

**EXHIBIT NO. \_\_\_(SSO-7)**  
**DOCKET NO. UE-13\_\_\_**  
**WITNESS: SAMUEL S. OSBORNE**

**BEFORE THE  
WASHINGTON UTILITIES AND TRANSPORTATION COMMISSION**

**In the Matter of the Petition of  
PUGET SOUND ENERGY, INC.  
For an Accounting Order Approving the  
Allocation of Proceeds of the Sale of  
Certain Assets to Public Utility District  
#1 of Jefferson County.**

**Docket No. UE-13\_\_\_\_\_**

**SIXTH EXHIBIT (NONCONFIDENTIAL) TO THE  
PREFILED DIRECT TESTIMONY OF  
SAMUEL S. OSBORNE  
ON BEHALF OF PUGET SOUND ENERGY, INC.**

**OCTOBER 31, 2013**

# Public Utility District #1

Of Jefferson County

Board of Commissioners  
Barney Burke, District 1  
Ken McMillen, District 2  
Wayne G. King, District 3  
  
James G. Parker, Manager

June 14, 2010

Mr. Steve Wright  
Administrator  
Bonneville Power Administration  
905 NE 11<sup>th</sup> Avenue  
Portland, Oregon 97232

**Re: Public Utility District No. 1 of Jefferson County's Request for Firm Electric Power Service from Bonneville Power Administration**

Dear Mr. Wright:

On June 11, 2010, the Public Utility District No. 1 of Jefferson County (JPUD) entered into a binding Asset Purchase Agreement (APA) for the purchase of all electrical utility system assets, facilities, and properties that Puget Sound Energy (PSE) currently uses to provide electrical service to PSE customers located in Jefferson County, Washington. We submit this letter to support JPUD's request for firm electric power service from the Bonneville Power Administration (BPA).

Under Washington law, JPUD has the power of eminent domain, and can therefore acquire PSE's facilities through condemnation. RCW 54.16.020. However, the PUD Board elected to explore whether PSE's electric facilities could be acquired through negotiation. JPUD began negotiations with PSE in mid-2009, and those negotiations culminated in the parties entering into a non-binding Letter of Intent dated April 30, 2010. Since early 2010, JPUD has been actively planning for implementation of its electric utility function. JPUD has engaged the services of experts in the fields of electric utility operations, engineering, and public finance, and has been meeting with neighboring utilities and the USDA's Rural Utility Service (RUS).

Over the course of its discussions with PSE, JPUD representatives have both corresponded and met with staff at the Bonneville Power Administration (BPA) to discuss JPUD's future access to BPA power. JPUD is the first "new public" to form and request power since BPA issued its "Long-Term Regional Dialogue Final Policy" in 2007. Accordingly, JPUD

has included considerable information in this letter and its attachments as evidence that JPUD fully complies with BPA's Standards for Service.

By this letter and its supporting documents, JPUD requests an expeditious determination that JPUD has sufficiently demonstrated compliance with all of BPA's Standards for Service and is eligible to receive power from BPA as a newly formed public utility. JPUD has reviewed the contract template for load following entities and stands ready to enter into a binding power purchase agreement with BPA. For the reasons described in detail in this letter and supporting materials, JPUD requests that BPA offer JPUD a power purchase contract at its earliest convenience for joint execution before July 1, 2010.

### **About JPUD**

JPUD was formed in 1939 and is one of 28 PUDs in the State of Washington. Of those 28, 23 are in the electric service business. JPUD will be number 24, and the first new public power utility in the State of Washington in many years. JPUD currently serves more than 3,500 water and sewer customers throughout East Jefferson County. JPUD is headquartered in Port Hadlock. It currently has nine employees and an annual budget of about \$2 million. The PUD has a board of three elected commissioners who serve six-year terms. The current PUD Board consists of Commissioners Ken McMillen (President), Barney Burke (Vice President) and Wayne King (Secretary). More information on JPUD can be found at its web site including information on rates for its water and sewer utility functions. See <http://pud.co.jefferson.wa.us>.

### **Bringing Public Power to Jefferson County**

On November 4, 2008, by a vote of 54 percent in favor, Jefferson County voters authorized JPUD to become an electric utility through either condemnation or negotiated acquisition of the electric facilities serving Jefferson County. The JPUD Board of Commissioners was prepared to condemn PSE facilities pursuant to its mandate from the voters. However, successful negotiations between the parties resulted in a non-binding Letter of Intent. Both parties have worked diligently to finalize all definitive agreements, and the JPUD Board of Commissioners approved the APA by resolution on June 11, 2010. JPUD expects to add 25-35 employees to its existing utility operations and serve about 18,000 electric customers in Jefferson County after it completes the implementation of its electric utility function.

