



PUGET  
SOUND  
ENERGY

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PETITION DEPARTMENT  
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STATE OF WA  
UTIL. AND TRANSP.  
COMMISSION

Via Messenger

March 16, 2000

Washington Utilities and  
Transportation Commission  
Attention: Carole J. Washburn, Secretary  
1300 S Evergreen Park Drive SW  
Olympia, WA 98504-7250

Re: Docket No. UE-991409

Dear Ms. Washburn:

Enclosed you will find an original and 19 copies of Puget Sound Energy's Petition for Reconsideration and Clarification.

Concurrent with this filing, we have served copies of all documents on all parties. A Service List is enclosed.

Sincerely,

Christy A. Omohundro  
Director, Rates & Regulation

Enclosures

cc: See Service List

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STATE OF WASH.  
UTILITY TRANSP.  
COMMISSION

BEFORE THE  
WASHINGTON UTILITIES AND TRANSPORTATION COMMISSION

In the Matter of the Application of

PUGET SOUND ENERGY, INC.,

For (1) Approval of the Proposed Sale of PSE's  
Share of the Centralia Power Plant and  
Associated Transmission Facilities, and (2)  
Authorization to Amortize Gain over a Five-  
Year Period

DOCKET NO. UE-991409

**PETITION FOR RECONSIDERATION  
and CLARIFICATION**

**I. INTRODUCTION**

Pursuant to WAC 480-09-810, Puget Sound Energy, Inc. ("PSE") hereby petitions the Commission for reconsideration and clarification of its Second Supplemental Order in this proceeding ("Order"), which approved the sale of the Centralia Power Plant with conditions. The Order, among other things, recognizes that:

- "The ratepayers and the utilities incur risks and benefits whether or not the plant is sold."
- "In this particular transaction, both ratepayers and shareholders have and will incur risks and burdens."
- In determining the fair allocation of the proceeds from the sale, utilities should not be inhibited from "pursuing opportunities beneficial to both ratepayers and shareholders."

PSE appreciates that in fashioning the conditions to be imposed in connection with the sale, the Commission was attempting to produce an outcome consistent with its stated objective to

avoid inhibiting utilities from “pursuing opportunities beneficial to both ratepayers and shareholders.”

In the case of PSE, however, the conditions attached to the proposed sale provide a significant disincentive to PSE proceeding with the sale. With the accounting treatment prescribed in the Order, and the additional power costs PSE will pay in the short term as a result of the sale, PSE will actually be harmed by proceeding with the transaction, as discussed below. This outcome, which is exacerbated by the treatment for financial reporting purposes of the carrying costs to be accrued for PSE’s customers, may not have been anticipated by the Commission.

By this Petition, PSE seeks (1) clarification of the method by which the gain was calculated in the Order, (2) clarification that PSE is not required to defer its allocated share of the gain, and (3) a modification of the Order’s prescribed accounting treatment to eliminate the requirement that PSE pay a carrying cost of 7.16% on the portion of the gain allocated to customers. PSE also seeks clarification of two other points in the Order regarding (1) any requirement imposed on PSE to file a general rate case by a date certain and (2) the precedent to be accorded this transaction in considering other asset sales.

### **REQUEST FOR RECONSIDERATION AND CLARIFICATION**

#### **A. The Commission Should Clarify that the Gain from the Sale is Calculated After Reflecting Taxes and Sale Expenses.**

Paragraph 65 of the Order states that:

Gain on the sale of an asset is a straightforward calculation. It results when the sale price exceeds the net book value (original cost less accumulated depreciation) of the asset(s), *plus any additional costs of the sale.*

It is clear from the Order’s definition of “gain” that any additional costs of the sale must be taken into account in the calculation of the gain on the sale of the Centralia plants.

However, Tables 4 and 5 in the Order do not deduct transaction costs in illustrating the allocation of gain between customers and shareholders. Moreover, Table 5 assumes a tax rate which is lower than the Company's actual tax rate for this transaction. In Attachment 1, the Company has calculated the net gain allocation applying the actual tax rate and estimated sale costs. This calculation reduces the amount of the net after-tax gain allocated to the Company's shareholders to \$1.42 million, compared to the \$2.08 million amount found in Table 5 of the Order. The Company requests that the Commission in its reconsideration order confirm that the calculation in Attachment 1 is correct, or provide a calculation of its own which reflects the actual tax rate and the deduction of transaction costs, as estimated by PSE.

**B. The Commission Should Clarify that PSE Is Not Required to Defer Its Allocated Share of the Gain.**

The Order sets forth an explicit allocation of the gain on the sale of the Centralia plants. The Order requires PSE to recalculate the gain on the sale to match the date that the sale closes, and to provide such calculation to the Commission. (Paragraph 162). There is some ambiguity in the Order, however, regarding *when* PSE can recognize its allocated share of the gain, inasmuch as the Order in some places appears to require *all* gain to be deferred.

