

**EXH. ZCY-5CT
DOCKETS UE-240004/UG-240005 et al.
2024 PSE GENERAL RATE CASE
WITNESS: ZACARIAS C. YANEZ**

**BEFORE THE
WASHINGTON UTILITIES AND TRANSPORTATION COMMISSION**

**WASHINGTON UTILITIES AND
TRANSPORTATION COMMISSION,**

Complainant,

v.

PUGET SOUND ENERGY,

Respondent.

**Docket UE-240004
Docket UG-240005
(consolidated)**

In the Matter of the Petition of

PUGET SOUND ENERGY

**For an Accounting Order Authorizing
deferred accounting treatment of
purchased power agreement expenses
pursuant to RCW 80.28.410**

**Docket UE 230810
(consolidated)**

PREFILED REBUTTAL TESTIMONY (CONFIDENTIAL) OF

ZACARIAS C. YANEZ

ON BEHALF OF PUGET SOUND ENERGY

REDACTED VERSION

SEPTEMBER 18, 2024

PUGET SOUND ENERGY

**PREFILED REBUTTAL TESTIMONY (CONFIDENTIAL) OF
ZACARIAS C. YANEZ**

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1 **PUGET SOUND ENERGY**

2 **PREFILED REBUTTAL TESTIMONY (CONFIDENTIAL) OF**
3 **ZACARIAS C. YANEZ**

4 **I. INTRODUCTION**

5 **Q. Are you the same Zacarias C. Yanez who submitted Prefiled Direct**
6 **Testimony on February 15, 2024 on behalf of Puget Sound Energy (“PSE”)**
7 **in this proceeding?**

8 A. Yes, on February 15, 2024, I filed the Prefiled Direct Testimony of Zacarias C.
9 Yanez, Exhibit ZCY-1CT, and three supporting exhibits (Exh. ZCY-2 through
10 Exh. ZCY-4C).

11 **Q. What is the purpose of your rebuttal testimony?**

12 A. My rebuttal testimony responds to the Response Testimony of John D. Wilson,
13 Exh. JDW-1CT, witness for Commission Staff who recommends that the
14 Commission find PSE’s execution of the power sales agreement with Chelan
15 PUD (the “Chelan PSA”) was imprudent or in the alternative, impose a so-call
16 guardrail on allowable production costs.

17 **Q. Please summarize your rebuttal testimony.**

18 A. My rebuttal testimony explains that the Chelan PSA contract does not include
19 nonstandard terms and conditions and Wilson’s concerns regarding the terms of
20 the contract are rooted in a lack of familiarity with commonly structured power

1 purchase agreements in the Pacific Northwest. Therefore, PSE’s execution of the
2 Chelan PSA was prudent and there is no need for a guardrail on allowable
3 production costs. More specifically, this rebuttal testimony: 1) provides a brief
4 discussion of the Chelan PSA; 2) explains that the Commission has previously
5 approved the contract provisions Wilson finds objectionable; and 3) provides an
6 analysis that demonstrates the benefits provided to PSE customers by the Chelan
7 PSA outweigh the risks alleged by Wilson.

8 **II. THE CHELAN PUD POWER SALES AGREEMENT**

9 **Q. Please summarize Wilson’s testimony regarding the Chelan PSA.**

10 A. Wilson states that he “confirmed the market data” PSE used in its evaluation of
11 the Chelan PSA and he finds the benchmarks PSE used to “support the levelized
12 pricing [are] reasonable.”¹ Wilson also agrees that “PSE has a capacity need for
13 the relevant time period and that the Chelan PSA contributes toward meeting that
14 need.”² Although Wilson finds “PSE’s price forecast for the Chelan PSA is
15 reasonable,” he believes certain “contract terms in the Chelan PSA place
16 customers at risk of large and unreasonable cost increases.”³ Wilson recommends
17 that the Commission require PSE to file a special request to re-evaluate the

¹ Wilson, Exh. JDW-1T at 49:2-4.

² Wilson, Exh. JDW-1T at 49:4-5.

³ Wilson, Exh. JDW-1T at 49:6-7.

