EXHIBIT NO. JHS-1T
DOCKET NO. UE-10____
PCA 8 COMPLIANCE
WITNESS: JOHN H. STORY

BEFORE THE
WASHINGTON UTILITIES AND TRANSPORTATION COMMISSION

In the Matter of the Petition of **PUGET SOUND ENERGY, INC.** **For Approval of its March 2010 Power Cost Adjustment Mechanism Report**	**Docket No. UE-10____**

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

MARCH 31, 2010

PUGET SOUND ENERGY, INC.

PREFILED DIRECT TESTIMONY (NONCONFIDENTIAL) OF JOHN H. STORY

PUGET SOUND ENERGY, INC.

PREFILED DIRECT TESTIMONY OF JOHN H. STORY

I. INTRODUCTION

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

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

Q. What is your educational and professional experience?

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

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

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

Q. What is the purpose of this filing?

A. In accordance with the Commission's Twelfth Supplemental Order in Docket No. UE-011570, the Company must file an annual report detailing the power costs included in its deferral calculation under the Power Cost Adjustment ("PCA") Mechanism. By approving the Settlement Agreement in the Fourth Order in PSE's power cost only rate case, Docket No. UE-050870, the

Commission authorized an amendment to the annual reporting period for the PCA Mechanism from a June 30th fiscal year to a calendar year. In compliance with this order, annual PCA true up filings are due by the end of each March for the prior PCA calendar year. Through its Petition, filed herewith, the Company is requesting approval of PSE's PCA Mechanism Report for the Twelve Months Ended December 31, 2009 ("PCA Period 8" or "PCA Annual Report").

II. BACKGROUND REGARDING THE PCA MECHANISM

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

A. As authorized by the Commission, the Company's PCA Mechanism accounts for differences in PSE's modified actual power costs relative to a power cost baseline. This mechanism accounts for a sharing of costs and benefits that are graduated over four levels of power cost variances. The Settlement Stipulation approved in the Commission's Twelfth Supplemental Order in Docket No. UE-011570 defines the specific sharing levels and conditions. It is attached as Exhibit A to the Petition.

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

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

Fixed Costs:

For PCA calculation purposes, fixed costs are power production related costs and rate of return. Power production related costs from the most recent general rate case or power cost only rate case are included and do not change during the PCA period. These costs include depreciation, property taxes for production plant, and specifically identified transmission plant. Other fixed costs include FERC Accounts 557 Other production expense, Hydro and Other Production O&M, and 500 KV O&M. Regarding the rate of return, the rate from the most recent general rate case is applied as appropriate in the PCA period.

Variable Costs:

PCA variable costs include actual monthly amounts recorded in FERC Accounts 501 – Steam generation fuel, 547 – Other power generation fuel, 555 – Purchased power, 447 – Sales for resale, 565 – Transmission of electricity by others. In addition, variable costs and credits for sales of non-core gas, Transmission Revenue for Colstrip 1-4 lines, Third AC and Northern Intertie, and costs related to the hedging line of credit are included. Allowed regulatory return on and of regulatory assets and liabilities associated with items that have been approved by order to be recovered through the PCA are also included in variable costs. A listing of these regulatory assets and liabilities are included in Exhibit D to the PCA Annual Report, Exhibit No. JHS-3.

Adjustments per the 2001 General Rate Case Settlement:

The following are adjustments as determined in Docket No. UE 011570:

1) Prudence disallowance from Docket No. UE-921262, disallowing a portion of the power costs associated with March Point 2 (3%) and Tenaska (1.2%);

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

3) New long-term resource pricing adjustment to bring the variable cost of the new resource to the lower of actual unit cost or the average embedded cost. This adjustment is reflected on PCA Exhibit G, "New Resource Adjustment." The specifics behind the calculation of this adjustment are further discussed below.

No adjustment was required during PCA Period 8 for item 2 above. Adjustments under items 1 and 3 are shown in the workpapers provided with this filing.

Q. Are there other adjustments to be considered along with those determined in Docket No. UE-011570?

A. Yes, per the Commission orders issued in Docket No. UE-031725, PSE is subject to the disallowance of costs associated with the Tenaska Benchmark Disallowance.

