EXHIBIT NO. ___(RG-1HCT)
DOCKET NO. UE-072300/UG-072301
2007 PSE GENERAL RATE CASE
WITNESS: ROGER GARRATT

BEFORE THE
WASHINGTON UTILITIES AND TRANSPORTATION COMMISSION

WASHINGTON UTILITIES AND TRANSPORTATION COMMISSION, **Complainant,** **v.** **PUGET SOUND ENERGY, INC.,** **Respondent.**	**Docket No. UE-072300** **Docket No. UG-072301**

PREFILED DIRECT TESTIMONY (HIGHLY CONFIDENTIAL) OF ROGER GARRATT ON BEHALF OF PUGET SOUND ENERGY, INC.

REDACTED VERSION

REVISED DECEMBER 21, 2007

Q. Did the Company accept PSRC's original offer?

A. No. PSE and PSRC settled on an asset purchase price of $[redacted] million. *See* Exhibit No. ___(RG-30C) at 6.

Q. What is the portfolio benefit associated with the purchase of Whitehorn Generating Station Units 2 and 3?

A. The portfolio benefit associated with the purchase of Whitehorn Generating Station Units 2 and 3 is $1.9 million. *See* Exhibit No. ___(WJE-1HCT) at 22.

VI. REPLACEMENT POWER AND PURCHASE OPTION OF THE SUMAS NATURAL GAS-FIRED COMBINED CYCLE COGENERATION PLANT

A. Existing Arrangement

Q. Please describe the events leading up to the default by Sumas Cogeneration Company, LP ("SCCLP") under its power purchase agreement with PSE.

A. In Spring 2006, SCCLP notified PSE that SCCLP would not be able to continue supplying energy under the long-term firm PPA with PSE because it was experiencing increasing financial pressures. SCCLP cited a variety of reasons for these financial pressures, including but not limited to high gas prices, increasing royalty costs on Canadian gas reserves, and concerns about meeting debt service coverage. SCCLP proposed the following restructuring of the long term PPA:

(i) SCCLP would sell its existing gas reserves and make a payment of not less than [redacted] to PSE;

(ii) SCCLP and PSE would terminate the existing PPA, PSE would enter into a replacement power purchase agreement, and the parties would split the savings resulting from such replacement; and

(iii) SCCLP would sell the cogeneration plant at a discount to PSE for approximately [redacted].

After several months of consideration, PSE notified SCCLP that the proposed restructuring was not compelling given the level of savings and risk to PSE's customers.

On March 14, 2007, PSE met with Commission Staff and presented the presentation prepared for the EMC meeting the following day to provide an update on the status of these discussions with SCCLP. Please see Exhibit No. ___(RG-32HC) for a copy of the presentation made to Commission Staff regarding PSE's discussions with SCCLP. PSE staff presented the same analysis and information with a revised order to the EMC on March 15, 2007, at which time PSE staff recommended a cessation of further discussions with SCCLP. Please see Exhibit No. ___(RG-33HC) for the presentation made to PSE's Energy Management Committee.

Q. How did the Company learn about SCCLP's default on its long term firm PPA?

A. On May 7, 2007, PSE received a letter from SCCLP, in which SCCLP stated that it would not make further deliveries of electricity to PSE under the PPA after June 30, 2007. Please see Exhibit No. ___(RG-34HC) for the letter from SCCLP. The

"market makers" and one generator. Please see Exhibit No. ___(RG-36C) for the term sheet solicitation. Two of the respondents declined to participate, citing reasons such as an inability to simulate the plant characteristics, complexity of the transaction, and other general contract issues, such as credit requirements. PSE received two responses to its solicitation for replacement power. Of the two proposals that PSE received, the analysis indicated that the cost to the Company to replace the contract on such terms and conditions ranged from $[redacted] million. Please see the prefiled direct testimony of Mr. W. James Elsea, Exhibit No. ___(WJE-1HCT), for a discussion of the projected cost to replace the SCCLP PPA.

Q. What steps did the Company take next?

A. PSE staff notified the EMC of the results of the solicitation. PSE staff then proceeded with replacing the energy as prescribed in the replacement power strategy outlined in the June 11, 2007 EMC meeting. For the long-term replacement (Step 3), PSE staff developed a second term sheet solicitation for a standard block product up to 125 MW with a term of January 1, 2009, through March 31, 2013. Please see Exhibit No. ___(RG-37C) for the term sheet for the standard block product solicitation.