1 prudency of the Chelan PSA if production costs exceed the forecast by
2 \$ [REDACTED] million.⁴

3 **Q. Please describe the Chelan PSA.**

4 A. The Chelan PSA is a 20-year power sales agreement with the Public Utility
5 District No. 1 of Chelan County (“Chelan PUD”) for a 25 percent share of the
6 output of the Rocky Reach and the Rock Island Hydroelectric Projects (the
7 “Projects”) that effectively renews and extends a 2006 power sales agreement
8 with Chelan PUD (“2006 Chelan PSA”) that expires in October 2031.⁵ The
9 Projects are currently used by Chelan PUD to serve its local load; Chelan PUD
10 sells surplus energy from the Projects to third parties under existing power
11 purchase agreements, including the 2006 Chelan PSA.⁶

12 **Q. Please describe the pricing provisions in the Chelan PSA.**

13 A. As explained in my Prefiled Direct Testimony, Exh. ZCY-1CT, PSE’s price under
14 the Chelan PSA includes two parts: an annual fixed cost premium and PSE pays a
15 25 percent share of the costs of operating the Projects. These pricing provisions
16 are similar to the pricing provisions in the 2006 Chelan PSA except that the 2006
17 Chelan PSA had a one-time adder rather than a fixed annual payment and minor
18 differences such as changes in Chelan PUD’s credit requirements, changes in

⁴ Wilson, Exh. JDW-1T at 7:16-19.

⁵ Yanez, Exh. ZCY-1CT at 2:5-10.

⁶ Yanez, Exh. ZCY-1CT at 4:17-19.

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1 transmission terms, and operating practices reflecting physical limits at the
2 projects.⁷

3 **Q. Please describe the pricing provision in the Chelan PSA that Wilson finds**
4 **objectionable.**

5 A. Wilson objects to PSE paying a percentage share of the costs of operating the
6 Projects equal to its 25 percent share of the Projects' output with no cap on costs.
7 Wilson claims, among other things, it is unreasonable to assume Chelan PUD will
8 act prudently and not make excessive investments in the Projects because: the
9 primary restraint on uneconomic investments is Chelan PUD's retail customers'
10 exposure to those costs; he has significant concerns about unforeseen relicensing
11 or civil works costs; Chelan PUD might make uneconomic investments in the
12 Projects to avoid retiring one of the Projects and reducing PSE's fixed annual
13 charge; and he has never seen a contract without a cap on capital expenses.⁸

⁷ Yanez, Exh. ZCY-1CT at 5:15-17 and 6:16 to 7:2.

⁸ Wilson, Exh. JDW-1TC at 49:16 to 51:10.

1 **A. It is Reasonable to Expect Chelan PUD to Act Prudently and Not Make**
2 **Excessive Investments in the Projects.**

3 **Q. How do you respond to Wilson’s concerns about PSE paying a percentage**
4 **share of the costs of operating the Projects equal to its 25 percent share of the**
5 **Projects’ output with no cap on costs.**

6 A. As stated in my Prefiled Direct Testimony, the Chelan PSA is modeled after the
7 2006 Chelan PSA and the contracts share identical terms pertaining to net costs
8 with no cap on capital expenses.⁹ PSE sought approval of the 2006 Chelan PSA in
9 Docket UE-060266. In its testimony in Docket UE-060266,¹⁰ PSE explained the
10 pricing provisions in the 2006 Chelan PSA and referred to PSE’s payment
11 obligation as “take or pay” and stated that the 2006 Chelan PSA was “cost-based
12 and provides the District with additional flexibility related to funding for future
13 capital expenditures...”¹¹ PSE also explained in its testimony in Docket UE-
14 060266 that Chelan PUD had stated in the negotiations of the 2006 Chelan PSA
15 that PSE’s contract would represent the first new long-term contract for Chelan’s
16 system output and, as such, would serve as a model for negotiations with other
17 prospective purchasers.¹² In Docket UE-060266, the Commission stated that
18 “PSE’s direct case includes substantial competent evidence showing the need and
19 appropriateness of the Company’s expenditures” for the 2006 Chelan PSA; the

⁹ Yanez, XCY-1CT at 6:14 to 7:2.

¹⁰ See Docket No. UE-060266, Prefiled Direct Testimony of Joel C. Molander, Exh. JCM-1HCT, at 2-17 (Feb. 15, 2006).

¹¹ Id. at 8; see also, 6:11-12, where Mr. Molander referred to Chelan PUD (the District) charging PSE under its “pay-as-you-go” capital financing program.

¹² See Docket No. UE-060266, Prefiled Direct Testimony of Joel C. Molander, Exh. JCM-1HCT, at 4:1-4 (Feb. 15, 2006).

1 Commission therefore found PSE’s acquisition of the 2006 Chelan PSA prudent
2 and that the associated costs were reasonable for recovery in rates.¹³ The
3 Commission should make the same findings regarding the Chelan PSA in this rate
4 case. Although Wilson may not have “seen a contract without a cap on expenses,”
5 the 2006 Chelan PSA has been in effect for eighteen years and has provided
6 benefits to PSE at reasonable cost without Chelan PUD attempting to incur
7 unnecessary and excessive costs that, as described below would be detrimental to
8 its customers, and PSE believes it is unlikely Chelan PUD has any incentives to
9 do so now. Notably, Wilson’s reference to the cost overruns for nuclear plant
10 Vogtle is inapposite. His testimony concedes the utility company was a minority
11 owner in the project, not an arm’s length power purchaser.¹⁴

