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BEFORE THE WASHINGTON UTILITIES AND

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TRANSPORTATION COMMISSION

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4 In the Matter of the) Docket No. UE-990267
 Application of)
 5) Volume IV
 PUGET SOUND ENERGY, INC., for) Pages 29-298
 6 (1) Approval of the Proposed)
 Sale of the Colstrip Generating)
 7 Units, and (2) Authorization)
 to Amortize Gain Over a)
 8 Five-Year Period.)
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A hearing in the above matter was

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held on July 15, 1999, at 9:35 a.m., at 1300

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Evergreen Park Drive Southwest, Olympia, Washington,

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before Administrative Law Judge MARJORIE SCHAER, and

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CHAIRWOMAN MARILYN SHOWALTER, COMMISSIONER WILLIAM R.

15

GILLIS, and COMMISSIONER RICHARD HEMSTAD.

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The parties were present as

18

follows:

19

PUGET SOUND ENERGY, INC., by
 Matthew R. Harris, Attorney at Law, Summit Law Group,
 20 1505 Westlake Avenue North, Suite 300, Seattle,
 Washington 98109, and Kimberly J. Harris, Attorney at
 21 Law, 411 108th Avenue N.E., OBC-15, Bellevue,
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22

23

INDUSTRIAL CUSTOMERS OF NORTHWEST
 UTILITIES, by S. Bradley Van Cleve, Attorney at Law,
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 24 2915, 1300 S.W. Fifth Avenue, Portland, Oregon,
 97201.

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1 THE COMMISSION, by Robert Cedarbaum,
2 Assistant Attorney General, 1400 South Evergreen Park
3 Drive, S.W., P.O. Box 40128, Olympia, Washington,
4 98504.

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6 PUBLIC COUNSEL, by Robert Manifold,
7 Attorney at Law, 6933 Via Valverde, La Jolla,
8 California 92037.

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Barbara L. Spurbeck
Court Reporter

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1 JUDGE SCHAER: The Washington Utilities and
2 Transportation Commission has set for hearing at this
3 time and place, on due and proper notice to all
4 parties, a hearing in Docket UE-990267, which is in
5 the matter of the application of Puget Sound Energy,
6 Inc., for (1), approval of the proposed sale of the
7 Colstrip generating units, and (2), authorization to
8 amortize gain over a five-year period.

9 We are here today for the cross-examination
10 hearing of the witnesses for parties to the
11 proceeding. I am Marjorie Schaer, Administrative Law
12 Judge. On behalf of the Commission, presiding today
13 are Chairwoman Marilyn Showalter, Commissioner
14 Richard Hemstad, and Commissioner Bill Gillis, who
15 will be joining us a little bit later this morning.

16 I'd like to start by taking appearances,
17 starting with Counsel for the Applicant, please.

18 MS. HARRIS: Kimberly Harris, representing
19 PSE.

20 MR. HARRIS: Matthew Harris, on behalf of
21 PSE.

22 MR. VAN CLEVE: Brad Van Cleve, on behalf
23 of Industrial Customers of Northwest Utilities.

24 MR. MANIFOLD: Robert Manifold, on behalf
25 of Public Counsel.

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1 MR. CEDARBAUM: Robert Cedarbaum, for
2 Commission Staff.

3 JUDGE SCHAER: All right. Any preliminary
4 matters that need to come before the Commission this
5 morning? Hearing none, I would like to first take up
6 the matter of the stipulation regarding EWG
7 determination, which the parties presented last week,
8 and I would like Mr. Harris to give us a presentation
9 on this document and what it means, please.

10 MR. HARRIS: I'd like to take a moment and
11 briefly address the stipulation and the proposed
12 order and then offer them both as exhibits in this
13 proceeding.

14 JUDGE SCHAER: Certainly.

15 MR. HARRIS: What's been marked, I believe,
16 as Exhibit 13, and is the order marked 14, then?

17 JUDGE SCHAER: I marked both documents as
18 Exhibit 13 --

19 MR. HARRIS: Thank you.

20 JUDGE SCHAER: -- for identification,
21 before we went on the record. And if you'd like me
22 to mark them officially now, I'd like to identify the
23 document, three pages, headed at the top Stipulation,
24 Re: EWG Determination, accompanied by a document, a
25 five-page document headed at the top Supplemental

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1 Order Re: EWG Determination Proposed. Those two
2 documents have been marked for identification as
3 Exhibit 13.