### **Key Benefits to a Negotiated Purchase**

JPUD's commissioners have carefully analyzed this transaction and concluded that entering into the APA will cost the citizens of Jefferson County less overall and provide for a much smoother, more efficient transition than condemnation could ever provide. JPUD was prepared to file a condemnation proceeding against PSE if its efforts to achieve a negotiated acquisition failed. Even though a condemnation lawsuit might have resulted in an initially lower purchase price for the facilities than the agreed price, a condemnation trial and appeal would be lengthy and expensive, with unpredictable results.

The JPUD Board has achieved a key advantage for the citizens of Jefferson County through negotiation of a transition period (Transition Period), which would not have been available using the condemnation process. JPUD benefits from the Transition Period for a

number of reasons. The Transition Period provides JPUD with an opportunity to secure its power supply from BPA sooner than the condemnation process would have allowed, it allows implementation of its electric utility function in a deliberate, cost-effective manner, and enables JPUD to secure long-term low-cost financing from the RUS. The value of these benefits is significant, because together they substantially reduce the cost of electricity to Jefferson County over the long-term.

### **JPUD is Eligible to Purchase Preference Power from BPA**

As a “public body,” JPUD has a legal right to purchase low cost power from BPA, and is entitled to both preference and priority for purchase of that power pursuant to sections 4 and 5 of the Bonneville Project Act of 1937, 16 U.S.C. §§ 832c(c) and 832c(d), and section 5(b)(1) of the Northwest Power Act (the Act). 16 U.S.C. § 839c(b)(1). JPUD recognizes, however, that BPA is only required to sell JPUD power *if* BPA determines that JPUD meets BPA’s “Standards for Service” 16 U.S.C. §§ 839c(b)(1)-(4). In determining whether or not a potential BPA customer is eligible to purchase federal power, BPA considers whether the customer meets its six separate Standards for Service.

BPA’s Standards for Service each relate to distinct issues, but together they serve the general purpose of insuring that the benefits of low cost federal power reach the citizens of the Pacific Northwest and that a public body has the financial and operational ability to meet its commitments to BPA under a power purchase contract. As set forth in this letter and the detailed discussion in **Attachment A**, JPUD is expeditiously taking all required and necessary steps to be ready to receive power from BPA on its expected service date.

The following is an overview of the reasons that JPUD satisfies BPA’s six Standards for Service.

1. Legally formed in accordance with local, state, federal or tribal laws.

JPUD was legally formed by the voters of Jefferson County nearly 70 years ago, in accordance with applicable Washington law (RCW 54).

2. Owens a system and will be ready, willing and able to take power from BPA within a reasonable period of time.

As described more fully in Attachment A, JPUD has entered into a binding agreement to acquire PSE’s facilities in Jefferson County. JPUD has equitable title to the facilities under the APA, and it will assume legal title and full operational responsibility as soon as December 2012 and no later than June 2013. Under the APA, both PSE and JPUD are required to tender a promissory note for \$2,500,000 as liquidated damages for any unexcused failure to close the transaction. Alternatively, either party may seek a court order compelling specific performance by the other party of its contractual obligations. Moreover, there are no “off ramps” in the APA that permit a third-party to unilaterally decide the fate of the transaction; the APA is designed so that JPUD has the ability to correct any regulatory deficiencies in the proposed transaction, insuring that the acquisition will occur. In the unlikely event that the transaction terminates prior to closing, JPUD intends to immediately commence condemnation proceedings.

In order to facilitate an efficient deployment of its electric utility function, JPUD has engaged the services of engineering, financial, and utility consultants:

- Brown & Kysar, Inc. (Engineering)
- Allan Dashen & Associates (Financing)
- Phil Otness (Utility Operations)

JPUD and its consultants have developed both a Utility Development Plan and an Electric System Financing Plan, and those plans are discussed in **Attachment A**, and attached as exhibits.

3. Has general utility responsibility within the service area.

JPUD currently provides water and sewer utility services to over 3500 connected customers throughout Jefferson County. JPUD has the authority under RCW 54 to provide water, sewer, telecommunications, and electric utility services throughout Jefferson County. The citizens of Jefferson County voted on November 4, 2008 to authorize JPUD to offer electric utility services. After cut-over from PSE's operations, JPUD will be the exclusive electric utility provider in eastern Jefferson County and will be responsible for billing its customers for electric service.

4. Has the financial ability to pay BPA for the Federal power it purchases.

JPUD has the authority to collect money for the utility services it now provides to its customers. JPUD has been a sewer and water utility for many years. After cut-over from PSE's operations, JPUD will be also billing and collecting fees and charges from approximately 18,000 electric customers. The ability to expand and enhance the current billing and collection functions of the utility to incorporate the electric utility customers will be implemented during the Transition Period. The amounts collected will be used to pay for power supply and services purchased from BPA.

5. Has adequate utility operations and structure.

JPUD has been an operating water and sewer utility for over 30 years. With the assistance of Brown and Kysar, Inc. and Phil Otness, JPUD has developed a plan for implementing its electric utility function and integrating that function with its existing water and sewer utility functions. This plan is included as an exhibit to Attachment A.