III. PCA PERIOD 8 ACCOUNTING

Q. Please explain how the Company has tracked its PCA Period 8 power costs.

A. The Company maintains detailed accounting instructions, which, when warranted, are provided in the supporting workpapers that provide guidance on how to track PCA Mechanism activity. There were no significant changes to the PCA Mechanism during 2009. Accounting instructions for the deferral of costs for the Mint Farm and Wild Horse Expansion projects have been included in the supporting workpapers provided with this filing. Each month the Company calculates the power costs subject to PCA sharing using the same methodology shown in PCA Exhibit B from the original PCA Mechanism filing.[1] Allowed power costs include the fixed and adjusted variable costs, net of the adjustments discussed above. Total allowable costs are then compared to the baseline power cost rate set forth in Exhibit A-1 to the PCA Annual Report, multiplied by the actual delivered load, and any difference is allocated to the Company or customers based on the different levels of sharing defined in the PCA Mechanism. Any difference allocated to the customers is recorded in FERC Account 182.3, Other regulatory assets or Account 254, Other regulatory credits depending on whether the accumulated balance is a debit or credit.

Under the PCA Mechanism, the deferred amount at the time of the next PCA annual true-up filing, along with the projected variable and fixed costs through

[1] *See* Docket No. UE-031725.

the next proposed rate year could be considered in the determination of any rate change for the subsequent PCA period. Amounts deferred, when authorized, will be amortized to FERC Account 407.3, Regulatory debits or 407.4, Regulatory credits as they are recovered or refunded by the Company to customers.

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

Q. Did the baseline power cost rate change during PCA Period 8?

A. No. From January 1, 2009 through December 31, 2009, the baseline rate was $62.841 per Megawatt Hour (MWh) as established in Docket No. UE-072300, the Company's 2007 general rate case. Included in the PCA Annual Report, Exhibit No. JHS-3, pages 12 through 18, is the calculation of this baseline rate and supporting schedules for this period.

Q. What is the average baseline rate experienced at the end of PCA Period 8?

A. As shown in the PCA Annual Report, Exhibit No. JHS-3, page 5, PCA Exhibit A-1 Power Cost Rate Updated, the average baseline rate experienced for the twelve month period ended December 31, 2009 is $64.314 per MWh.

Q. Why did the average baseline rate differ from the baseline rate in effect during PCA Period 8?

A. The average baseline rate differed from the baseline rate in effect during PCA Period 8 for the following reasons:

1) Changes in variable components of the PCA Mechanism, which are discussed in the testimony of David Mills, Exhibit DEM-01T.

2) A $5.0 million refund was received for state utility taxes paid on displacement costs under the Tenaska contract.

These displacement taxes were not included in any of the baseline rate calculations for the PCA periods impacted, however, the displacement taxes actually paid were included in power costs for PCA Period 4 through PCA Period 8. As this refund exceeded $1 million, the customer deferral and interest for prior PCA periods were recalculated as if the taxes had not been paid in the applicable time periods. A correcting accounting entry was made in October 2009. This treatment is consistent with the "Methodology for Adjustments of Costs Outside of the PCA Period" ("the Methodology") which was agreed to by the parties and approved by the Commission in the Company's PCA Period 1 compliance filing, Docket No. UE-031389. *See* Exhibit No. JHS-4.

Q. How did the actual power costs compare to the average baseline rate in effect during PCA Period 8?

A. Actual power costs exceeded the average baseline rate in effect during the PCA Period 8 by $32,198,328 (after adjustment for Firm Wholesale). The Company's share of this under-recovery of power costs was $26,099,164. As discussed in more detail below, the customers' share of this under-recovery of power costs was $6,099,164.

Q. What is the distribution of the resulting cumulative imbalance for sharing at the end of PCA Period 8?

A. Considering the activity which occurred in PCA Period 8 along with the true-up for the Tenaska Displacement Tax Refund, the cumulative imbalance for sharing at the end of PCA Period 8 was $34,744,387. The Company's share of this imbalance was $27,475,134 with the remaining $7,269,253 being attributable to the Customer. *See* Exhibit No. JHS-3 page 4.

Q. Were there any PCA Exhibit G adjustments necessary in PCA Period 8?

A. Yes. As discussed in David Mills' testimony, there were five new resources included in PCA Period 8. Two of these resources, Mint Farm and the Wild Horse Expansion, were not analyzed for purposes of PCA Exhibit G, the reasons for which are discussed in more detail later in my testimony. Three of these new resources required analysis to determine whether an adjustment was necessary under PCA Exhibit G. These resources are summarized as follows:

Resource	In-Service / Effective	Rates in Effect / Expected to be in Effect	Actual variable unit cost > Baseline Rate?	PCA Exhibit G Adjustment?
Credit Suisse PPA	1/01/2009	4/07/2010	Yes	Yes
Farm Power Rexville PPA	8/28/2009	Next Rate Filing	Yes	Yes
Qualco PPA	3/09/2009	4/07/2010	Yes	Yes