4 MR. HARRIS: Thank you, Your Honor. The
5 stipulation and proposed order address a very narrow
6 issue that the parties have negotiated an agreement
7 with respect to. We negotiated this agreement while
8 we were all preparing our cases on the main issue in
9 this case, which is, of course, whether the sale of
10 the facilities themselves should be approved.

11 One of the issues in the case, and it's an
12 issue that came up early, has to do with whether the
13 purchasers, PP&L Global, will be permitted to operate
14 the facility as an exempt wholesale generator
15 facility or with exempt wholesale generator status.

16 Because the facilities are currently in
17 PSE's rate base for jurisdictional sales of
18 electricity, federal law requires that PP&L Global
19 include with its application to FERC a determination
20 or a statement by this Commission. And the statement
21 is very specific, it's set forth in the statute, and
22 the statement says that the Commission has determined
23 that allowing the plant to be a wholesale facility
24 operated by an EWG, quote, will benefit consumers, is
25 in the public interest, and does not violate state

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1 law.

2 So the parties put together this
3 stipulation, together with the proposed order, and to
4 summarize all of it, it says that if the sale is
5 ultimately approved, the parties agree that those
6 conditions are met. And that's what the stipulation
7 is, that's what the proposed order is, and we're
8 asking that these matters be resolved while the
9 Commission is considering whether the sale ultimately
10 will be approved.

11 JUDGE SCHAER: Well, what is the need for
12 that early approval, Mr. Harris?

13 MR. HARRIS: It allows us to start the
14 process at FERC, and my understanding is that that
15 application process will take 60 days. And so it
16 becomes the critical path for getting the sale closed
17 if it's ultimately approved. So we'd like to be able
18 to start that process and run in parallel so we don't
19 end up at the end of this process within a further
20 delay at FERC before we can finally get the sale
21 approved.

22 The one thing I would add is I think it's
23 fair to say that Counsel, the parties that were
24 involved in the stipulation, are available to answer
25 any questions about it. Whether you want to do that

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1 now or at the end of the hearing or not at all, I
2 would just make that offer.

3 JUDGE SCHAER: Did you want to offer
4 Exhibit 13?

5 MR. HARRIS: Yes, we'd offer Exhibit 13.

6 JUDGE SCHAER: Any objection? That
7 document is admitted. Commissioners, did you have
8 questions for Counsel?

9 CHAIRWOMAN SHOWALTER: I have a question.
10 The standard that applies to the FERC is that it's
11 beneficial to the consumers, whereas the standard
12 that is at issue, whether we approve the transfer, is
13 or arguably is not inconsistent with the public
14 interest or a hold harmless.

15 So are we being asked, are you asking us to
16 prejudge that question by finding that,
17 theoretically, if we find that this is a hold
18 harmless, that somehow we've lumped over into a
19 beneficial standard?

20 MR. HARRIS: Absolutely not. I think
21 that's a good question, and there's been quite a bit
22 of discussion and confusion about that.

23 The stipulation itself makes clear that the
24 parties have reached no agreement about that issue in
25 particular, and because of the way the statute is

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1 worded, it is somewhat confusing, because it talks
2 about finding an affirmative benefit to consumers,
3 but the test is whether allowing the plant itself to
4 be operated as a wholesale facility or operated as an
5 EWG, whether that particular narrow question is
6 answered in a way that you can say yes, that benefits
7 consumers, not the sale itself. So they really are
8 two different inquiries.

9 CHAIRWOMAN SHOWALTER: Two different
10 standards, but applied to two different issues.

11 MR. HARRIS: Absolutely.

12 COMMISSIONER HEMSTAD: What is your
13 expectation of the Commission on signing the proposed
14 order?

15 MR. HARRIS: Timing?

16 COMMISSIONER HEMSTAD: In other words, are
17 you expecting us to sign this now or at the end of
18 the case?

19 MR. HARRIS: It would facilitate the
20 transaction if it could be signed before the end of
21 the case. If it can be resolved before the
22 Commission undertakes the whole process of deciding
23 the much bigger and more complicated issues on
24 whether the sale itself should be approved, it would
25 facilitate the process at FERC. Of course, if the

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1 sale ultimately isn't approved, then the FERC process
2 just goes away.