6. Is able to purchase power in wholesale amounts

JPUD intends to rely on BPA for its entire power supply requirements. The average annual load for its estimated 18,000 customers is estimated to be approximately 38 to 40 aMW.

JPUD complies with BPA's Standards for Service and will be ready, willing, and able to take power and fully comply with the terms of a negotiated contract for purchase of power by a reasonable date agreed to by both JPUD and BPA.

**JPUD's Goal is to Qualify for Tier 1 Power in BPA's Next Rate Period**

JPUD is aware that under the "Long-Term Regional Dialogue Final Policy," BPA is implementing a new Tiered Rate Methodology (TRM) that will go into effect in October of 2011. Under the TRM, all public customers that become eligible to purchase PF power after December 1, 2008 will have their Contract High Water Mark (CHWM) calculated through the procedures for new publics described in section 4.1.6 of the TRM. Section 4.1.6.2 provides that a "new public" with a forecast load of 10 aMW or greater:

*Must provide binding notice to BPA by the earlier of three years before the date on which service to the New Public at Tier 1 Rates is to begin or July 1 of the Forecast Year to receive a Contract High Water Mark for the next Rate Period.*

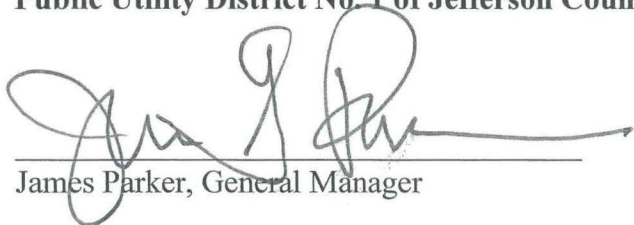
JPUD understands that it must meet BPA's Standards for Service and have taken the necessary steps to enter into a BPA Regional Dialogue power sales contract in order to provide BPA with the "binding notice" required by the TRM. JPUD is ready to enter into a binding power supply agreement. For this reason JPUD proposes to indemnify BPA for any costs BPA incurs should JPUD fail to meet the intended service connection date identified in its power supply agreement with BPA. It is JPUD's goal to receive a CHWM for the 2012-2014 Rate Period. JPUD wants to have its loads served from the current 50 MW reserved for new publics.

**Request for Power**

JPUD hereby requests that BPA offer JPUD a power purchase contract at its earliest convenience and for joint execution on or before July 1, 2010. Please contact JPUD's General Manager, James Parker (360-385-5800 Ext. 307) should you have any questions or desire further information.

Sincerely,

**Public Utility District No. 1 of Jefferson County**



James Parker, General Manager

cc w/ Attachments:

Scott Coe, BPA  
Tim Johnson, BPA  
Tom Miller, BPA  
Scott Wilson, BPA  
Shannon Greene, BPA  
Mark Gendren, BPA

**Attachment A:**

Discussion in Support of Jefferson County's Request for Determination of Eligibility under BPA's Standards for Service, with Exhibits 1 through 11.

**List of Exhibits to Attachment A:**

- Exhibit 1: Asset Purchase Agreement Between Public Utility District No. 1 Of Jefferson County And Puget Sound Energy Company, Inc.
- Exhibit 2: Resolution Of The Board Of Commissioners Of Public Utility District No. 1 Of Jefferson County Approving The Asset Purchase Agreement With Puget Sound Energy, Inc.
- Exhibit 3: Electric Utility Development Plan, prepared by Brown & Kysar, Inc.
- Exhibit 4: Electric System Financing Plan, prepared by Allan Dashen & Associates
- Exhibit 5: Jefferson County Auditor Certified Results of November 5, 1940 Election Showing Voter Approval and Formation of JPUD
- Exhibit 6: Resolution #1 of JPUD, "Rules Governing the transaction of business by the Commission" (December 28, 1940).
- Exhibit 7: General information regarding the current JPUD Board of Commissioners and Districts
- Exhibit 8: Jefferson County Auditor Certified Results of November 4, 2008 Election Authorizing JPUD to Acquire Electric Facilities
- Exhibit 9: Jefferson County Board of Commissioner's Grant of Non-Exclusive Franchise to JPUD.
- Exhibit 10: Letter from Scott Coe of BPA to JPUD dated November 9, 2009

## ATTACHMENT A



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- Exhibit 10: Letter from Scott Coe of BPA to JPUD dated November 9, 2009

## SUPPORT FOR JPUD's REQUEST FOR DETERMINATION OF ELIGIBILITY UNDER BPA's STANDARDS OF SERVICE

This attachment supplements Public Utility District No. 1 of Jefferson County's (JPUD) letter of June 14, 2010 requesting a determination of eligibility under Bonneville Power Administration's (BPA) Standards for Service. JPUD presents this attachment to provide BPA with additional detailed support and analysis for its determination that JPUD demonstrates compliance with BPA's Standards for Service and is eligible to receive power from BPA as a newly formed public utility.

