Exhibit T___ (JMR-1T)
Docket No. UE-031725
Witness: James M. Russell

BEFORE THE WASHINGTON UTILITIES AND TRANSPORTATION COMMISSION

WASHINGTON UTILITIES AND TRANSPORTATION COMISSION, **Complainant,** **v.** **PUGET SOUND ENERGY, INC.,** **Respondents.**	**DOCKET NO. UE-031725**

DIRECT TESTIMONY OF

James M. Russell

STAFF OF
WASHINGTON UTILITIES AND
TRANSPORTATION COMMISSION

January 30, 2004

DIRECT TESTIMONY OF

JAMES M. RUSSELL
DOCKET No. UE-031725

Q. Please state your name and business address.

A. I am James M. Russell. My business address is 1300 S. Evergreen Park Drive S.W., P.O. Box 47250, Olympia, WA 98504.

Q. By whom are you employed and in what capacity?

A. I am employed by the Washington Utilities and Transportation Commission as a Regulatory Analyst.

Q. How long have you been employed by the Commission?

A. Approximately 19 years, from June 1985 to the present.

Q. Would you please state your educational and professional background?

A. I graduated from Washington State University in 1983 receiving a Bachelor of Arts in Business Administration with a major in accounting.

My work at the Commission generally includes financial, accounting, and other analysis of general rate case and tariff filings, incentive proposals, special

contracts, least cost plans, and rulemaking proceedings involving investor owned electric and natural gas utilities regulated by the Commission. Over my career at the Commission I have provided testimony in approximately 10 formal general rate case proceedings and have been involved in numerous negotiated electric and natural gas general rate case settlements. I have also presented Staff recommendations in many Commission open public meetings.

Q. What is your responsibility in this proceeding?

A. I am responsible for Staff's calculation of Puget Sound Energy's ("PSE" or the "Company") revenue deficiency in this proceeding. I am also responsible for rate spread and rate design issues. The responsibilities I have mirror those of PSE witness Mr. John Story.

Q. Would you briefly summarize your recommendation?

A. Staff recommends that the Commission grant PSE an additional $7,527,693 (.55% increase) in annual Power Cost revenues collected consistent with the rate spread and rate design methodologies established in the Power Cost Adjustment ("PCA") settlement in Docket No. UE-011570.

Q. Are you sponsoring any exhibits in this proceeding?

A. Yes, I am sponsoring the following exhibits:

Exhibit ___ (JMR-2), Restating and Pro forma Power Cost Adjustments
Exhibit ___ (JMR-3), PCA-2 Power Cost Rates and Exhibits
Exhibit ___ (JMR-4), Revenue Deficiency Calculation
Exhibit ___ (JMR-5), Allocation of PCORC Revenue Deficiency
Exhibit ___ (JMR-6), Statement of Current and Proposed Revenues

I. POWER COST ADJUSTMENTS, NEW POWER COST RATES, AND REVENUE DEFICIENCY

Q. Would you please begin by briefly describing what is included in your Exhibit ___ (JMR-2), Restating and Pro forma Power Cost Adjustments?

A. Exhibit ___ (JMR-2) summarizes Staff's restating and pro forma Power Cost adjustments, average Power Cost rates, and Power Cost revenue deficiency. For ease of comparison, the figures that have been shaded on all my exhibit pages indicate input differences from PSE's direct case. Also, on page 18 of Exhibit ___ (JMR-2) there is a case comparison summarizing the differences between PSE's and Staff's direct filed cases, by adjustment. This page is provided for illustrative purposes only and it must be recognized that almost all of the adjustments within Exhibit ___ (JMR-2) are interdependent.

Q. Would you please describe Exhibit ___ (JMR-2) in more detail?

A. Beginning on page 1 of Exhibit___(JMR-2), the first column entitled "Test Year Actual 2003 TY" reflects the test year (July 2002- June 2003) Power Cost amounts. Adjustments 1 through 13, on pages 1 and 2, show the individual impact of Staff's proposed restating and pro forma adjustments to PSE's Power Cost accounts. The first line on pages 1 and 2 of this exhibit indicates which Staff witness is responsible for the issues and calculation of the amounts in that particular adjustment column. The total test year amounts, net of all adjustments, is shown on page 2, second to last column entitled "Restated 2003 TY". The last column shows the average cost rates (in $/MWh) for each line item and for the total of all Power Costs. Pages 3 through 15 support each of the Adjustments 1 through 11. Adjustments 12 and 13 come from Mr. Schooley's Exhibit ___ (TES-4C) and Exhibit ___ (TES-6C). Page 16 of my Exhibit ___ (JMR-2) shows the impact of Mr. Mariam's temperature normalization adjustment on MWh sales. Page 17 shows the current and proposed revenue sensitive conversion factors. Finally, page 18 shows the comparison between PSE and Staff's direct cases. This exhibit generally parallels the format of Mr. Story's Exhibit ____ (JHS-4).