3 COMMISSIONER HEMSTAD: Does Staff Counsel
4 have any comment?

5 MR. CEDARBAUM: On the timing?

6 COMMISSIONER HEMSTAD: Yes.

7 MR. CEDARBAUM: No, we have no objection to
8 the Commission issuing an order sooner than the final
9 order in this case, given that the effect of the
10 final order will determine whether or not the EWG
11 order has any effect whatsoever. So in terms of
12 allowing the company that opportunity, we don't
13 object to that.

14 I would just have one comment with respect
15 to Mr. Harris' discussion of the standard in the
16 statute, in response to Chairwoman Showalter's
17 question. That was an issue that did come up in
18 discussions with respect to the stipulation. By my
19 silence, by correcting that silence now, I don't want
20 to indicate any agreement with Mr. Harris about what
21 the narrowness or what the breadth of what the
22 Commission would be -- the consumer benefits test
23 from the EWG determination would be.

24 The Staff has argued that that is a factor
25 that should be considered in terms of what standard

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1 should be applied, that the consumer benefits test
2 that Staff is proposing in the main case is
3 consistent with the federal statute. So I don't want
4 to leave the impression that we're reading it as
5 narrowly as the company might be.

6 CHAIRWOMAN SHOWALTER: I think that's my
7 question. If you are suggesting the standard is --
8 are you suggesting the standard for the underlying
9 transfer is beneficial to consumers?

10 MR. CEDARBAUM: In the Staff case, the
11 Commission can adopt that standard and should.

12 CHAIRWOMAN SHOWALTER: Then that means
13 there's a congruence between that standard and the
14 FERC standard. But supposing we decide that there's
15 a different standard. Have we precluded anything by
16 -- have we precluded anything on the issue of the
17 standard of what then applies for these different --

18 MR. CEDARBAUM: I don't think so, because,
19 again, the EWG order is contingent upon your final
20 order in the case, so I don't think you're precluding
21 yourself from doing that. We're just saying that the
22 EWG order, because of the federal standard that
23 requires consumer benefits, is consistent with the
24 Staff's position in the main case.

25 JUDGE SCHAER: I'm a little bit concerned,

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1 Mr. Cedarbaum, also about the appearance of issuing
2 an order that says that EWG allowing the plant to be
3 a wholesale facility will benefit consumers and is in
4 the public interest if the Commission should choose
5 to decide in a later order that there is no -- that
6 this deal is not consistent with the public interest
7 or that this standard applies and isn't met.

8 MR. CEDARBAUM: In that case, the
9 Commission's order on the EWG determination would
10 have no effect, so --

11 JUDGE SCHAER: So FERC will let the parties
12 file this as a conditional order?

13 MR. CEDARBAUM: That's my understanding.
14 Ms. Harris could add to that.

15 JUDGE SCHAER: Even though it's not binding
16 on anyone and it's clearly conditioned as determined
17 by the later outcome of the case; is that --

18 MR. CEDARBAUM: That was the understanding
19 we had through discussions with Counsel.

20 MS. HARRIS: It's been represented to us
21 that when we brought this back to FERC, that
22 basically any EWG order or any EWG determination from
23 FERC is kind of conditional in that you are not in
24 EWG unless the entire transaction closes. So this
25 condition did not meet with any resistance from FERC.

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1 And I believe Counsel for ICNU, Mr. Van Cleve,
2 represented that Oregon has issued an order to
3 continue the Colstrip --

4 MR. VAN CLEVE: That's correct, in the past
5 week, and it also is conditional.

6 JUDGE SCHAER: So I guess I would feel a
7 little bit more comfortable if we had some clear
8 statement from Puget, maybe, and maybe the clear
9 statement is here, that any kind of citing of this
10 order would never be cited to the Commission later as
11 evidence of agreement, unless there is a parallel
12 order as a result of this case that finds the same
13 standards are met.

14 MR. HARRIS: Absolutely, that's correct,
15 and I believe we've captured that in the stipulation
16 and order itself. If there's any additional language
17 that the Commission would like on that, we'd be happy
18 to include it.

19 JUDGE SCHAER: Any further questions from
20 the Commissioners? Okay.

21 MR. MANIFOLD: Your Honor, given the
22 questions on this, may I just suggest that after the
23 Commission has had a chance to digest Exhibit 13 and
24 the proposed order, it seems to me that what the
25 parties are saying is that if there are questions on

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1 that that the Commission would like the parties to
2 resolve prior to resolving the rest of the case, that
3 we're very open to doing that.