/////

/////

Q. How did the replacement power cost compare with the cost of the remaining value of the SCCLP PPA?

A. PSE was able to replace the power at a cost of approximately $[redacted] than the cost of energy under the SCCLP PPA. Although this lower power cost is beneficial to PSE's customers, this lower price does not address the loss of the inherent dispatch flexibility of the resource or the displacement optionality of the resource. Please see the prefiled direct testimony of Mr. W. James Elsea, Exhibit No. ___(WJE-1HCT) at 28-29, for a discussion of the calculation of the direct damages.

Q. Did the Company discuss damages with SCCLP?

A. Yes. PSE met with SCCLP to discuss direct damages on August 8, 2007. At that meeting, PSE indicated that it may suffer in the range of [redacted] million of direct damages as a result of the SCCLP breach. SCCLP countered that, based on PSE's solicitation and analysis, PSE suffered negligible damages, if any.

After further discussion and negotiation, PSE and SCCLP agreed to pursue a settlement whereby SCCLP would sell the Sumas Cogeneration Station to PSE at a significant discount -- approximately [redacted] or [redacted]. On August 31, 2007, PSE and SCCLP signed a Letter of Intent for the purchase and sale of the Sumas Cogeneration Station. Please see Exhibit No. ___(RG-38HC) for the Letter of Intent between PSE and SCCLP.

C. Acquisition of the Sumas Cogeneration Station

1. Ownership Arrangement

Q. Please describe the Sumas Cogeneration Station.

A. The Sumas Cogeneration Station is an approximately 125 MW natural gas-fired combined cycle generating facility located on an approximately six-acre site within the City of Sumas, Washington. The Sumas Cogeneration Station was developed and constructed by a Washington joint venture formed by Industrial Power Corporation and Haskell Corporation, with HIPP Engineering of Vancouver, British Columbia serving as project engineer. Sumas Cogeneration Station was developed on a greenfield site and achieved commercial operation in April 1993.

The plant consists of one combined cycle train. Primary components of the plant include (i) a GE Frame 7EA model combustion turbine and generator rated at 87 MW, (ii) a Vogt 3-pressure heat recovery steam generator with a total steam output of 370,000 lbs/hr., and (iii) a GE SC2 steam turbine generator rated at 37 MW. The plant's heat rate is [redacted] Btu/kWh and provides heat rate diversity to PSE's natural gas-fired fleet.

The GE 7EA is a mature and proven technology. The GE 7EA model has accumulated millions of hours of service and is well recognized for its high reliability and availability. There are more than 750 units in service worldwide.

Independent data confirms that average reliability is 99% with an availability of 96%. The availability of parts and service is excellent.

The Sumas Cogeneration Station was originally designed for baseload operations, with the entire electrical output of the plant sold to PSE under a 20-year firm PPA. The steam host, which is adjacent to the plant, is a lumber drying plant owned by Socco Forest Products ("Socco"), an affiliate of SCCLP. Exhaust steam from the plant provides the thermal requirements for the lumber dry kilns. An exhaust boiler ensures supply of saturated steam during curtailment events. After acquiring the Sumas Cogeneration Station, PSE will continue to supply steam to the lumber dry kilns under the terms and conditions of a steam supply agreement.

Q. Please describe the electric transmission arrangements for the Sumas Cogeneration Station.

A. The Sumas Cogeneration Station is interconnected to PSE's transmission grid at the Sumas substation. There are two 115 kV overhead transmission lines that direct the output of the plant east and west on PSE's transmission system. The maximum interconnection capacity is 135MW. As a westside resource, the Sumas Cogeneration Station provides a reliable source of power for PSE's customers, particularly during Puget Sound Area Northern Intertie events, in which BPA may require PSE to run the Sumas Cogeneration Station to clear

congestion in the Puget Sound area. Upon closing, the resource will be designated as a network resource to serve PSE's network load.

Q. Please describe the gas transportation arrangements for the Sumas Cogeneration Station.

A. The Sumas Cogeneration Station owns a 3.7 mile, 8 inch, natural gas pipeline that connects the plant with Westcoast's pipeline facilities at the U.S./B.C. border at Huntingdon, British Columbia. There is a pressure reducing gate station, trip valve and condensate facility located on the U.S. side that PSE will maintain as operator of the pipeline.