Q. Please briefly discuss what is shown in Exhibit ___ (JMR-2) page 1, lines 2 through 22.

A. Lines 2 through 4 are the production related regulatory assets and rate base values used to determine the Power Cost amounts (return and federal income tax) on lines 6 through 8. Line 5 is the "Net-of-tax rate of return" that is used to calculate the return on rate base and regulatory assets on lines 2 through 4. Lines 6 through 8 are the return and federal income taxes on the rate base and regulatory assets items and is calculated by multiplying lines 2 through 4 by the "Net of tax rate of return" divided by 1 minus the federal income tax rate of 35%. Lines 9 through 22 are the Power Cost operating expense items included within the PCA mechanism.

Q. Please indicate for which adjustments you and other Staff members are responsible.

A. Mr. McIntosh is generally responsible for the determination of pro forma "rate year" power costs used in the calculations for Adjustments 1 and 2. I am responsible for converting the "rate year" Power Costs back to "test year" levels in these two adjustments. Mr. McIntosh is also responsible for the prudence issues and power costs associated with the Fredrickson I purchase (Adjustment

3, "New Plant") and I am responsible for calculating the dollar amounts shown in Adjustment 3 for Production Rate Base (Fixed), Depreciation, and Property Taxes. I am also individually responsible for Adjustments 4 through 11. Mr. Schooley is responsible for Adjustment 12, "UE-921262 Tenaska Adjustment". Mr. Elgin is responsible for Adjustment 13, "Tenaska and Encogen Fuel Adjustment", while Mr. Schooley provides the calculation of that adjustment amount.

Q. Please describe the reason for the production factor and how it is used in this rate proceeding?

A. "Production factoring" and the so-called "Production Adjustment" (Adjustment 11) is specific to PSE because PSE is the only regulated electric utility in Washington that uses a future test period when calculating Power Costs (production related costs) for revenue requirement purposes. The production factor is simply rate year volumes divided by test year volumes. The production factor is used to complete the pro forming of production costs from the forward looking "rate year" (April/04-March/05) level back to the pro forma "test year" (July/02-June/03) amount. In the power supply models run to support Mr. Gaines' and Mr. McIntosh's pro forma rate year calculations, rate year levels of

consumption are used rather than the test year level of consumption. In these models, and in other pro forma calculations, future rate year costs are considered. As that future rate year has a different level of consumption than the normalized historic test period, the production factor is applied to pro forma rate year costs, on a unit basis, before applying them in the historic test year. I will discuss the Production Adjustment in more detail later in my testimony.

Q. Please continue with a description of the test year amounts shown in Exhibit __ (JMR-2), page 1, and each of the adjustments for which you have partial or total responsibility.

A. Test Year Amounts. I was responsible for reviewing the calculation of the test year amounts. As a result of my review, there are four line items in the test year amounts on page 1 that have been revised from the Company's presentation. First, the amount shown for Regulatory Assets (Variable) (line 2) has been revised to reflect the PCA settlement agreement in Docket No. UE-031389, which the Commission approved through the issuance of Order No. 4 in that docket. The Regulatory Asset amounts and associated amortization should not be at issue in this proceeding.

Second, the test year amount for Production Rate Base (Fixed) (line 4) has been lowered by $12,045,679 to remove construction work in progress ("CWIP") associated with the costs to re-license the Snoqualmie Falls Hydro Project. PSE does not address the reasons for including this cost as an addition to production rate base, but after reviewing the test year amounts and data requests on the subject, it became clear that PSE would most likely not receive Federal Energy Regulatory Commission ("FERC") approval for re-licensing of the Snoqualmie Falls Hydro Project during the rate year because of ongoing litigation.