4 JUDGE SCHAER: Would you like to call your
5 first witness, Mr. Harris?

6 MR. HARRIS: Yes, PSE calls Mr. John Story
7 as its first witness.

8 Whereupon,

9

JOHN STORY,

10 having been first duly sworn by Judge Schaer, was
11 called as a witness herein and was examined and
12 testified as follows:

13 JUDGE SCHAER: Mr. Harris.

14 MR. HARRIS: Your Honor, would you like at
15 this time to mark for identification Mr. Story's
16 rebuttal testimony and the two exhibits that go along
17 with that?

18 JUDGE SCHAER: Okay.

19 MR. HARRIS: It's JHS-5T.

20 JUDGE SCHAER: It will be marked for
21 identification as Exhibit T-16.

22 MR. HARRIS: JHS-6.

23 JUDGE SCHAER: That will be marked for
24 identification as Exhibit 17.

25 MR. HARRIS: And JHS-7.

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1 JUDGE SCHAER: That will be marked for
2 identification as Exhibit 18.

3 D I R E C T E X A M I N A T I O N

4 BY MR. HARRIS:

5 Q. Good morning, Mr. Story. Do you have
6 before you what's now been marked for identification
7 as Exhibit T-1, Exhibits 2 through 5, Exhibit T-16,
8 Exhibit 17 and Exhibit 18?

9 A. I do.

10 Q. Do you recognize those as your prefiled
11 testimony in this case, together with the supporting
12 exhibits?

13 A. Yes.

14 Q. Do you have any corrections to make to your
15 prefiled direct testimony? That's Exhibit T-1.

16 A. Yes, I do. On page four, line seven, "or
17 expenses" should be struck. The words "or expenses".
18 It should just read "for company employees."

19 Q. Do you have any other corrections to
20 Exhibit T-1?

21 A. No.

22 Q. Is it complete and accurate, to the best of
23 your knowledge?

24 A. Yes.

25 Q. Do you have any corrections to make to

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1 Exhibit T-16?

2 A. Yes, I do. Page five, line 11, before the
3 words "real property," it should be added
4 "non-depreciable" real property.

5 CHAIRWOMAN SHOWALTER: I'm sorry.

6 COMMISSIONER HEMSTAD: What page was that?

7 THE WITNESS: Page five, line 11.

8 JUDGE SCHAER: On his rebuttal testimony.

9 CHAIRWOMAN SHOWALTER: Oh, I'm sorry.

10 MR. HARRIS: I'm sorry, we jumped to

11 Exhibit T-16.

12 COMMISSIONER HEMSTAD: I'm sorry, would you
13 repeat the change?

14 THE WITNESS: The word non-depreciable
15 should be put in front of real property. So it
16 reads, "Applies to sales of non-depreciable real
17 property" on line 11.

18 Q. Do you have any other corrections to
19 Exhibit T-16?

20 A. No, I don't.

21 Q. Is it complete and accurate, to the best of
22 your knowledge?

23 A. Yes.

24 MR. HARRIS: At this time, Your Honor, PSE
25 would offer Exhibit T-1, Exhibits 2 through 5,

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1 Exhibit T-16, and Exhibits 17 and 18.

2 JUDGE SCHAER: Are there any objections?

3 Those documents are admitted.

4 MR. HARRIS: Mr. Story is available for
5 cross-examination.

6 JUDGE SCHAER: Mr. Cedarbaum.

7 C R O S S - E X A M I N A T I O N

8 BY MR. CEDARBAUM:

9 Q. Good morning, Mr. Story.

10 A. Good morning.

11 MR. CEDARBAUM: Your Honor, before we went
12 on the record this morning, I circulated an exhibit
13 for cross-examination of Mr. Story. If I could have
14 that marked for identification, please.

15 JUDGE SCHAER: Yes, marked for
16 identification at this time a multi-page exhibit
17 which states that it is the revised response to Data
18 Request Number Three at the top of the first page,
19 and I've marked that for identification as Exhibit
20 14.

21 Q. Mr. Story, referring you to Exhibit 14, do
22 you recognize this as the company's revised response
23 to Data Request Number Three of Commission Staff?