PSE will own the pipeline as a tenant-in-common with Sumas Pipeline Company and Socco. The capacity of the pipeline is 45,000 Mcf. Of that, PSE's pro rata share will be 57.3%, or 25,785 Mcf per day, with the remaining capacity to be allocated between Sumas Pipeline Capacity (41%) and Socco (1.7%).

To effectuate the change in ownership of the pipeline, PSE, Socco, Sumas Pipeline Company, and SCCLP will file a joint application to amend the Presidential Permit issued to SCCLP in 1991. PSE anticipates that the amendment application will be filed with FERC in December 2007, and the parties estimate that such amendment application will take six to nine months to be approved. In addition to FERC approval, the U.S. Department of State and the U.S. Department of Defense must approve the application. The transaction closing is contingent upon approval of the amendment application.

Q. How will the gas pipeline be operated?

A. PSE will operate the natural gas pipeline. Representatives of PSE, Socco, and Sumas Pipeline Company will establish a management committee to determine policies and procedures for the operation of the pipeline. The management committee will have budget authority for operational and maintenance issues. Each of the parties will contribute based on their pro rata share of the pipeline.

Q. Please describe the fuel supply arrangements for the Sumas Cogeneration Station.

A. Natural gas is the sole fuel supply for the Sumas Cogeneration Station. PSE will manage fuel supply requirements in a manner consistent with the Company's hedging strategies. PSE's operations and trading group will monitor and evaluate the need for additional fuel supplies based on daily updates of its dispatch models.

Q. Please describe PSE's obligations under the steam supply agreement with Socco's lumber dry kiln facilities.

A. PSE will supply steam to the lumber dry kilns when the Sumas Cogeneration Station is operating at PSE's sole election. PSE has no obligation to supply steam to Socco when the station is not operating. When PSE does supply steam to Socco, the dry kiln operation must return condensate to the Sumas Cogeneration Station. Socco has an auxiliary boiler that supplies adequate steam when the Sumas Cogeneration Station is not operating. PSE projects that the auxiliary

boiler will supply much of the steam demand for the lumber operations post closing because of the expected reduced capacity factor of the plant.

2. Due Diligence

Q. Did PSE evaluate the Sumas Cogeneration Station during the RFP?

A. Yes. PSE evaluated the Sumas Cogeneration Station during the RFP post-proposal period. In PSE's updated analysis of the Sumas Cogeneration Station in March 2007, the Company's analysis indicated a portfolio benefit of $32 million, a positive benefit ratio of 0.121, and a levelized cost of [redacted]/MWh (all based on a capital cost of [redacted]). Please see the prefiled direct testimony of Mr. W. James Elsea, Exhibit No. ___(WJE-1HCT), for a discussion of this analysis.

Further, PSE reviewed comparable asset sales for natural gas-fired generation plants to estimate a reasonable purchase price based on adjustment for plant efficiency, vintage, fixed gas transportation and transmission costs. As compared to the other resource alternatives from the short list of RFP projects, the acquisition of the Sumas Cogeneration Station by PSE is reasonable. *See* Exhibit No. ___(WJE-1HCT).

/////

/////

/////

Q. What additional due diligence did PSE conduct with respect to the Sumas Cogeneration Station?

A. The Company conducted a review of legal, commercial, environmental, real estate, insurance, operations and maintenance, and technical concerns related to the Sumas Cogeneration Station.

a. Commercial and Legal Due Diligence

Q. Please describe the commercial and legal due diligence conducted by the Company.

A. The Company and its outside counsel reviewed the various contracts pertaining to the ownership and operation of the Sumas Cogeneration Station. The Company focused on potential liabilities and provisions that could affect the acquisition, such as consents, assignments, and accrued liabilities.

b. Real Estate Due Diligence

Q. Please describe the real estate due diligence conducted by the Company.

A. Real estate due diligence included title review, boundary and easement survey review, and review of legal descriptions and survey documentation related to the fee property acquired and appurtenant and encumbering easements.

As discussed above, the Sumas Cogeneration Station is located within the City of Sumas, Washington. During the due diligence period, SCCLP purchased, in fee,

the property upon which the Sumas Cogeneration Station is located. Previously, SCCLP leased the property from the then-fee owners, the Port of Bellingham. The Port of Bellingham approved the sale of fee property to SCCLP on November 6, 2007.