Third, the test year amount for Account 557–Other Power Expense (line 11) has been reduced by $475,859 for an error in PSE's calculation of the test year amount of property insurance that is included in this account. In the test year property insurance amount, PSE's calculation included an extra seven months of property insurance on Colstrip.

Fourth, the test year amount for Property Taxes – Production (line 21) has been increased by $500,434 because of an error PSE made in calculating the test year production plant percentage.

Adjustment 1, "Power Costs". The Company's adjustment has been revised for two main reasons. First, and most importantly, Mr. McIntosh

proposes various adjustments to PSE's Power Costs, which flow through Staff's Adjustments 1 and 2. Second, Staff's production factor has been increased to reflect Dr. Mariam's additional test year KWh sales associated with weather normalization. Page 3 of Exhibit ___ (JMR-2) shows Staff's support for Adjustment 1. The column entitled "Pro forma RYE Mar 05" on page 3 comes from page 4, last column entitled "After Prod Factor of .99101". The sixth column on page 4, entitled "12ME 3/31/05" is provided by Mr. McIntosh and is adjusted for items he discusses in his testimony. This adjustment decreases Power Costs by $156,127,724.

Adjustment 2, "Sales For Resale". This adjustment is also the responsibility of Mr. McIntosh and it flows forward in the same manner as Adjustment 1: from page 4, line 15. Adjustment 2 is also corrected for the change in the production factor. This adjustment increases Power Costs by $152,573,194.

Adjustment 3, "New Plant". This Adjustment pro forms the costs of the Fredrickson 1 plant into the test year. Staff has revised the Company's adjustment for two items. First, Staff removed the proposed capitalization of sales tax associated with the purchase of Fredrickson I. Mr. Story indicates in his testimony (pages 10-11) that PSE requested a ruling from the Washington Department of Revenue ("WDOR") verifying that sales tax would not be

applicable to this transaction. However, PSE has included capitalized sales tax in its case pending a final determination from the WDOR. Subsequent to filing its case, and on January 5, 2004, PSE received a positive determination from the WDOR on this issue and the capitalized sales tax of $6,258,328 has been removed in the "Plant Balance" shown on my page 6, line 2. Also on page 6, "New Plant Depreciation Expense" (line 9) and "Deferred FIT" (line 4) have been revised for the impact of removing capitalized sales tax from the new plant balance.

Second, PSE stated the "Accumulated Depreciation" (line 3) balance at the rate year end-of-period amount rather than at an average-of-monthly-average basis. I have corrected the accumulated depreciation amount for the capitalized sales tax item and restated it to an average accumulated depreciation basis. This adjustment increases Power Costs by $42,368,805

This adjustment amount does not represent the total revenue requirement associated with the Fredrickson I purchase. Adjustment 1, 2, and 11 also include impacts associated with the Fredrickson I purchase. In response to Staff Data Request No. 2, PSE provided a calculation of its case excluding the impacts of Fredrickson I. PSE's revenue deficiency excluding Fredrickson I was approximately $46 million, or approximately $18 million less than it was with Fredrickson I. The revenue requirement impact of Fredrickson I in Staff's case

would be a bit different however, because of the revisions to the Fredrickson I adjustment for capitalized sales tax and the impact of Dr. Mariam's revised sales volumes.

One last issue with the Frederickson I purchase is that if the power plant is not placed in service at the time the PCORC rates become effective, then the PCA deferral calculations should account for the delay by removing the rate base, depreciation, and other Fredrickson I fixed costs from the deferral calculations.

Adjustment 4, "Transmission Income". My Adjustment 4 restates the transmission revenue in Account 456-17 to a normalized level given the variability in this account due to market conditions during a particular year. It is my understanding that PSE had only included firm transmission revenues for which it had commitments during the rate year at the time it prepared its filing. That methodology is not appropriate as it would most likely understate actual variable transmission revenues received in the future rate year. PSE also assumed no "non-firm" transmission revenues in its adjustment, again most likely understating actual rate year transmission revenues. I propose that the Commission adopt a normalization (averaging) methodology for this item when establishing the new PCA benchmark rate. I propose an adjusted (as necessary) 3-year average of actual experience for this item in this Power Cost Only Rate

Case ("PCORC") and subsequent PCORC and general rate case filings. This normalization process results in estimating rate year transmission revenues of $3,739,245, rather than the Company's proposed amount of $1,399,117. The calculation of Staff's proposed amount of $3.74 million is shown on page 8, line 20. This adjustment increases Power Costs by $3,253,602.