24 A. Yes, I do.

25 Q. Was this prepared by you or under your

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1 supervision and direction?

2 A. Yes, it was.

3 Q. It's true and correct, to the best of your
4 knowledge and belief?

5 A. Yes.

6 Q. The revision that you've provided in
7 Exhibit 14 corrects a \$6.3 million environmental
8 remediation expense with a \$2,805,000 remediation
9 expense; is that right?

10 A. That's correct.

11 Q. And the remaining pages of the exhibit are
12 updated versions of your direct exhibits, JHS-2
13 through 5; is that right?

14 A. That's correct.

15 MR. CEDARBAUM: Your Honor, I would offer
16 Exhibit 14.

17 JUDGE SCHAER: Any objection? The
18 document's admitted.

19 Q. The revisions that are contained in Exhibit
20 14 assume an estimated closing date of September 1st,
21 1999; is that right?

22 A. That's correct.

23 Q. And it also includes the sale of all of the
24 Colstrip facilities, and it assumes that PGE obtains
25 approval of the sale of its share of Colstrip; is

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1 that right?

2 A. That's correct.

3 Q. Turning to page two of the exhibit, it
4 shows an amount on line nine of \$40,091,449. Do you
5 see that?

6 A. Yes.

7 Q. And that's the same number that appears on
8 your Exhibit 18, JHS-7, Schedule One?

9 A. Actually, JHS-7 has \$41,908,545.

10 Q. I'm looking at the second page behind the
11 cover page.

12 A. Oh, that's correct.

13 Q. Again, on line nine?

14 A. Yes.

15 Q. If you turn to the first page of Exhibit
16 18, on line nine, that figure reflects removing the
17 estimated environmental remediation costs consistent
18 with the Staff recommendation; is that right?

19 A. That's correct.

20 Q. Now, if we switch back to Exhibit 14, it's
21 the last page under entry number seven at the top of
22 the page. Do you see that?

23 A. Excuse me. Which exhibit are you in now?

24 Q. I'm now in Exhibit 14.

25 A. Okay. And the last page?

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1 Q. The last page, entry number seven at the
2 top.

3 A. Okay.

4 Q. It states in the note that a ten-year
5 amortization period is included. Do you see that?

6 A. Yes, that should be five years.

7 Q. So was that purely a typographical mistake,
8 or can you explain why ten years is there, rather
9 than five years?

10 A. No, that was when we first started putting
11 this together, we were following the Morgan Stanley
12 presentation, and they had a ten-year amortization in
13 their presentation. After we were doing the
14 analysis, we changed it to a five-year amortization.

15 Q. So at one point in time, the company was
16 considering a ten-year amortization period?

17 A. I wouldn't say we were considering it. We
18 were putting the case together and we were just
19 basing it off the numbers as we pulled the new
20 numbers in.

21 Q. Now, I'm through with Exhibit 14. I just
22 have a few other questions on a different topic.
23 With respect to the rate plan that's currently in
24 effect, is it correct that the rate plan includes
25 annual increases and rates for electric service of

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1 one to one and a half percent, depending on customer
2 class?

3 A. That's correct.

4 Q. And would you accept, subject to check, or
5 do you recall that the stipulation from the merger
6 states that the rate plan is based upon recovery of
7 power cost components for 1997 through 2001, as set
8 forth in Exhibit D to the stipulation?

9 A. That's correct.

10 Q. And Exhibit D, which Mr. Elgin has included
11 in his testimony, forecasts power costs for 1997, and
12 then escalates them for the years 1998 to 2001; is
13 that right?

14 A. That's correct.

15 Q. And they contain -- those forecasts contain
16 expenses associated with Colstrip One through Four
17 generation of transmission facilities; is that right?

18 A. They would have contained the expenses for
19 all of our plant at that time and contracts.

20 Q. Including Colstrip?

21 A. Yes.

22 Q. Are you familiar with the testimony of Mr.
23 Flaherty from the merger proceeding?

24 A. It's been a while since I've read it, but
25 I've read it, yes.

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1 Q. He was a witness that testified for the
2 company in that case, and he identified and
3 quantified merger savings that could be achieved
4 solely with respect to the merger, as opposed to
5 separate operations; is that right?

6 A. That's correct.

7 Q. He didn't identify the sale of Colstrip
8 facilities as one source of savings from the merger;
9 is that right?

10 A. He had nothing to do with power cost
11 savings, no.

12 Q. Also in the merger, there was discussion
13 and some evidence about a rating agency presentation.
14 Do you recall that?