PSE expects that in December 2007 SCCLP will submit a permit application to the City of Sumas to amend the previously recorded short plat of the property. The amended short plat, once approved, will consist of Lots A, B and C. At closing, PSE will acquire Lot A, the power plant property consisting of approximately 5.54 acres and Lot C, the affiliated substation lot consisting of approximately 0.59 acres.

Q. Are there any easements required in order for the facility to operate?

A. The Sumas Cogeneration Station is served by a series of easements. Utility easements benefiting the plant include a 40 foot wide easement for ingress and egress to and from the Sumas Cogeneration Station. Additional easements appurtenant to the plant include those for industrial and potable water, sanitary sewer, communication lines, electric distribution and transmission lines, and other related operation infrastructure. Additionally, an easement corridor for natural gas pipelines begins at the Canadian border and ends at the south border of the 5.54 acre power plant property.

/////

c. Environmental Due Diligence

Q. Please describe the environmental due diligence conducted by the Company.

A. PSE's environmental due diligence review consisted of site visits, interviews with facility employees, review of all available environmental documentation, including but not limited to review of correspondence with environmental agencies, status of existing environmental permits, Phase I Environmental Site Assessment to support the transfer of ownership and operation of the plant, environmental plans and policies, and regulatory requirements.

Q. Will the Sumas Cogeneration Station require new air permits?

A. Yes. The Sumas Cogeneration Station, under PSE's ownership, will require Title IV (Acid Rain) and Title V (Clean Air Act) permits.

Q. Will these permits require modifications due to the expected lower dispatch rate of the Sumas Cogeneration Station?

A. No. The Company does not anticipate that either the Title IV (Acid Rain) permit or the Title V (Clean Air Act) permit will trigger stricter emission limits, provided that New Source Review (NSR) is not triggered.

/////

/////

Q. Please describe the water supply arrangements for the Sumas Cogeneration Station.

A. The Sumas Cogeneration Station receives its water supply from the City of Sumas pursuant to the 50-year Agreement for Utility Services that expires in 2041. The City of Sumas also provides for industrial wastewater discharge pursuant to an Agreement for Waster Water Utility Services between the City of Sumas and SCCLP. PSE expects SCCLP and the City of Sumas will enter into an Upgrade and Chemical Treatment Agreement in December 2007, in which SCCLP will agree to fund construction and operation of an upgrade to the City's treatment plant. The installation of this chemical injection system will treat the formation and buildup of bacterial growth before discharge to the City of Abbotsford, British Columbia, at the site where the City of Abbotsford and Fraser Valley Regional District of British Columbia treat and dispose of the City of Sumas's sewage. SCCLP estimates that the installation of the injection equipment will be completed by December 31, 2007. Additionally, SCCLP, the City of Sumas and the City of Abbottsford will enter into a Payment and Release Agreement in December 2007 to ensure full payment to the City of Abbottsford for extraordinary sewer system cleaning services rendered.

At closing, SCCLP will assign the Agreement for Utility Services, Agreement for Waste Water Utility Services, and the Upgrade and Chemical Treatment Agreement to PSE. Please see Exhibit No. ___(RG-39HC) for a copy of the

Agreement for Utility Services, Agreement for Waster Water Utility Services, and the Upgrade and Chemical Treatment Agreement.

Q. What are the ongoing costs for the operation of the wastewater treatment program?

A. The ongoing costs associated with the wastewater discharge system include the chemical costs, consulting services for periodic monitoring and testing of the system, and periodic trunk sewer line cleaning by the City of Abbotsford. Please see Exhibit No. ___(RG-40HC) for an analysis of these costs.

Q. Please describe the stormwater separation between the power plant and the lumber operations.

A. Currently, the Sumas Cogeneration Station and Socco share a detention pond and stormwater conveyance pipes. The stormwater system requires separation to meet current regulatory agency requirements because the lots will be subdivided with separate owners post-closing. In October 2007, SCCLP requested a proposal from David Evans and Associates to provide engineering services to design modifications to the existing stormwater system at the power plant and at the Socco site in order to separate the two. Modifications at the power plant site include a V-shaped cutoff drain along the northern property line to prevent runoff from leaving the site, installation of a new catch basins and underground drain lines, and an increase in the depth of the existing detention pond. PSE reviewed

the David Evans and Associates design with its consultants for constructability and compliance. SCCLP anticipates that the project will be completed by June 2008.