Adjustment 5, "Production Plant Depreciation and Amortization". This adjustment is made to restate depreciation expense and accumulated depreciation at an average-of-monthly-average basis in the test year and reduces Power Costs by $65,231. This adjustment is the same as the Company's.

Adjustment 6, "Property Taxes". This adjustment restates the test year for known changes in property tax rates and for changes in production plant balances. I have made a revision to the test year amount of property taxes to correct an error in PSE's production plant allocator used to determine the test period amount on page 10. This correction has no impact on the revenue deficiency in this case because both the "Test Year Actual 2003" amount in Exhibit ___(JMR-2) page 1, line 21, and the test year amount shown in Adjustment 6, page 10, are revised. There is no correction to the "Restated" amount shown on page 10. This adjustment increases Power Costs by $152,265.

Adjustment 7, "Montana Energy Tax". This adjustment pro forms Montana Energy tax based on Colstrip generation during the rate year. This adjustment is revised for Mr. McIntosh's rate year Colstrip generation. This adjustment increases Power Costs by $92,218.

Adjustment 8, "Property Insurance". This adjustment pro forms property insurance to current levels. The test year amount has been revised for the error in calculating property insurance for Colstrip that I discussed earlier in the "Test Year Amounts" section of my testimony. This adjustment correction has no impact on the revenue deficiency in this case because both the "Test Year Actual 2003" amount embedded in line 11 on Exhibit ___ (JMR-2), page 1, and the test year amount shown in Adjustment 7, page 12 are revised. There is no correction to the "Pro forma RYE Mar 05" amount shown on page 12. This adjustment increases Power Costs by $126,210.

Adjustment 9, "White River". PSE's proposed Adjustment 9 removes the White River Hydro Project from the test period because the current FERC license expired on January 15, 2004. Subsequent to PSE filing its case in this docket, and on December 10, 2003, the Company filed an accounting petition (Docket No. UE-032043) requesting to defer the remaining net book value of White River as a regulatory asset and to begin amortization of this regulatory asset within the

PCA mechanism. Currently, Staff has a tentative agreement with PSE on how to handle both the White River Hydro Project in this proceeding and in the pending accounting petition. For this proceeding, we have tentatively agree to include White River in the test period at the rate year level and have agreed to leave depreciation and amortization at current levels. The final agreement on the accounting petition filed in Docket No. UE-032043 will be presented to the Commission at an open meeting within a short time. This adjustment increases Power Costs by $208,049. This compares to PSE's original adjustment to remove White River, which decreased Power Costs by $6,752,621.

Adjustment 10, "Regulatory Assets/Acq.". This adjustment pro forms the rate year rate base and amortization for the regulatory assets associated with Tenaska, Cabot, and Bonneville Exchange Power ("BEP") contract buyouts. I have revised the Company's adjustment for two items. First, the Tenaska and Cabot regulatory assets have been restated to the level reflected in the recent PCA settlement in Docket No. UE-031389. This revision should not be at issue in this proceeding. Second, I have restated the amount for the Encogen Acquisition Adjustment (line 8) at the test year level ($52,615,858), consistent with the intent of the original PCA settlement in Docket No. UE-011570. PSE had incorrectly

stated this item at the rate year level ($47,973,283). This adjustment decreases Power Costs by $3,521,669.

Adjustment 11, "Production Adjustment". This adjustment pro forms Staff's revised rate year production rate base items and production operating expenses for all items exclusive of production related amounts which have already been production factored in Adjustments 1, 2, 3 (lines 15-17), 4, 12, and 13. I have included a calculation comparing Staff and PSE's production factor at the bottom of page 15, at line 44. This adjustment reduces Power Costs by $1,353,766.

Adjustment 12, "UE-021262 Tenaska". Mr. Schooley's testimony addresses the rational and calculation for Adjustment 12 that is shown on page 2 of Exhibit ___(JMR-2). These amounts come directly from Mr. Schooley's Exhibit ___ (TES-4C), line 29. This adjustment reduces Power Costs by $11,947,000.

Adjustment 13, "Tenaska and Encogen Fuel". Mr. Elgin's testimony addresses the rational for Adjustment 13 and Mr. Schooley discusses the calculation of the amount that is shown on page 2 of Exhibit ___(JMR-2). These amounts come directly from Mr. Schooley's Exhibit ___ (TES-6C), line 28. This adjustment reduces Power Costs by $33,341,000.