15 A. Exhibit 107, yeah.

16 Q. Can you just -- what was the rating agency
17 presentation?

18 A. It was the Companies' forecasts combined.
19 It was both taking WNG forecasts at the time and
20 Puget's forecast, Puget Power's forecast, combining
21 them, and showing what the impact would be going
22 forward.

23 Q. So it was a forecast of power stretch goals
24 and best practices; is that right?

25 A. I wouldn't call it a forecast of that. It

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1 indicated that we had those goals on the bottom, I
2 believe, on one of the pages, yes.

3 Q. Do you recall the date that the rating
4 agency presentation was created?

5 A. It would have been late '96, most probably,
6 early '97.

7 Q. Would you accept, subject to check, it was
8 dated January 1996?

9 A. Could be, yes.

10 Q. Do you know when the state of Montana --

11 A. January of '96?

12 Q. Yes.

13 CHAIRWOMAN SHOWALTER: What was the
14 question?

15 JUDGE SCHAER: Okay. You had asked if he'd
16 accept, subject to check, that that was January of
17 '96; is that correct?

18 MR. CEDARBAUM: The rating agency
19 presentation.

20 JUDGE SCHAER: And you had agreed that it
21 was, subject to check?

22 THE WITNESS: Subject to check. Just
23 seemed like a strange date.

24 JUDGE SCHAER: Would you ask your next,
25 please?

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1 Q. My next question is do you know when the
2 state of Montana issued its statute calling for
3 divestiture of generation assets?

4 A. I don't recall, no.

5 Q. Would you accept, subject to check, that it
6 was May 1997?

7 A. Sure.

8 MR. CEDARBAUM: Thank you. Those are all
9 my questions.

10 JUDGE SCHAER: Okay. Mr. Van Cleve, did
11 you have questions of Mr. Story?

12 MR. VAN CLEVE: Yes.

13 JUDGE SCHAER: Go ahead, please.

14 C R O S S - E X A M I N A T I O N

15 BY MR. VAN CLEVE:

16 Q. Mr. Story, do you know how the Company's
17 actual power stretch and best practices savings
18 compared to the forecast provided to the rating
19 agencies?

20 A. No, we've not done a line item by line item
21 type comparison. I believe the way the rate
22 department is checking merger savings versus what's
23 actually happened is by comparing the forecast
24 against actuals. They have not identified the
25 underlying items.

00056

1 Q. Do you have a general understanding of
2 whether the best practices and power stretch savings
3 are higher or lower than the forecast with the rating
4 agencies?

5 A. Just going by what's on our financials, I
6 would say a combination of all the three. Most
7 probably, they're a little lower, but some of them
8 are being achieved, yes.

9 Q. And by all three, what do you mean?

10 A. I mean merger savings, the synergy savings,
11 the best practices and power costs.

12 CHAIRWOMAN SHOWALTER: What was the last
13 one?

14 THE WITNESS: Power cost savings.

15 JUDGE SCHAER: Mr. Story, you're going to
16 need to speak up a little bit.

17 THE WITNESS: Okay.

18 Q. Did you submit testimony in the merger
19 proceeding?

20 A. Yes, I did.

21 Q. And did that testimony address the
22 potential accounting treatment for asset sales?

23 A. Yes, they did.

24 Q. Can you explain how it addressed it?

25 A. What we were talking about in the merger

00057

1 was property sales. Some of the merger savings were
2 going to be property, so we asked for a waiver of the
3 treatment of those merger-related property sales.

4 Q. Did any of your testimony in the merger
5 proceeding discuss the rate plan?

6 A. Indirectly, it could have, yes.

7 Q. Were you a witness on the terms of the rate
8 plan?

9 A. I can't recall in rebuttal if I addressed
10 any of the rate plan or not. It would have been Ron
11 Amen or myself that would have done it. I believe
12 Ron Amen did most of it.

13 Q. Do you know if any of the testimony you
14 have submitted in the merger proceeding addressed the
15 definition of power stretch savings?

16 A. There was a lot of testimony in the merger
17 proceeding that addressed that, and it was defined as
18 -- the Company didn't have it defined. It was a
19 goal. Mr. Sonstelie did it, Mr. Torgerson did it.