Q. Please describe other facilities that were required to be separated or relocated by SCCLP?

A. In addition to the separation of the stormwater facilities, SCCLP must relocate the ammonia tank onto Lot A, in close proximity to the heat recovery steam generator. SCCLP anticipates that relocation of the ammonia tank will be complete by the end of calendar year 2007.

d. <u>Insurance Due Diligence</u>

Q. Please describe the insurance due diligence conducted by the Company.

A. PSE hired Marsh USA Inc. to conduct a property evaluation survey. The property insurance engineer conducted a site visit on September 12, 2007. The Property Evaluation Report submitted to PSE indicates that the facility has an excellent operating history with no property losses. Please see Exhibit No. ___(RG-41HC) for a copy of the Property Evaluation Report.

The Property Evaluation Report indicates that the Sumas Cogeneration Station is well separated from the lumberyard operation. Nonetheless, the Property Evaluation Report suggests the parties take the following three actions:

(i) construction of a reinforced concrete block wall between the two main generation step-up transformers to protect the fire exposure created from the adjacent transformers;

(ii) installation of automatic smoke detection systems in the Mark V control equipment room and the electrical breaker room; and

(iii) construction of a fire resistance rated enclosure around the electrical cable trays that contain the generation output cables to the step-up transformers.

Q. Were there any other concerns identified?

A. Yes. Later, in the due diligence process, PSE obtained an April 2007 boroscope inspection report from SCCLP that showed cracking on one of the guide vanes of the first stage nozzles. First stage nozzles are subject to the highest temperatures in the turbine section, and such conditions can cause cracking. GE had previously noted this cracking in an April 2006 inspection report. Generally, first stage nozzles are repaired or replaced at each hot gas path inspection. PSE requested that SCCLP work with GE to gain a better understanding of the continued safe operation of the plant until the next scheduled hot gas path inspection. GE responded with a letter to PSE, which recommended periodic borescope inspections but no operational curtailments or changes to normal operating procedures. This response was satisfactory to PSE's insurers.

/////

/////

/////

e. O&M Due Diligence

Q. Please describe the O&M due diligence conducted by the Company.

A. The Company and its consultants reviewed the operating reports, maintenance inspection records, and software used at the plant, and conducted site visits to the Sumas Cogeneration Station. The plant was determined to be exceptionally clean and well-maintained at the time of the site visit. The gas turbine enclosure and exterior buildings were in excellent repair.

The Sumas Cogeneration Station has historically run at a high load factor and with few starts. The plant performance and availability have consistently exceeded 97%. The Contractual Services Agreement between GE and SCCLP currently has approximately 14,000 factored fired hours remaining. Based on the contract provisions, the expiration of the contract is estimated to occur in 2013, which coincides with the second hot gas path inspection, unless such inspection is accelerated. A routine combustion inspection is planned at the next 2,000 factor-fired hours. At such inspection, GE will assess the cracking of the first stage nozzles to determine whether the hot gas path inspection should be performed simultaneously with the combustion inspection.

Q. How does the Company propose to staff the Sumas Cogeneration Station?

A. SCCLP entered into an Amended and Restated Operations and Maintenance Agreement with Calpine Operating Services, Inc. ("Calpine") on January 24,

1992. That contract originally had an expiration date of December 31, 2007, but it will be extended until the transaction closes (estimated to be third quarter of 2008).

PSE is in the process of developing an Asset Management Plan to transition the existing Calpine employees, all software and vendor contracts, and all O&M policies and procedures of the plant. PSE anticipates that many of the Calpine employees will become PSE employees and expects staffing at the Sumas Cogeneration Station to remain at approximately 15 employees. PSE expects that this level of staffing will remain over the life of the plant. PSE plans to staff the plant in a manner similar to the current design, though the labor force would become members of IBEW Local 77, pursuant to PSE's human resources labor relations protocol. PSE plans to operate the project with a Plant Manager, an Operations Supervisor, and an Assistant Manager.

f. Technical Due Diligence

Q. Please describe the technical due diligence conducted by the Company.

A. PSE staff engineers conducted the technical due diligence, with some assistance from North American Energy Services. The Sumas Cogeneration Station is a conventional one-on-one combined cycle cogeneration power plant. As stated above, the plant achieved commercial operation in April 1993, is rated nominally at 125 MW, and is designed for baseload operation.