12 **Q. How do you respond to Wilson’s claim that Chelan PUD exposing its**
13 **customers to increased rates does not restrain Chelan PUD from making**
14 **excessive investments in the Projects?**

15 A. I disagree with Wilson. It is my understanding that Chelan PUD is a customer-
16 owned public utility district that takes pride in having some of the lowest electric
17 rates in the nation.¹⁵ I also understand that the governing body of Chelan PUD is a
18 five-member elected board that has responsibility to approve the plans, budgets,

¹³ *Washington Utilities and Transportation Commission vs. Puget Sound Energy*, Docket UE-060266 Order 08 at ¶ 165 (Jan. 5, 2007) (“Order 08”)(the 2006 Chelan PSA was 1 of 5 resource acquisitions at issue and 1 of 2 long-term power purchase agreements the Commission approved in Order 08).

¹⁴ Wilson, Exh. JDW-1T at 51:13-15.

¹⁵ [Our Strategic Plan \(chelanpud.org\)](https://www.chelanpud.org), last visited September 13, 2024.

1 and expenditures of Chelan PUD.¹⁶ I find it highly unlikely that the Chelan PUD
2 board would approve making excessive unneeded investments in the Projects
3 since the Chelan PUD customers are responsible for 65 percent of the operating
4 and capital costs of the Projects. Approving excessive unneeded investments in
5 the Projects would almost certainly increase the rates for Chelan PUD customers
6 and risk putting those customers' historically low rates at issue; and it would
7 likely put every board member at risk of losing its elected board seat.

8 **Q. How do you respond to Wilson's concern about Chelan PUD incurring**
9 **unforeseen relicensing or civil works costs at the Projects?**

10 A. First, I would note that Wilson offers no support for, nor explanation regarding,
11 why he has this concern about unforeseen costs. Second, I believe this
12 unsupported concern is unfounded based on PSE's extensive history, knowledge
13 of, and experience with Chelan PUD's operation of the Projects, as well as the
14 due diligence PSE conducted prior to executing both the Chelan PSA and the
15 2006 Chelan PSA, as is more fully described in my Prefiled Direct Testimony.¹⁷
16 In addition, given that Chelan PUD's customers would be responsible for 65
17 percent of such costs, Chelan PUD has a vested interest in responsibly managing
18 the Projects' costs.

¹⁶ [Our Commissioners \(chelanpud.org\)](http://OurCommissioners(chelanpud.org)), last visited 13, 2024.

¹⁷ Yanez, Exh. ZCY-1CT at 14:3-22; information on the licensing process and cost estimates is in Exh. ZCY-3HC.

1 **B. Chelan PUD is Not Incentivized to Make Excessive Investments to Avoid**
2 **Retiring the Projects.**

3 **Q. Do you agree with Wilson's claim that Chelan PUD might be incentivized to**
4 **make excessive uneconomic investments to avoid retiring the Projects?¹⁸**

5 A. No. As stated earlier, the Chelan PUD customers are responsible for 65 percent of
6 the operating and capital costs of the Projects while PSE's customers are
7 responsible for 25 percent of those costs. It would not be economically reasonable
8 for Chelan PUD to make excessive investments in the Projects since its retail
9 customers would be responsible for 65 percent of any excessive or uneconomic
10 costs.

11 **Q. Please describe the hypothetical maximum Chelan PUD cost increase**
12 **scenario presented by Wilson.**

13 A. Wilson provides a hypothetical scenario that he claims shows Chelan PUD would
14 be willing to bear a [REDACTED] percent increase in annual production costs before it
15 would decide to retire the Projects.¹⁹ Wilson claims his hypothetical scenario is
16 based on an assumption that Chelan PUD would be willing to invest in the
17 Projects up to the point at which its costs equal its benefits.²⁰

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¹⁸ Wilson, Exhibit JDW-1T at 50:17-51:4.

¹⁹ Wilson, Exh. JDW-1T at 3:3-4, see also, Exh. JDW-1T, Table 3 at 4:1-2.

²⁰ Id. at 3:10-11.

1 **Q. How do you respond to Wilson’s hypothetical scenario?**

2 A. Wilson is comparing a one-year cost increase Chelan PUD would be
3 hypothetically inceded to incur for the Projects in 2032 to the annual production
4 costs of the Projects in 2032. In response to a data request, Wilson confirmed the
5 hypothetical cost increase shown in Table 3 of Exh. JDW-1T corresponds to a
6 total cost increase of [REDACTED] in 2032 dollars. However, the correct analysis
7 is to compare the present value of the \$ [REDACTED] million hypothetical cost increase of
8 the Projects to the present value of the benefits of the Projects.