20 Q. My question was did any of your testimony
21 address that?

22 A. It would have been on cross-examination,
23 and I can't recall if I did or not.

24 Q. It's true that you're requesting that the
25 gain from the sale of the Colstrip assets be

00058

1 amortized over a five-year period?

2 A. Yes.

3 Q. Is that proposed accounting treatment
4 driven by the existence of the rate plan?

5 A. No.

6 Q. If the rate plan didn't exist, do you
7 anticipate that you would propose a five-year
8 amortization?

9 A. I think we would have, yes.

10 Q. And what do you base that on?

11 A. It's a methodology to take an extraordinary
12 type gain or cost and amortize it over a time period
13 so that it's more reasonable in rates. It's not
14 unusual to do that for an extraordinary type gain or
15 loss.

16 Q. And is there precedent for a five-year
17 amortization period that you're aware of?

18 A. In this state or other states? Other
19 states have used five years, yes.

20 Q. And this state?

21 A. This state has used various time limits.
22 On our Skagit project, which was a loss associated
23 with a nuclear, it was amortized over ten years. I
24 think the Commission normally looks at -- and
25 property sales are amortized over three years. The

00059

1 storm damage is amortized over three or four years.
2 I can't recall that. Maybe it's six years now.

3 The -- could you ask your question again?
4 I've lost my train of thought.

5 Q. I asked what the precedent for a five-year
6 amortization was?

7 A. I think it's mainly just what is an
8 appropriate time period to allocate the extraordinary
9 gain or loss.

10 Q. Is it your position that any generating
11 asset sales should be amortized over five years?

12 A. I think you have to look at them
13 individually.

14 Q. And what factors would lead you to decide
15 what the appropriate amortization period would be?

16 A. I think size of the gain would be one,
17 impact on the income statement. We're in a time
18 period where the company was challenged to meet
19 benefits given to the customers up front during the
20 merger through finding cost savings. One thing we
21 looked at is how are we going to get these cost
22 savings into our income statement to support those
23 kind of costs that we were supporting on the rate --
24 you know, get those costs down so that we'd have good
25 financials. That was one of the considerations on

00060

1 five years.

2 Q. You stated that the size of the gain
3 impacted the amortization period; correct?

4 A. It could, yes.

5 Q. Would a larger gain indicate a longer or
6 shorter amortization period?

7 A. I think you would have to look at the
8 circumstances.

9 Q. Assume, hypothetically, that the Company
10 sold all of its rights to the output of the
11 Mid-Columbia projects and received a lump sum
12 payment. How would you propose to account for a gain
13 like that?

14 A. I wouldn't even begin to guess. I would
15 have to know the price, I would have to know what
16 we're planning on replacing it with. Just a -- it's
17 too hypothetical.

18 Q. Is it your position that the Company could
19 sell all of its below-market resources and amortize
20 that gain during the rate plan?

21 A. I don't think the rate plan has anything to
22 do with it. Five years going forward falls outside
23 the rate plan. The customers are receiving the
24 benefit already. You know, five years we chose for
25 impact on financials.

00061

1 Q. Could you look at Exhibit 17, please?

2 A. Could you give me the reference number, the
3 JHS?

4 Q. This is JHS-6.

5 A. All right.

6 Q. On line 28 of page one of Exhibit 17, on
7 the far right side, there's two numbers. And does
8 the first number, 72,060,000, indicate that there's
9 -- is that the net present value of the gain -- well,
10 why don't you explain what that number is?

11 A. It's the cumulative present value. This
12 exhibit was done in the same format as Mr. Lazar's,
13 where it's put based on 2002, the potential of a
14 general rate case coming into effect. So 72,060,000
15 is the number that's shown on line nine, which is
16 just the cumulative present value for the three years
17 during the rate stability period. The minus
18 twenty-seven-eight-thirty-four is the sum of the
19 numbers on line 10 through 26.

20 Q. Is it fair to say that the \$72 million
21 number is the net present value of the benefit that
22 shareholders receive from the sale?

23 A. No.

24 Q. Why not?

25 A. Because the customers are receiving it.

00062

1 Q. Well, I'm asking what the benefit that the
2 shareholders are receiving is?

3 A. I think the benefit the shareholders get is
4 if we can find enough gains or cost reductions during
5 this time period to cover all the costs that we took
6 on at the beginning of the merger, the Company has a
7 potential of earning its return or maybe even
8 slightly above or slightly less.

