APPENDIX B

Excerpts from Mr. John Story's Testimony
Relating to Specific Accounting Items

RE: BPA Transmission Upgrade Regulatory Asset

Q. What does the adjustment for the Hopkins Ridge Project prepaid transmission expense represent?

A. The $9,138,350 increase to ratebase on Line 9 of Adjustment 3 represents the AMA balance during the rate year of the ten million dollar payment made to BPA to upgrade their transmission substation and transmission lines for interfacing with the Hopkins Ridge Project. As discussed by Mr. Garratt, Exhibit No.___(RG-1HCT), the Company will receive a credit for the demand charge on its transmission billing for this payment.

Q. How does the Company propose to handle this payment for the PCA?

A. The Company proposes to handle this payment for the PCA as a regulatory asset that will earn the current net of tax rate of return in the same manner as other power cost related regulatory assets. The Company will clear this account based on BPA transmission billings that will show the actual transmission demand cost associated with Hopkins Ridge for a given month.

This demand charge for the transmission billing will be offset by two adjustments. The first adjustment is a credit against the transmission demand charge for a carrying cost that is based on the remaining balance of the original payment times

the monthly FERC interest rate. This will be a reduction in transmission expense that is passed through to the customer. The second offset will be a reduction on the demand charge associated with the original ten million dollar payment. This reduction in cost is credited against the prepayment and as long as there is a balance associated with the prepayment this second adjustment will reduce the demand charge to zero. For ratemaking purposes, PSE will credit the regulatory asset account for this second adjustment and charge transmission expense. This charge to transmission expense will be picked up in the PCA.

For this filing, the Company has calculated the regulatory asset balance on the projected average of the monthly balances during the rate year based on the expected generation for Hopkins Ridge. PSE has also included the associated transmission costs in operating expenses. These costs are shown as variable expenses and will be trued up to actual generation and transmission expense during the PCA period.

Q. Why is the Company proposing to earn its authorized rate of return on the transmission investment rather than retaining the FERC interest rate?

A. The FERC interest rate at the date of this filing is 5.3%. By contrast, the Company's currently authorized net of tax rate of return is 7.01%. When the Company earns a return on funds it has invested that is lower than its authorized rate of return, it drives down the rate of return that the Company is capable of actually earning. The Company's proposal to treat its transmission investment for the Hopkins Ridge Project as a regulatory asset that earns the Company's authorized rate of return will reimburse the Company for its actual cost of funds

as allowed in its last general rate case.

The Company believes that this treatment is appropriate as the transmission investment was required in order to use the generation from the Hopkins Ridge Project to serve PSE's system, and as such, is part of the costs of that plant that should be treated on par with the ratebase portion of the production asset.

PSE's proposed method, described above, of passing through to customers the transmission cost credit associated with the FERC interest rate paid by BPA will prevent double collection by the Company of a return on its transmission investment.

RE: Production Tax Credit Tracker & Related PCA Mechanism Calculation

I. REQUESTED RATE INCREASE

Q. Please explain how the Company calculated the rate increase required after taking into consideration the power cost pro forma and restating adjustments.

A. As the Company is only requesting that a portion of its rates be adjusted using the power cost only rate filing, the Company has calculated the required change in rates using the difference between the current and proposed Power Cost Rate. This calculation is shown in Exhibit No.___(JHS-6). As shown on line 15 of this exhibit, the new rate is $54.876 and the current rate is $51.445 after revenue sensitive items are applied. The difference between these two rates is multiplied by the normalized delivered load for the test period. The result of this calculation is the requested change in revenue requirement of $68,711,052 after revenue

sensitive items. This change in rates results in an average increase of approximately 4.52%. However, the rate increase being requested by the Company is lower than this amount due to the impact of the Production Tax Credit associated with the Hopkins Ridge Project, as described below.

Q. Would you please explain what the Production Tax Credit is?

A. The Production Tax Credit ("PTC") is a subsidy provided by the U.S. Government for generating electricity from wind. The amount of the subsidy is currently 1.9 cents per kilowatt hour for wind generation and will be adjusted over time due to inflation adjustments. As of the date of this filing, this subsidy can be claimed for the first 10 years for a new wind project put into service prior to January 1, 2006. The use of the credit is restricted in that it can only be used to offset 25% of a company's current taxes payable. However, unused credits can be carried forward for up to 20 years.

Q. How does the Company propose to pass the PTC through to the customer?

A. The PCA mechanism only includes tax accounts associated with production plant and production related regulatory assets. As mentioned above, the use of the tax credits are restricted to offsetting 25% of the Company's current taxes payable, with the possibility of being carried forward to future years' taxable income if it is not possible to utilize them in the current year. In addition, the tax credits are associated with the current years taxable income which is payable in quarterly installments during the year with any final payments being made in September of the following year. This creates a deferred tax account based on the timing difference between the generation of the tax credits associated with actual

generation of electricity from the wind plant and how the tax credits would impact current taxes for taxable income. This accounting impacts Account 236, current taxes payable, and Account 190, Accumulated deferred income taxes which are not reflected in the PCA tracking.

To properly flow these tax credits through to the customer, the Company proposal is to create a PTC tracker that will pass through to the customer the actual production tax credits as they are generated and the tracker would not be subject to the sharing bands in the PCA. This pass through will be adjusted by the carrying costs for the deferred tax account for the PTCs that have been generated but have not been used for the current years tax credit. As the customer is receiving the benefit of the tax credits as they are generated and the Company does not receive a credit from the IRS until the tax credits are utilized the Company is reimbursed its carrying costs for funds through this calculation. This tracker would initially be used for the Hopkins Ridge Project, but would also be available for the PTCs that may be associated with other wind generating facilities that the Company may acquire in the future.

The initial tracker for these credits has been estimated using the projected PTCs to be generated by the Hopkins Ridge Project and the estimated balance of the deferred tax account. This calculation is shown on Exhibit No.___(JHS-7). During the rate year, and beyond, the actual PTCs generated by PSE's wind facilities and the return on the actual deferred tax balance will be compared to the amount included on customers' bills. Any difference between the actual amounts versus what was credited to customers will be used to adjust the tracker. PSE will

also adjust the tracker for any new estimates of PTCs based on a forward looking tax year. It is our expectation that this tracker will be adjusted yearly to reflect these differences or a report will be filed showing why an adjustment is not necessary. As this tracker is not tied to a PCA period or a PCORC filing, and instead is tied to the Company's tax filings, the Company proposes to file an update every October for the next tax year with the ability to file sooner to adjust a tax year if the PTC's generated versus what were estimated vary by more than 25%.