### Background

Under the Northwest Power Act (the Act), any requesting "public body," has a legal right to purchase low cost power from the Bonneville Power Administration, and is entitled to both preference and priority for purchase of that power pursuant to sections 4 and 5 of the Bonneville Project Act of 1937. 16 U.S.C. §§ 832c and 832d. The Act requires the BPA to "offer to sell [its power] to each requesting public body," but "only if the public body \* \* \* complies with the Administrator's Standards for Service in effect on December 5, 1980, or as subsequently revised." 16 U.S.C. 839c(b)(1) and 839c(b)(4). BPA issued its current policy on "Standards for Service" on January 13, 2000 (hereinafter Standards for Service or SFS Policy) based on a lengthy Record of Decision issued by BPA on December 22, 1999 (hereinafter SFS ROD).

On June 11, 2010, Public Utility District No. 1 of Jefferson County entered into a binding Asset Purchase Agreement (APA) for the purchase of all electrical utility system assets, facilities, and properties that Puget Sound Energy (PSE) currently uses to provide electrical service to PSE customers located in Jefferson County, Washington. *See Exhibit 1* (Asset Purchase Agreement between PSE and JPUD). Immediately thereafter, the JPUD Board passed a resolution authorizing execution of the APA with PSE and directing General Manager Jim Parker to request service from BPA and commence utility development operations, including rate design. *See Exhibit 2* (June 11, 2010 Resolution of JPUD Board of Commissioners). By letter dated June 14, 2010, JPUD has formally requested service from BPA as a newly formed "public." JPUD submits this discussion to support its request to BPA for a determination that it meets each of the six criteria identified in BPA's SFS Policy.

The six Standards for Service set forth in BPA's SFS Policy each relate to distinct issues, but together the SFS serve the general purpose of insuring that the benefits of low cost federal power reach the citizens of the Pacific Northwest and that a prospective purchaser has the financial and operational ability to meet its commitments to its customers and BPA under a power purchase contract. JPUD meets BPA's Standards for Service. The following discussion demonstrates that JPUD will be ready, willing and able to take power and fully comply with the terms of a negotiated power purchase agreement within a reasonable period of time.

**I. JPUD is eligible for BPA preference power because it is a “public body” and it meets BPA’s Standards for Service.**

In determining whether or not a potential BPA customer is eligible to purchase federal power, BPA considers whether the customer:

- Was legally formed in accordance with local, state, Federal or tribal laws;
- Owns a distribution system and will be ready, willing and able to take power from BPA within a reasonable period of time;
- Has a general utility responsibility within the service area;
- Has the financial ability to pay BPA for the Federal power it purchases;
- Has adequate utility operations and structure; and
- Is able to purchase power in wholesale amounts.

See BPA, *Policy Decision Regarding Bonneville Power Administration’s Standards for Service*, and (January 13, 2000). For the reasons explained below, JPUD meets each of these standards and therefore qualifies for BPA service.

**A. LEGAL FORMATION (Standard for Service #1).**

The first of BPA’s six Standards for Service requires that the entity requesting BPA power be “legally formed in accordance with local, state, Federal or tribal laws.” JPUD meets this standard. JPUD is a “public utility district” legally formed in accordance with applicable Washington law.

In 1930, the voters of Washington enacted a law, now codified as RCW 54, authorizing the establishment of public utility districts to “conserve the water and power resources of the State of Washington for the benefit of the people thereof, and to supply public utility service, including water and electricity for all uses.” In full compliance with the procedures of RCW 54.08.060, the voters of Jefferson County considered a proposition for the formation of a public utility district for water and electrical service on December 28, 1940. The voters of Jefferson County approved the proposition, which included identification of the boundaries of the proposed district and the election of the first three PUD commissioners. See **Exhibit 3** (Jefferson County Auditor certified results of 1940 election results showing voter approval and formation of PUD).

JPUD has a board of three elected commissioners who serve six-year terms. All business before the PUD Board of Commissioners is conducted pursuant to RCW Title 54.04, generally, and Resolution No. 1, as well as Washington public meeting laws. See **Exhibit 4**. The current PUD Board consists of Commissioners Ken McMillen (President), Barney Burke (Vice President) and Wayne King (Secretary). See **Exhibit 5** (Information regarding current Commissioners districts/terms).

JPUD had continuously served as a water and sewer district for almost 30 years when, in November 2008, the voters of Jefferson County voted to authorize JPUD to “construct or acquire electric facilities for the generation, transmission or distribution of electric power.” RCW

54.08.070. A majority of the voters voted in favor, and JPUD was thereby granted the authority to construct or acquire electric facilities. *See Exhibit 6* (Jefferson County Auditor certified results of November 4, 2008 election). On June 11, 2010, the JPUD Board passed a resolution authorizing execution of the APA with PSE and directing Jim Parker to request service from BPA and commence utility development operations and acquire long-term financing. *See Exhibit 1.*

**B. OWNERSHIP OF DISTRIBUTION SYSTEM (Standard for Service #2).**

The second of BPA's six Standards for Service requires that the entity requesting BPA power "owns a distribution system and will be ready, willing and able to take power from BPA within a reasonable period of time." JPUD believes that it already meets this standard as it applies to newly forming public bodies, and will necessarily have full legal title to the distribution system prior to taking any power from BPA.