A GE Frame 7EA combustion turbine provides electrical power via a GE generator and exhaust heat ducted to a Vogt three-pressure heat recovery steam generator, which is used to generate high, intermediate, and low pressure steam. Steam generated by the heat recovery steam generator drives a GE SC2 steam turbine. The plant has redundancy on almost every system and has proven to be very reliable over time. PSE's technical due diligence team concluded that SCCLP maintained the plant well and that the plant has an excellent operating history.

Q. Has PSE and SCCLP finalized contracts for PSE's acquisition of the Sumas Cogeneration Station?

A. No. PSE and SCCLP have finalized all major business terms with respect to PSE's acquisition of the Sumas Generating Station, and the parties are, as of the time of this filing, finalizing several definitive agreements, including the following:

(i) a Membership Interest Purchase and Sale Agreement by and between SCCLP and PSE;

(ii) an Agreement for the Ownership and Operation of Gas Pipeline by and among PSE, Sumas Pipeline Company, and Socco;

(iii) a Steam Supply Agreement by and between PSE and Socco; and

(iv) a Statutory Warranty Deed by and between SCCLP and Sumas SPE, LLC.

After PSE and SCCLP finalize the definitive agreements, PSE will supplement this testimony to provide copies of such definitive agreements. PSE anticipates

that PSE and SCCLP will finalize and enter into the definitive agreements before the end of calendar year 2007.

Consummation of the transaction will be final at the time that all precedent conditions have been satisfied, FERC has approved transfer of the Station and the amendment and transfer of the Presidential Permit, and the parties are in receipt of such approvals.

Q. Does the Company's acquisition of the Sumas Cogeneration Station satisfy the evaluation criteria set out in the RFP?

A. Yes. The Company's acquisition of the Sumas Cogeneration Station satisfies the evaluation criteria as follows:

(i) The Sumas Cogeneration Station is compatible with PSE's need. The Sumas Cogeneration Station provides up to 135 MW of winter capacity, has significant operational flexibility, and has a reasonable heat rate among PSE's natural gas fleet.

(ii) The Sumas Cogeneration Station will minimize PSE's costs. PSE was able to acquire the Sumas Cogeneration Station at a favorable price. There are no additional transmission costs as the plant is located in PSE's service territory and is interconnected to PSE's 115 kV system.

(iii) The Sumas Cogeneration Station minimizes PSE's risks. By purchasing an existing facility, the costs are known and quantifiable. The Sumas Cogeneration Station has proven to be very reliable over time.

(iv) The Sumas Cogeneration Station includes public benefits. The Sumas Cogeneration Station is an efficient gas fired generating facility with low regulated emissions and CO_2 levels that meet the performance standards established in SB 6001.

(v) The Sumas Cogeneration Station met PSE's strategic and financial needs. Acquisition of the Sumas Cogeneration Station at a discounted price provides for the settlement of damages and all other claims arising from SSCLP's default under the PPA. Owning a west-side resource in PSE's control area allows PSE the flexibility with respect to future dispatch of the plant.

3. Project Acquisition Process

Q. Please describe the process resulting in PSE's acquisition of the Sumas Facility.

A. As discussed above, PSE and Sumas entered into a Letter of Intent on August 31, 2007, for the purchase and sale of the Sumas Cogeneration Station as settlement of SCCLP's PPA default. PSE and Sumas established an exclusive due diligence period ending November 16, 2007. Concurrent with the due diligence activity, PSE and Sumas negotiated in earnest the Membership Interests Purchase and Sale Agreement and ancillary agreements. PSE and Sumas expect to successfully conclude negotiations and execution of definitive agreements in December 2007

Q. What concessions did PSE secure from SCCLP?

A. Through negotiations, PSE was able to obtain concessions that included a reduced purchase price for the spare parts inventory and payment by SCCLP of 100% of the real estate excise tax.

/////

/////

Q. Has FERC approved the disposition of the Sumas Cogeneration Station?

A. No. PSE and SCCLP expect to file a joint application in December 2007 for FERC approval under Section 203 of the Federal Power Act. PSE anticipates receipt of FERC's ruling on its Section 203 application within two to three months after filing.