PSE requests that the Commission clarify that PSE is not required to defer its allocated share of the gain. The customers are not harmed by PSE booking its allocated share at the time that the sale closes. At the same time, if PSE is required to defer the gain, the practical effect would be to deny shareholders *any portion of the gain*, a result that appears to be contrary to the objectives of the Order.



**C. The Requirement That PSE Pay a 7.16% Carrying Cost on Customers' Portion of the Gain Should be Eliminated.**

The Order requires PSE to defer the customer's allocated share of the gain and to pay carrying costs on the deferred amount until its next general rate proceeding. PSE requests that the Commission reconsider the carrying cost requirement imposed in the Order. The basis for imposing such a requirement is not clear from the Order. It apparently springs from the notion that PSE "owes" its customers this share of the gain, and therefore must pay interest on the customers' portion of the gain so long as PSE "keeps" the proceeds. Such an approach may have been appropriate if this were a general rate proceeding, where rate base can be adjusted to reflect, on the down side, the elimination of the Centralia asset and, on the upside, all the other capital investments which PSE has undertaken to meet its obligations to serve customers.

During the years 1997, 1998 and 1999, for example, PSE has invested more than \$595 million in capital additions, net of retirements, to electric utility rate base to meet its obligations to serve its growing customer base and to provide high quality, reliable service. PSE has not asked that rate base be adjusted between rate cases to reflect these new plant additions. The notion that PSE "owes" its customers money due to a single-item rate base adjustment fails to recognize the significant additions to rate base made by PSE during the Rate Plan.

Moreover, the portion of the gain due to be "returned" to PSE's customers will be reinvested by PSE in utility rate base items. Rate base will not be adjusted for this investment until rates are reset in the next general rate case. There is no windfall to PSE by virtue of having access to these funds until PSE's next general rate case. If the Commission is concerned that these proceeds will be used for non-utility purposes or not for the benefit of

PSE's customers, it can impose a condition that PSE shall be required to re-invest in utility rate base the gain from the Centralia Plant sale allocable to PSE's customers.

As corrected in Attachment 1, the amount of the gain allocated to customers is \$12.10 million. Given the 7.16% carrying cost prescribed by the Order, the carrying charge on the deferred amount would be nearly \$1 million per year until PSE's rates are reset in its next general rate proceeding. Although it may not have been anticipated by the Commission in fashioning the conditions set forth in the Order, under generally accepted accounting principles *these carrying costs will result in a current charge against PSE's income for financial reporting purposes*. They are not simply a journal entry to accumulate a capitalized amount to be added to a deferral for later recovery. These costs are an amount which must be recognized as a current expense for financial reporting purposes.

As a consequence of imposing the requirement to pay carrying costs to PSE's customers, PSE's net income each year until its next general rate adjustment will be reduced by the carrying costs. This condition imposes a strong incentive against PSE proceeding with the proposed sale, as *PSE is better off, until its next general rate case, if it retains the Centralia Plant rather than selling it subject to the carrying cost requirement*. Moreover, this consequence arises not from the economics of the transaction itself, which the Order concludes "is consistent with the interest of the ratepayers, shareholders, and the broader public." Rather, the consequence arises from the accounting requirements imposed by the Order with respect to charging carrying costs on the customers' portion of the gain from the sale. Imposing a requirement with this consequence does not appear to be consistent with the stated objective of the Commission to "not inhibit utilities from pursuing opportunities beneficial to both ratepayers and shareholders."

The consequence seems particularly unfair when it is considered that PSE will bear higher power costs during the Rate Plan period if it proceeds with the proposed sale. As

summarized in the Order, using the most recent forecast on the record of the AURORA model of market costs, along with all of Staff's modifying assumptions, PSE is expected to bear at least \$1.1 million in additional power costs during the remaining period of the rate plan if PSE proceeds with the proposed sale. Until power costs for Centralia rise to reflect the costs of required new scrubbers, Centralia costs are expected to be lower than the replacement power costs. Because these higher replacement power costs will be incurred during the Rate Plan period, they will be borne by PSE and cannot be passed through to PSE's customers.

Thus, PSE would be penalized if it proceeds with the proposed sale, which does not represent "an allocation that strikes a fair balance between ratepayers and shareholders." PSE should not be put in a materially worse condition by proceeding with the sale. We urge the Commission to eliminate the requirement in the Order that the deferred gain accrue carrying costs. If this carrying cost charge is eliminated and the Commission makes clear that PSE may book its allocated share of the net gain, the net gain will approximately fund the additional power costs PSE will bear. The end result is that shareholders would not be harmed from the sale (although they will not receive any financial benefits, either). Customers, on the other hand, will clearly benefit since virtually all the gain will be allocated to them.