**1. Statutory Source and Public Policy for "Ownership" Requirement.**

A new public entity such as JPUD will not be able to acquire (or condemn) significant electric facilities without having qualified for long-term debt to finance the purchase of those facilities. Any lenders involved with utility facility acquisition will require proof of a revenue stream (to pay debt requirements) before they will agree to finance a public entity's purchase of electric facilities. Essentially, in order to prove it is credit-worthy, the new public entity must have a Power Purchase Agreement in place. Thus, the normal commercial cycle is: (i) acquire the facilities; (ii) obtain a power supply; and (iii) secure long-term financing. If BPA, the federal agency directed to sell low-cost federal power to public entities, required a new public be to demonstrate "complete ownership" (*i.e.*, full title to the electric facilities) before offering the power purchase agreement that the new public needs to get financing to purchase the facilities, any new public entity would inevitably fail.

Fortunately for public entities wishing to enter the electric utility business, both Congress and BPA have recognized that--when applied to newly forming public bodies--the "ownership of distribution" standard must be applied with care, so that the newly forming public entity has an opportunity to succeed.

In BPA's Policy Decision Regarding Bonneville Power Administration's Standards for Service, BPA explains that its requirement that "prospective BPA purchasers own the distribution facilities necessary and used to deliver federal power to the purchaser's retail consumers" arises from section 4c(c) and 4c(d) of the Bonneville Project Act, which provide as follows:

*4c(c) Allowance of time for financing*

*An application* by any public body or cooperative for an allocation of electric energy ***shall not be denied***, or another application competing or in conflict therewith be granted, to any private corporation, company, agency, or person, ***on the ground that any***

*proposed bond or other security issue of any such public body or cooperative, the sale of which is necessary to enable such prospective purchaser to enter into the public business of selling and distributing the electric energy proposed to be purchased, has not been authorized or marketed, until after a reasonable time, to be determined by the administrator, has been afforded such public body or cooperative to have such bond or other security issue authorized or marketed.*

4c(d) *Congressional declaration of policy; allowance of time for creation and organization*

It is declared to be the policy of the Congress, as expressed in this chapter, to preserve the said preferential status of the public bodies and cooperatives herein referred to, and to give to the people of the States within economic transmission distance of the Bonneville project reasonable opportunity and time to hold any election or elections or take any action necessary to create such public bodies and cooperatives as the laws of such States authorize and permit, *and to afford such public bodies or cooperatives reasonable time and opportunity to take any action necessary* to authorize the issuance of bonds or to arrange other financing necessary to construct or acquire necessary and desirable electric distribution facilities, *and in all other respects legally to become qualified purchasers and distributors of electric energy available under this chapter.*

16 U.S.C. §§ 832c(c) and (d) (emphasis added). By requiring distribution ownership as a standard for service, BPA is assured that it "sells power consistent with the legal requirement that federal power be sold to customers engaged in the public business of buying and distributing power through distribution facilities owned by the customer." BPA SFS Policy at 5. BPA wants the benefits of low cost federal power to flow to the citizens of the Northwest. The citizens of Jefferson County are aligned with BPA in that respect. BPA further explains on page 5 of the SFS Policy:

*"For newly forming public body and cooperative utilities, BPA must give the applicant a reasonable opportunity to achieve ownership, including time needed to finance the acquisition or construction of the necessary distribution."*

(Emphasis added.) BPA has consistently demonstrated its commitment to this Congressional directive (e.g. exception to "ownership" requirement for tribal utilities, as discussed in BPA's SFS ROD and the request for power by Emerald PUD

**2. JPUD's Ownership of the Distribution System under the APA.**

Under the terms of the APA, PSE has agreed to sell and JPUD has agreed to buy all of PSE's right and title to "all electrical utility system assets, facilities, and properties (including real property) that, as of the Closing Date, PSE uses to provide electrical service to PSE customer located in Jefferson County, Washington \* \* \*" for a total purchase price of \$103,000,000. See **Exhibit 1**. The Closing Date is a date selected by JPUD. JPUD will be spending the interim time implementing its electric utility function (Transition Period). The Closing Date must occur no earlier than eighteen (18) months, or not later than thirty-six (36) months from the APA Effective Date of June 10, 2010.

Any transaction of this nature would normally be subject to conditions which must be satisfied or waived prior to Closing. This transaction is no different. There are standard conditions the parties must meet prior to the closing and the takeover by JPUD as provider of electric utility service for Jefferson County. In order to assist BPA in understanding the structure and certainty provided by the APA, the next two sections provide an overview of the relevant conditions in the APA.