Q. Have PSE and SCCLP closed the sale of the Sumas Cogeneration Station?

A. No. As discussed above, the parties estimate that the transaction will close in the third quarter of 2008 after approval and receipt from FERC of the Section 203 approval and the amendment to the Presidential Permit to reflect the change in ownership of the natural gas pipeline. The Presidential Permit is a long approval process because it requires approvals from FERC, the U.S. State Department, and the U.S. Department of Defense.

4. <u>Project Acquisition Costs</u>

Q. Please describe the acquisition costs for the Sumas Cogeneration Station.

A. The Company's total purchase price for the Sumas Cogeneration Station is $[redacted], or approximately $[redacted] per kW. The "all-in" capital cost of the acquisition is $30,439,921, which includes the following additional costs (please see Exhibit No. ___(RG-42HC) for additional detail):

/////

Sumas Cogeneration Station	Project Costs
Facility Purchase Price	[redacted]
Spare Parts Inventory	[redacted]
Facility Improvements	[redacted]
One Time Permitting Fees	[redacted]
Transaction & Due Diligence	[redacted]
Property Taxes	[redacted]
Total Capital Expense	**$30,125,113**

Q. Please describe the line item "Facility Purchase Price."

A. The "Facility Purchase Price" represents the costs associated with the purchase of all assets of the Sumas Cogeneration Station.

Q. Please describe the line item "Facility Improvements."

A. "Facility Improvements" are funds to upgrade the communications and security systems at the Sumas Cogeneration Station ($[redacted]) and to retrofit the cooling tower exhaust stack to mitigate rust particulate that is emitted during start up of the plant ($[redacted]). PSE anticipates that startups of the plant occur more frequently because the plant will now be dispatched based on the market signals. Therefore, retrofit of the cooling tower will include a stack damper, coating the inside of the stack, and adding a heat exchanger.

Q. Please describe the line item "Transaction & Due Diligence."

A. "Transaction & Due Diligence" costs are PSE's internal costs for due diligence and negotiations, title insurance, third party expert consultants and legal fees

associated with the transaction. For example, "Transaction & Due Diligence" costs reflect (i) the costs paid by PSE to third parties that assisted in due diligence efforts for the Sumas Cogeneration Station, and (ii) fees paid to legal counsel.

Q. Please describe the line item "Property Taxes."

A. In Washington State, property is assessed at the end of each calendar year with taxes paid in April and October of the following year, in arrears. It is customary in real estate transactions in Washington for property taxes to be prorated based on taxes payable in the year of closing. Consistent with accounting treatment, where property taxes are accrued, those taxes paid at closing and those paid up until the first anniversary of the closing date are capitalized.

5. <u>O&M Expenses</u>

Q. What does the Company project its expenses will be for the Sumas Cogeneration Station during the rate year?

A. The Company projected total O&M expenses of $ 4,342,942 for the Sumas Cogeneration Station.

Sumas Cogeneration Station Expense	Expense
Production O&M	$3,693,382
Property Tax	$543,257
Insurance	$106,303
Total O&M Expense	**$4,342,942**

Please see Exhibit No. ___(RG-43HC) for detail regarding the projected total O&M expenses for the Sumas Cogeneration Station.

VII. EXTENSION OF POINT ROBERTS SUPPLY CONTRACT WITH POWEREX

Q. Please describe the Point Roberts contract extension with Powerex.

A. Due to the unique geography of Point Roberts, Washington, it is not electrically connected to PSE's system, and PSE must use Powerex to serve this load in the absence of a distribution tariff on BC Hydro's system.

The contract extension with Powerex to supply the Point Roberts load provides for another two (2) years of service, commencing October 1, 2007, and ending September 30, 2009, at a renegotiated price of [redacted]. The contract is a full requirements contract, up to a maximum of 8 MW. Peak capacity is estimated to be 6 MW with an annual average load of 2.5 aMW.

Q. Has the Company discussed the potential for a distribution tariff with BC Hydro?

A. PSE contacted BC Hydro in June 2007 to discuss the potential for a distribution tariff. At the time, BC Hydro was in a rate proceeding but indicated interest in meeting with PSE in the future.

////