Q. How was the amount of the PCA Exhibit G adjustment determined?

A. The period that each new resource was analyzed for purposes of PCA Exhibit G was the period between the effective date of the new resource and the expected date that the new resource will be included in rates (the bridge period). Each month during the bridge period, the estimated variable costs were determined for the bridge period. The estimated generation attributable to that resource for the bridge period was then used to determine the estimated variable unit cost. This unit cost was compared to the baseline rate in effect during the bridge period. When the actual variable unit cost exceeded the baseline rate in effect, the excess unit cost was multiplied by the ratio of the current month's generation to the estimated bridge period generation to determine the amount of the PCA Exhibit G adjustment for that month. There were three new resources—the Credit Suisse, Farm Power Rexville, and Qualco purchase power agreements ("PPAs")—each of which resulted in an adjustment during PCA Period 8. This calculation resulted in a total reduction to total allowable costs of $261,589: $179,144 for the Credit Suisse PPA, $25,869 for the Farm Power Rexville PPA, and $56,576 for the Qualco PPA. This information is included in the Updated Power Cost Rate in the PCA Annual Report, Exhibit No. JHS-3, p. 5, line 24b.

Q. Why has the Company not applied PCA Exhibit G to Mint Farm or Wild Horse Expansion PCA Period 8 costs?

This is an issue in dispute in the current general rate case filing, Docket No. UE-090704. The Company believes that the adjustment is inappropriate for the reasons provided in that case. The Commission has not ruled on whether PCA Exhibit G should be applied to these new resources whose costs are being deferred pursuant to RCW 80.80.060.

Q. **Please explain how the Company tracked the variable deferral for Mint Farm and Wild Horse expansion under PCA Period 8.**

PSE is currently deferring all of the costs, both fixed and variable, for Mint Farm and Wild Horse Expansion including those during PCA Period 8. The only deferrals that impact the PCA are the variable deferrals. PSE deferred the PCA defined variable costs associated with Mint Farm and Wild Horse expansion including fuel, transmission and fuel transportation. These costs were removed from the PCA Period 8 total allowable costs for purposes of calculating the PCA deferral. Replacing these costs, PSE credited the variable cost deferral with the hourly market price of power used to determine the current baseline rate approved in PSE's 2007 general rate case rebuttal filing dated July 3, 2008. This calculated amount was included as a credit to the 186 deferral account and a charge to FERC Account 555, Purchased Power. The charge to FERC Account 555 was included in the monthly PCA true-up calculation as a power cost. During PCA Period 8, a total of $69,975,266 in variable costs for Mint Farm and $118,000 in variable costs for Wild Horse Expansion were deferred. Offsetting charges to FERC Account 555 for the replacement market power totaled $81,478,311 for Mint Farm and $597,535 for Wild Horse Expansion.

Q. What is the resulting customer PCA deferral balance for PCA Period 8?

As of December 31, 2008, the Company had deferred for future recoveries $1,804,703 of under-recovered power costs before revision for the Tenaska Displacement Tax Refund. After revisions were made pursuant to the Methodology, the revised customer deferral balance was $1,170,089. During PCA Period 8, the customers' share of the power cost under-recovery was $6,099,164. Therefore, the customer deferral balance at December 31, 2009 is $7,269,253. Interest of $1,229,577, as revised for the impacts of the Tenaska Displacement Tax Refund, represents the accrual at the end of PCA Period 7. PCA Period 8 interest was $30,536. Adding the total accrued interest of $1,260,113 to the deferred balance of $7,269,253, results in a total customer deferral balance under the PCA Mechanism at December 31, 2009 of $8,529,366. *See* the PCA Annual Report, Exhibit No. JHS-3, page 4.

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

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

IV. ADJUSTMENT OF COSTS OUTSIDE OF THE PCA PERIOD

Q. Please describe in more detail the adjustments made in PCA Period 8 for the Tenaska tax refund.

PSE received a refund during PCA Period 8 that related to PCA Periods 4 through 8; thus, there was an adjustment necessary to PCA periods 4 through 8 totaling ($5,023,074). These adjustments were associated with a refund of payments made for Tenaska Displacement Tax as a result of the Thurston County Superior Court granting PSE's motion for summary judgment against the Washington Department of Revenue for recovery of the state utility tax that PSE had been paying under protest since 2006. The tax refund was a credit to the total purchase power costs in FERC Account 555 as this was the account to which the original tax payments were expensed and included in total allowable costs for PCA purposes when booked. A revised version of the summary schedules for PCA Period 4 through PCA Period 7 that incorporates these adjustments has been provided in the workpapers related to this filing.

Approximately ($0.7) million of the ($5.0) million related to PCA Period 8 power costs, and as such, the payments made and refunds received net to zero in PCA Period 8, as if the payments had not been originally included in total allowable costs.

Q. Does this conclude your testimony?

A. Yes, it does.