**a. Conditions to JPUD's Performance under the APA.**

The Conditions Precedent to the Closing of JPUD's purchase of PSE assets are set forth in sections 7 and 8 of the APA. With respect to JPUD and the conditions it must satisfy prior to being able to consummate the transaction, JPUD must: (i) obtain long-term financing in an amount and cost with which it is fully satisfied; and (ii) determine that the facilities being purchased are not contaminated. These contingencies are commercially routine for an entity acquiring a substantial asset. The majority of the conditions are standard given the nature of the agreement (e.g. no litigation pending, verification of asset value by 3<sup>rd</sup> party, delivery of purchase price to Escrow Agent). JPUD sees no reason for any of these conditions not to be met on a timely basis. The conditions relating to long-term financing and environmental due diligence are described the following two paragraphs.

**b. Long-Term Financing.**

JPUD's obligation to purchase PSE's assets arises when the conditions described in Sections 8.1 through 8.7 of the APA have been fulfilled.

The most significant condition precedent to JPUD's performance is that "JPUD shall have obtained Long Term Financing, on terms and conditions satisfactory to JPUD, within thirty-six (36) months from the Effective Date of the APA. JPUD is already well-positioned to satisfy this standard. See **Exhibit 7** (JPUD's "Electric System Financing Plan," which includes a letter from RUS acknowledging that JPUD qualifies for RUS financing). As noted earlier, the utility must acquire the facilities and secure a power supply agreement before a financing entity will consider providing any funding. JPUD must acquire adequate funding before it is able to complete the purchase of the assets and have the transaction close.

**c. Due Diligence.**

Under section 2.9 of the APA, JPUD is entitled to perform due diligence activities. If, in the course of its due diligence, JPUD were to develop information suggesting that any of the representations or warranties made by PSE in the APA are not “true or correct in all material respects,” JPUD has the right to terminate the Agreement under Section 12.1 of the APA if, as a result, “the transactions contemplated by this Agreement presents an unanticipated and previously unknown material risk to JPUD.” During the Transition Period, JPUD will have access to all of PSE’s environmental records and be able to survey the facilities and property for environmental conditions. While JPUD understands that it is purchasing utility property and facilities, this contingency is simply prudent business judgment should an untenable environmental situation be discovered.

**d. Conditions to PSE’s Performance under the APA**

There are several “conditions precedent” to PSE’s obligation to perform under the APA. Because PSE (a regulated investor-owned utility) is regulated by both state and federal agencies, the parties necessarily had to provide for some level of regulatory oversight in the APA. Despite the fact that the Washington Utilities and Transportation Commission (WUTC) does not have authority to approve the terms of the purchase by JPUD (RCW 80.12.020(2)), the resolution of certain WUTC issues was important to PSE. It is important to note that, where necessary, JPUD was able to negotiate the ability to cure any issues that could be legitimately raised by the WUTC. In the APA, JPUD has the legal right to decide whether to resolve or cure issues that arise in order for PSE to obtain the requested WUTC determinations. *See* Section 7.2 of the APA. Consequently, the WUTC is not in unilateral control of the viability of the transaction.

With respect to federal oversight, some of the facilities being purchased by JPUD appear to fall under the jurisdiction of the Federal Energy Regulatory Commission (FERC). The parties could not avoid this contingency that FERC, must approve this transaction. Importantly, FERC is looking at these types of transaction in the light of market power concerns that could come into play when generation and or large amounts of transmission facilities are involved. Neither is the case with this transaction and, while both parties considered the approval by FERC to be necessary, the approval is more of an administrative matter under the circumstances at hand and thus neither PSE or JPUD expect FERC’s approval to be withheld.

**e. Necessary Regulatory Approvals**

PSE’s obligation to sell its assets arises when the conditions described in Sections 7.1 through 7.7 have been fulfilled. Despite the fact that PSE has agreed to this sale under threat of condemnation by JPUD, section 5.4 of the Agreement requires PSE to “use its reasonable best efforts to effectuate the transactions contemplated by the Agreement, including, without limitation of the foregoing, promptly making application for Necessary Approvals \* \* \*.”

As noted above, PSE is an electric utility regulated by both the WUTC and FERC. Although Washington law provides that the sale of a public service company’s assets to a public utility district does not require WUTC approval, RCW 80.12.020(2), and federal oversight will



likely be minimal, some form of review of PSE's actions by these regulatory bodies must occur. Therefore, under the APA, PSE must apply for and receive two "Necessary Approvals": (1) a WUTC Order containing the "WUTC Confirmations" described in the APA; and (2) an order from FERC approving the transactions set forth in the APA, if and as required for the transfer of any FERC-jurisdictional facilities that are part of the PSE Assets.

JPUD believes the necessity for these confirmations is a result of the amount of time since the last municipalizations in the state of Washington (over 60 years). For the following reasons, neither of these "Necessary Approvals" presents significant or substantial barriers to fulfillment.

**f. WUTC Confirmations**

Under the APA, PSE is required to ask the WUTC for three different confirmations. This section describes each in turn.