9 **Q. What are the customer benefits relative to the available alternatives as**
10 **estimated by PSE?**

11 A. The Chelan PSA is essentially a “cost plus” contract for PSE’s customers under
12 which PSE will pay a 25 percent share of the net cost to operate the Projects, plus
13 a fixed price adder. This means that for a modest fixed price adder, PSE
14 customers benefit from the low cost of production at the existing hydroelectric
15 Projects. As illustrated in Table 1 of Exh. ZCY-1CT, and based on analysis at the
16 time of acquisition, PSE expects the Chelan PSA to have a net present value
17 (“NPV”) of approximately \$ [REDACTED] million (\$ [REDACTED]/MWh levelized) as compared to
18 resource alternatives having an NPV between \$ [REDACTED] million and \$ [REDACTED] million
19 (\$ [REDACTED]/MWh to \$ [REDACTED]/MWh). This range translates to PSE customer benefits

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1 between \$173 million and \$969 million from the Chelan PSA compared to the
2 resource alternatives.

3 **Q. Please explain how the cost increase of the Projects hypothesized by Wilson**
4 **would compare to the benefits provided by the Projects to PSE?**

5 A, The starting point in this comparison is to discount the \$ [REDACTED] million in 2032
6 dollars to 2022 dollars using the same discount rate PSE used to discount the
7 benefits presented in PSE's analysis. This would result in a 2022 cost value of
8 \$ [REDACTED] million. PSE's expected benefits would be based on its 25 percent share of
9 the costs of the Projects, a 25 percent share of \$ [REDACTED] million is \$ [REDACTED] million. This
10 hypothetical scenario would result in the net benefits to PSE being lowered from a
11 range between \$ [REDACTED] million and \$ [REDACTED] million to a range of \$ [REDACTED] million to
12 \$ [REDACTED] million.

13 **Q. Does the Chelan PSA incentivize Chelan PUD to incur excessive unnecessary**
14 **costs for the Projects?**

15 A. No. In the hypothetical scenario presented by Wilson, Chelan PUD customers are
16 currently forecasted to incur \$ [REDACTED] million of costs for the Projects annually.
17 Wilson's hypothetical scenario would increase the annual costs to Chelan
18 customers to \$ [REDACTED] million an increase of [REDACTED] percent.²¹ As stated before, Chelan

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²¹ See Exh. JDW-1T, Table 3 line 6 at 53:1-2.

1 PUD is incented to minimize cost increases to its own customers. Wilson's
2 hypothetical scenario might show a zero net benefit (cost) for Chelan PUD
3 customers, but it would result in a [REDACTED] percent increase in Project costs to be paid
4 by those customers which would certainly result in a rate increase. Chelan PUD,
5 acting as a prudent utility, would carefully evaluate resource alternatives before
6 making a financial commitment of that magnitude.

7 **Q. Does Wilson's hypothetical scenario reflect a reasonable analysis?**

8 A. No. It does not appear that Wilson's hypothetical scenario considered reasonable
9 alternatives. Rather, Wilson's analysis is focused on comparing hypothetical costs
10 to the [REDACTED]
11 [REDACTED] not on a comparative resource analysis such as that used by PSE
12 when it is evaluating a potential resource acquisition. For example, if Chelan PUD
13 could replace the power (energy and non-energy attributes including capacity and
14 environmental attributes) with other resources at a lower cost than \$ [REDACTED] million,
15 it would not choose to invest \$ [REDACTED] million in the Projects. As described above,
16 PSE performed a detailed comparative analysis that identified benefits between
17 \$173 million and \$969 million to PSE customers relative to replacing the output
18 of the Projects with other resources. The Commission should reject Wilson's
19 hypothetical scenario.

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1 **Q. Would it be appropriate to evaluate the Chelan PSA as if it were a power**
2 **market hedge?**

3 A. No. Wilson concedes in his testimony that the Chelan PSA is a physical
4 transaction and not a financial hedge.²² Evaluating the Chelan PSA as if it were a
5 power market hedge is unreasonable and inappropriate.

6 **III. CONCLUSION**

7 **Q. Does the Chelan PSA appropriately balance risk between Chelan PUD and**
8 **PSE and its customers?**

9 A. Yes. As shown in my Prefiled Direct Testimony, PSE's analyses, negotiation, and
10 execution of the Chelan PSA meet the specific factors the Commission reviews in
11 making a prudency determination.²³ As described above, Wilson's testimony that
12 the pricing provisions in the Chelan PSA expose PSE customers to excessive risk
13 unfounded and there is no need to impose guardrails on allowable production
14 costs of the Projects.

15 **Does that conclude your prefiled rebuttal testimony?**

16 A. Yes, it does.

²² Wilson, Exh. JDW-1T at 54:1-5.

²³ Yanez, Exh. ZCY-1CT at 7-20.