Q. Does this conclude your discussion of Exhibit __(JMR-2)?

A. Yes.

Q. Please explain what is included in your Exhibit ___ (JMR-3), PCA-2 Power Cost Rates And Exhibits.

A. This exhibit mirrors Mr. Story's Exhibit ___(JHS-5). Exhibit ___(JMR-3), pages 1 through 8, are based on, and support, Staff's "Restated 2003 TY" amounts and average $/MWh rates shown in Staff's Exhibit ___(JMR-2), page 2, last 2 columns. The reason for Exhibit___(JMR-3) is to update the current PCA settlement exhibits in Docket No. UE-011570 with those pages that will be used for calculating PCA deferrals in accordance with the PCA settlement beginning in the rate year. The Commission will need to adopt these exhibits (recalculated in accordance with the final order in this docket) for use in the PCA periods subsequent to the Commission's Order in this docket.

One other revision to these exhibits, besides the dollar amounts, are proposed revisions to page 8, Exhibit E – Contract Adjustments. I have split the North Wasco contract rate into separate Winter and Summer pricing periods in accordance with the recent PCA settlement. In addition, I propose that PSE defer the actual costs associated with the Hutchison Creek, Port Townsend,

Sygitowicz, and Nooksack power supply contracts because they are so small and some contain market-pricing provisions.

Q. Please explain your Exhibit ___ (JMR-4), Revenue Deficiency.

A. Exhibit ___(JMR-4) shows the calculation of Staff's revenue deficiency in the amount of $7,527,693. This exhibit simply calculates the change in the current and proposed "grossed up" PCA rate multiplied by the pro forma test year volumes.

There is an issue with regard to the calculation of the revenue deficiency between my Exhibit ___ (JMR-4) and Mr. Story's Exhibit ___(JHS-6). The issue is whether the impact of tax rate changes, up or down, on PCA revenues (65% of PSE, electric revenues) should be reflected in a PCORC proceeding. This issue was not resolved by the PCA settlement. Mr. Story's method does not flow-through the impact from revenue sensitive tax rate changes on PCA revenues, while mine does. As an example, the current PCA cost rate is $43.953/MWh with a current revenue conversion factor of .95523, while Staff's proposed PCA cost rate is $44.337/MWh with a proposed conversion factor of .95547 and pro forma sales volumes of 19,271,717 MWhs. My method results in a total increase of $7,527,693 as shown in Exhibit ___(JMR-4). This amount includes a cost

reduction of $224,684 associated with the revenue sensitive tax decrease [(((44.337/.95547)-44.337) - ((44.337/.95523)-44.337)) x 19,271,717]. Using PSE's approach, the revenue deficiency would be $217,542 higher at $7,745,235 [((44.337-43.953) x 19,271,717)/.95547]. PSE's method, reflected in Exhibit ___(JHS-6), does not flow-through the savings associated with the reduction in revenue sensitive taxes. The method of calculating the revenue deficiency in Exhibit ___(JMR-4) should be adopted by the Commission in order to clarify this issue for future PCORC proceedings.

II. RATE SPREAD, RATE DESIGN, AND PROPOSED TARIFFS

Q. Please explain your Exhibit ___ (JMR-5), Allocation of PCORC Revenue Requirement.

A. This exhibit calculates the rate spread and rate design using the peak credit methodology used in PSE last general rate case, Docket No. UE-011570. The proposed rate spread is shown in column (g), and rate design is shown in column (i). Exhibit ___ (JMR-5) is simply Mr. Story's Exhibit ___(JHS-7) updated for Staff's sales volumes and revenue deficiency of $7,527,693.

Q. Please explain your Exhibit ___ (JMR-6), Statement of Current and Proposed Revenue.

A. Page 1 of this exhibit shows PSE's electric revenues at current and proposed rates and the percentage increases, by schedule. Page 2 shows the individual rates for street lighting. This Exhibit is the same as Mr. Story's Exhibit ___(JHS-8), updated for Staff's sales volumes and revenue deficiency.

Q. Have you reviewed Mr. Story's Exhibit ___(JHS-9) and do you have any issues with the proposed tariff sheets?

A. I have reviewed the proposed tariff sheets and, except for the rate levels, I have no issue.

Q. Does this conclude your testimony?

A. Yes.