 1, 1998, through December 31, 2001. The rate plan set  
24 forth the specific rate adjustments that were allowed each year. Also during this time,

1 there was no rate mechanism to adjust for or track changes in power related costs, such as  
2 power cost adjustment mechanism that PSE has in place today. Accordingly, PSE  
3 wholesale activities during the energy crisis were solely for the benefit or detriment of its  
4 shareholders. The receivable that PSE carries on its books was created during this time  
5 period in which PSE's activities benefited shareholders. With this being the case, there is  
6 absolutely no justification for now allowing PSE's current shareholders to benefit from  
7 the net revenues from the REC sales, nor is there any justification for ratepayers to  
8 compensate shareholders for activities during this period. Also, during the many years  
9 when PSE was pursuing the various California energy crisis litigations, the associated  
10 costs for outside legal and consulting services was borne by the ratepayers. See Exhibit  
11 DWS-15. To my knowledge, none of this effort was paid for by PSE's shareholders. In  
12 addition, there is no relationship between the net revenues associated with renewable  
13 energy projects and PSE's wholesale activities in 2000-2001. Finally, even if PSE  
14 shareholders were entitled to a portion of the REC net revenues, PSE has not presented  
15 any evidence demonstrating that the Company should be entitled to \$21.1 million. For all  
16 these reasons, PSE's ratepayers should receive all of the net revenue benefit.

17 **Q. WHY DON'T YOU SUPPORT USING A PORTION OF THE FUNDS TO**  
18 **SUPPLY ADDITIONAL LOW INCOME ACTIVITY?**

19 **A.** The net revenues from the REC sales are the result of all non-direct access customers  
20 contributing to the costs associated with the renewable generation resources based on  
21 PSE's cost of service studies. No customer class should receive preferable allocation of  
22 the benefits of the REC sales. There is no reason to treat REC revenues different from  
23 any other utility revenue which is used to offset utility costs and lower rates for all

1 customers. The Commission should continue its current policy of addressing low income  
2 credits and funding in general rate proceedings.

3 **Q. WHAT DO YOU RECOMMEND IF THE COMMISSION DECIDES TO**  
4 **SPECIFICALLY ALLOCATE A PORTION OF THE REC NET REVENUES TO**  
5 **LOW INCOME CUSTOMERS?**

6 **A.** I have always advocated that such programs should be borne by the primary beneficiaries  
7 of the program under a “cost follows benefit” approach. As the direct beneficiaries of  
8 these program commitments are the residential class, any monies earmarked for  
9 increasing low income program funding should come from the net benefit assigned to the  
10 residential class.

**V. CREDITING THE NET REVENUE TO RATEPAYER CLASSES**

11 **Q. HOW SHOULD THE NET REVENUE BE ALLOCATED TO EACH CUSTOMER**  
12 **CLASS?**

13 **A.** The net revenue should be allocated in the same manner in which the costs of the  
14 resources from which the sales are attributable is done in PSE’s cost-of-service study. As  
15 these are generating resources, PSE’s peak credit classification and allocation percentage  
16 should be used to assign the net revenue to each class. Based on PSE’s cost-of-service  
17 study filed in docket UE-090704, the following table shows the class percentages  
18 resulting from this recommendation.

Recommended Net Revenue Allocation	
Class	Peak Credit Percentage
Residential Sch 7	53.31%
Sch 24 (kW < 50)	12.11%
Sch 25 (kW > 50 & < 350)	13.81%
Sch 26 (kW > 350)	9.25%
Sch 31 (General Service)	5.47%
Sch 35 (Irrigation)	0.02%
Sch 43 (Interruptible)	0.58%
Campus Sch 40	2.80%
Sch 46 & 49	2.25%
Sch 449 Primary	0.00%
Sch 449 HV	0.00%
St Lighting	0.37%
Special Contract	0.00%
Firm Resale (Small)	0.03%

The calculation in the above table assumes the firm resale class has a contractual arrangement under which it is entitled to a portion of the net revenue benefit. If this is not the case, the net benefit should only be assigned to the applicable retail customers.

**Q. DOES ICNU HAVE A RECOMMENDATION ON HOW THE NET REVENUE SHOULD BE FLOWED BACK TO EACH CUSTOMER?**

**A.** Yes. ICNU recommends that a separate tariff be established setting forth class specific kilowatthour credits. By returning the revenues in this manner, all parties will be able to readily check or audit the crediting of the net revenues to ratepayers.

**Q. DOES THIS CONCLUDE YOUR DIRECT TESTIMONY?**

**A.** Yes, it does.