First, PSE is required to ask the WUTC to issue an order confirming that \$103 million is an amount sufficient to fully compensate PSE customers for the sale of the assets. Based upon JPUD's own analysis, the amount that is being paid is well within the reasonable range of purchase prices and therefore JPUD has no concern regarding this condition. PSE apparently seeks this confirmation to avoid payment of any additional amounts should the WUTC believe that PSE did not receive adequate compensation for its facilities. Importantly, JPUD can adjust the purchase price should it deem it necessary and prudent under the terms of Section 7.2.

Second, PSE is required to ask the WUTC to confirm that the transition plan provided for in the APA is consistent with PSE's public service obligations. The Transition Period in the APA allows PSE to operate the Jefferson County facilities until JPUD provides notice that it will assume all the responsibilities of providing electric service. There should be no issue with the manner in which PSE operates in the view of the WUTC as PSE remains responsible for its service obligations until the moment JPUD actually takes over.

Third, the APA requires PSE to ask the WUTC to issue an order confirming that WUTC approval of this transaction is *not* required prior to PSE's transfer of assets to JPUD. Given the plain language of the relevant Washington statutes on this point, the WUTC should provide the desired confirmation.

The WUTC has regulatory oversight over many aspects of PSE's business in Washington. RCW 80.12.020, in particular, provides that a public service company like PSE shall not "sell, lease, assign or otherwise dispose of the whole or any part of its franchises, properties or facilities whatsoever \* \* \* without having secured from the commission an order authorizing it to do so." If the law said nothing further, it would be clear that PSE *would* need WUTC approval in order to sell its Jefferson County facilities to JPUD. However, subsection (2) of RCW 80.12.020 expressly provides that "this section shall *not apply* to any sale, lease, assignment or other disposal of such franchises, properties or facilities to a *special purpose district as defined in RCW 36.96.010 \* \* \**" (emphasis added). The term "special purpose district," in turn, is defined as "water-sewer districts, fire protection districts, port districts, *public utility districts* \* \*

\*." RCW 36.96.010 (emphasis added). Thus, Washington law is clear that a public service company's sale of assets to a public utility district does *not* require WUTC approval. *See Roehl v. PUD No. 1 of Chelan County*, 43 Wash 2d 214, 261 P.2d 92 (1953) (affirming that an earlier version of RCW 80.12.020 did not require WUTC approval of a public service company's sale of assets to a PUD (or group of PUDs)).

**g. FERC Approval**

Section 203 of the Federal Power Act provides, in relevant part, that “no public utility shall, without first having secured an order of the Commission authorizing it to do so – (A) sell, lease, or otherwise dispose of the whole of its facilities subject to the jurisdiction of the Commission, or any part thereof of a value in excess of \$10,000,000.” 16 U.S.C. § 824b.

Section 203 essentially provides that FERC is required to approve a disposition of assets, so long as it (1) is consistent with the public interest; and (2) will not result in cross-subsidization of a non-utility associate company or the pledge or encumbrance of utility assets for the benefit of an associate company. *Id.* Pursuant to authority granted to FERC by 203(5), FERC has adopted regulations that specify criteria for a transaction that will normally meet the standard for approval. FERC's analysis, under its Merger Policy Statement, of whether a disposition is consistent with the public interest generally involves consideration of three factors: (1) the effect on competition; (2) the effect on rates; and (3) the effect on regulation. To the extent that any of the PSE Assets that JPUD is purchasing are, in fact, FERC-jurisdictional facilities requiring FERC approval of the transaction, it is extremely unlikely that FERC would not approve the transaction as none of the issues that FERC is concerned with are present in this transaction.

**h. If Necessary, JPUD Can Require Specific Performance or Condemn**

Under the APA, PSE and JPUD are each required to tender a promissory note in the amount of \$2,500,000 payable to the other party, as liquidated damages for the unexcused failure to close the transactions contemplated by this Agreement. In lieu of the liquidated damages, either party may instead seek a court order compelling the non-performing party to perform. The liquidate damages amount is there to serve as a deterrent to bad acts and the specific performance provision is designed to assure the deal is consummated.

PSE does have a right to termination under the APA under certain limited circumstances (see 12.1), but “upon termination, JPUD shall be immediately free to initiate or proceed with any condemnation or other action to acquire the PSE Assets.” JPUD has the power of eminent domain, RCW 54.16.020, which allows it to acquire the distribution facilities through condemnation should such action be necessary. As evidenced in the Resolution of the JPUD Board of Commissioners, JPUD will not hesitate to proceed with condemnation proceedings to abide by the will of the voters of Jefferson County should this transaction be terminated for some reason.

### **3. BPA Ownership Standard Applied to JPUD Facts**

JPUD will own a distribution system and be ready, willing, and able to take power from BPA no later than June 9, 2013, the date on which BPA will deliver power to JPUD under a Regional Dialogue Power Purchase Agreement. As the foregoing discussion demonstrates, JPUD is engaged in the serious and deliberate implementation of its electric utility function. Indeed, JPUD is moving forward in a deliberate, cost-effective manner in accordance with prudent utility practices. JPUD has equitable title to the facilities and will achieve legal title through the Transition Period. JPUD meets BPA's ownership standard for newly forming publics.