**D. The Commission Should Clarify That the Order Does Not Impose a Requirement on PSE to File a General Rate Case by a Specified Date.**

The Commission Press Release accompanying the issuance of the Order states that PSE "is required to file for new rates before June 30, 2002." Nowhere in the Order is such a requirement imposed. As the Commission is aware, PSE is operating under a Rate Plan pursuant to the Commission's merger order in Docket No. UE-960195. Although that Rate Plan precludes PSE from filing for a rate increase that would be effective earlier than



December 31, 2001, there is no requirement to file a rate case by a date certain. PSE requests that the Commission clarify that the Order imposes no requirement on PSE to file a general rate case by a specified date. PSE submits that, given the fact that it has already invested more than \$595 million in electric utility net capital additions during the Rate Plan period, requiring the timing of the next general rate case to be governed by a desire to “true up” the relatively small amount deferred by the Order would have the tail wagging the dog.

**E. The Commission Should Clarify that the Order Is Not Precedential with Respect to the Treatment of Gain.**

The Order includes a discussion of the precedent to be accorded to the Order in the case of other asset sales. According to the Order:

In determining the fair allocation of the appreciation, we must consider in particular the uncertain future of the electricity industry and new opportunities for both shareholders and ratepayers in a competitive wholesale generation market. In light of that uncertainty and those opportunities, regulators must be cautious not to apply precedent in a way that could inhibit utilities from pursuing opportunities beneficial to both ratepayers and shareholders. We must be flexible enough to allow managers of regulated utilities to exercise sound judgments regarding the restructuring of their portfolios of assets so as to maximize the value of their entire systems, minimize rates, and best serve both ratepayers and shareholders.

In reaching its conclusion with respect to the Centralia sale, the Commission introduced a number of new concepts, including the analysis of appreciation above original cost and depreciation recapture in determining an appropriate method of allocating the gain from this sale. Some of the concepts discussed by the Commission in reaching its conclusion are novel and raise potentially troubling issues if applied in other contexts. We request that the Commission further clarify in its Order on reconsideration that the rationale and methodologies used in rendering this decision are specific to the Centralia situation; i.e., the allocation methodology and accounting treatment set forth in the Order do not have any



precedential effect on other asset sales.

In subsequent asset sales, the Company should be free to propose and the Commission should be free to adopt a different allocation methodology and accounting treatment based on the facts and evidence presented in such proceeding.

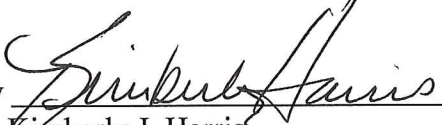
### CONCLUSION

For the foregoing reasons, PSE request that the Commission:

- Clarify that the net gain calculation set forth in Attachment 1 is correct;
- Clarify that PSE is not required to defer its allocated share of the gain;
- Reconsider and eliminate the Order's requirement that PSE pay a carrying cost of 7.16% on the portion of the gain allocable to PSE's customers;
- Clarify that the Order does not impose on PSE a requirement to submit a general rate case filing as a condition of the sale; and
- Clarify that the Order is not precedential on the treatment of gain from other asset sales.

RESPECTFULLY SUBMITTED this 16<sup>th</sup> day of March, 2000.

**PUGET SOUND ENERGY, INC.**

By   
\_\_\_\_\_  
Kimberly J. Harris  
Assistant General Counsel  
WSBA #27480



**Centralia Power Plant Sale  
 Commission Methodology With Corrected Numbers  
 (millions of dollars)**

	Total	Customer	PSE
	(a)	(b)	(c)
1 Sales Proceeds	\$ 33.57		
2 Allocation:			
3 Net book value of plant	\$ 7.98	\$ -	\$ 7.98
4 Book value of fuel and material inventory	1.89	-	1.89
5 Accumulated depreciation	19.05	19.05	-
6 Appreciation (Note 1)	4.65	2.32	2.33
7 Proceeds	33.57	21.37	12.20
8 Less net book value	(9.87)	-	(9.87)
9 Gain before taxes and transaction costs	23.70	21.37	2.33
10 Less cost of transaction (Notes 2 and 3)	(1.45)	(1.31)	(0.14)
11 Total pre-tax gain	22.25	20.06	2.19
12 Total taxes due Note 4)	(9.44)	(8.67)	(0.77)
13 Existing deferred taxes	0.71	0.71	-
14 Net Book Gain (Note 5)	\$ 13.52	\$ 12.10	\$ 1.42

- Note 1 Proceeds of \$33.57 less original cost of \$27.22 and fuel and material inventory of \$1.89
- Note 2 \$.42 scrubber cost overruns, \$.65 costs related to sale and \$.38 loss on fuel and inventory
- Note 3 \$1.45 allocated in proportion to gain before taxes and transaction costs
- Note 4 Reversal of deferred income taxes due to accelerated depreciation assigned to accumulated depreciation component of gain and remaining taxes spread proportionately to remaining gain
- Note 5 Agrees with Exhibit No. 109 (KRK-1) before true ups to actual

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