#### **C. GENERAL UTILITY RESPONSIBILITY (Standard for Service #3)**

JPUD currently has a general utility responsibility within the Jefferson County service area. It currently provides water service to over 3500 connections throughout Jefferson County, and maintains a franchise with Jefferson County for both water and sewer utility functions. *See Exhibit 8* (Copy of Jefferson County Board of Commissioner's Grant of a Non-Exclusive Franchise to JPUD). JPUD is an established utility with all the responsibilities and authorities related to that operation. In addition to normal operational activities of billing, customer interface, and system operations, JPUD also complies with state audits of its operations on a two year cycle, prepares quarterly and annual reports, and creates annual budgets.

More information on JPUD, as it currently exists, can be found at its web site including information on rates for its water and sewer utility functions. *See* <http://pud.co.jefferson.wa.us>. JPUD's plan for moving forward with the implementation of its electric utility function is shown in the Utility Development Plan. *See Exhibit 3* (Utility Development Plan).

#### **D. ABILITY TO PAY FOR BPA POWER (Standard for Service #4)**

This standard requires that an applicant have the authority to collect money for services it renders to a retail consumer, and in turn pay for power provided by BPA. JPUD has been water utility for over 30 years with over 3500 connections and another 300 sewer connections. JPUD charges and collects for its utility services on a monthly basis.

JPUD will have to use long term debt in order to finance the acquisition and start-up of a new public power utility. Attached documents show that JPUD can both finance and operate a new power utility. JPUD has received acknowledgement from RUS that it qualifies for RUS financing for the purchase and initial costs to serve power in Jefferson County. *See Exhibit 9* (Electric Utility Financing Plan). According to RUS, its application and approval process could take over 2 years to fund the acquisition and operations of the system.

During the Transition Period, JPUD will be taking all measures necessary to safeguard its investment through the hiring of key individuals, contracting of services and participating with PSE in the decision making process for system operations. Additionally, JPUD has taxing authority and in the past has used it for regional water, power, and telecom purposes.

## **E. UTILITY OPERATIONS AND STRUCTURE (Standard for Service #5)**

The PUD has been in operations as a water and sewer utility for over 30 years. It currently has approximately 3500 connections to the water systems (a number of which are also sewer customers). The PUD water system facilities are located throughout the county, with the bulk of them in the current PSE power service area. The PUD currently has all the elements established to meet the requirements of operating an electric power utility: billing, administrative, field personnel, and management already exist for the PUD's water, sewer, and telecom roles. Over the past 18 months, JPUD has been investigating how best to organize to meet the challenges of operating a power utility. In general, the utility backbone already exists for the management to run the electric service side of the PUD. As discussed in greater detail in **Exhibit 3**:

- JPUD will use existing PSE facilities already in place and fully operational (including PSE headquarters)
- JPUD will use BPA as its exclusive power/ transmission supplier.
- JPUD will continue to use Brown and Kysar as consulting engineers.
- JPUD will use local contractors and suppliers whenever practicable (e.g. for maintenance, grounds, receipt collections)
- JPUD may initially contract out some system maintenance tasks, such as tree-trimming and substation maintenance/testing.
- JPUD will expand its existing billing system and continue to contract out the bill mailing.
- JPUD will employ a limited number of servicemen and supplement them with two line crews and the corresponding supporting staff – groundmen, metermen, operation managers, engineers.

In order to meet the requirements of operating an electric utility, the PUD will use an organizational chart similar to the organizational chart set forth in **Exhibit 3**. During the Transition Period, in addition to the continued use of our consultants, we will be expanding our existing organizational structure by hiring key personnel. During the Transition Period, JPUD also expects to enter into intergovernmental agreements with both the Clallam and Mason PUDs to assist each other in times of need. JPUD will establish policies and procedures similar to those used by other PUDs, but will also take into consideration existing PSE policies and the needs of the citizens of Jefferson County, where appropriate. As a community-based utility, JPUD will seek input from the citizens of Jefferson County as it continues the process of implementing its electric utility function.

**F. JPUD is able to purchase power in wholesale amounts.**

JPUD plans to initially receive all its power requirements from BPA. JPUD's current engineering estimates are that the load it will serve is approximately 38 to 40 average annual MW, with a peak of 80 MW. JPUD representatives have met with the BPA Transmission Group and are in the process of completing an application for BPA transmission service. The BPA Transmission Group requires a utility to have a power supply agreement before it will undertake any substantive analysis.

**II. CONCLUSION**

As demonstrated by the foregoing discussion, JPUD will be ready, willing and able to take power and fully comply with the terms of a negotiated power purchase agreement within a reasonable period of time. JPUD therefore requests that BPA issue a determination that JPUD has met its Standards for Service, together with an offer of a power supply agreement. As time is of the essence, please do not hesitate to contact Jim Parker, General Manager, with any questions or concerns regarding JPUD's request for service.