9 Q. But my question is, you've proposed an
10 accounting treatment for the sale of the Colstrip
11 assets?

12 A. Right.

13 Q. And does this \$72 million number reflect
14 the net present value to shareholders of that
15 accounting treatment?

16 A. No.

17 Q. Why not?

18 A. I've already answered that. When the
19 merger started, and the Commission order addresses
20 this, is that the ratepayers were given rate
21 stability during the five-year time period. The
22 Company was challenged to obtain the merger cost
23 savings or the merger benefits, the synergy or the
24 power cost savings and the benefits, you know, best
25 practices benefits. If we could do that, we would

00063

1 forgo our general rate cases. I know we basically
2 had great pressures during the merger, at the
3 beginning of the merger for Puget of about 74
4 million, I believe, 79 million. We had a general
5 rate case filing that could have been presented
6 before. We didn't file it.

7 Basically, the customers kept their lower
8 rates, we guaranteed the residential exchange rate
9 would not change during this time period, and we had
10 to find the cost savings to make up for the benefits,
11 or give them -- support that benefit and keep our
12 financial integrity.

13 So what we've been doing during the last
14 two and a half, three years, is going out and finding
15 the cost savings that we can -- that are valid, good
16 cost savings and not going to harm the company in
17 some way or, in the future, harm the customers to
18 cover those benefits we've already given the
19 customers.

20 Q. Didn't you just testify that the five-year
21 amortization of the gain was unrelated to the rate
22 plan?

23 A. That's true. It just happens to fall in
24 the rate plan, too. It just happens that this was
25 two and a half years into the rate plan. We chose a

00064

1 five-year amortization period to levelize an
2 extraordinary gain, and a piece of it happens to fall
3 into the rate period and a piece falls outside.

4 Q. And what is the net present value gain to
5 shareholders from the five-year amortization, given
6 the effect of the rate plan?

7 A. It depends how well we do on covering all
8 of our costs.

9 Q. But what I'm looking at is, with this
10 transaction and without, what is the benefit to
11 shareholders?

12 A. The problem I'm having with your question
13 is it's a benefits to shareholder, and you can't do
14 that off of this. The shareholder benefit is if we
15 can cover the costs that we showed during the merger
16 as increasing and we can maintain the low rates for
17 the customer that was agreed to at the beginning of
18 the merger plan, then the Company has a benefit. I
19 mean, you have to almost look over the whole
20 five-year period as to what's happened to the Company
21 during this time period. You look at 1997's earnings
22 for this company and they were around a
23 dollar-twenty-eight. That's nowhere close to being
24 adequate. Last year, they were a lot better. They
25 were a dollar-eighty-five. I don't know what the

00065

1 impact is going to be exactly, basically.

2 Q. In the years 1999, 2000, and 2001, will the
3 sale of the Colstrip assets affect the Company's
4 earnings?

5 A. Yes, they will.

6 Q. And can you explain how it will affect the
7 Company's earnings?

8 A. I think that if you look at the exhibits
9 that were attached to Mr. Gaines' testimony, you can
10 see the change in power costs, what we'd be going to
11 as a market rate versus a Colstrip rate, so there
12 would be a reduction in overall power costs, and then
13 there's also this piece of the gain that's being
14 amortized.

15 But, again, these are cost savings that are
16 being used to cover cost benefits we've already given
17 to the customers.

18 Q. Does the \$72 million net present value
19 number reflect the impact on earnings that the
20 transaction will have?

21 A. No, I don't believe so. Just hold a
22 minute. Let me think about that. It will have an
23 impact on earnings, yes. As to whether it's, in your
24 terminology, a benefit to the ratepayer or the
25 customer or the shareholders, I couldn't tell you.

00066

1 Q. Does the negative 27,834,000 number on line
2 28 reflect the cost to customers of sale of the
3 Colstrip assets?

4 A. No, it's just -- it's the sum of line 10
5 through 26. I think if you added in the first two to
6 three lines, the 72,060,000, then you get more of an
7 impact on customers.

8 Q. But the first three lines won't have any
9 impact on customers' rates; is that correct?

10 A. I believe they already have, yes. I'm not
11 trying to be confusing here. The way the merger was
12 set up is that the customers' rates were -- we were
13 told that they were going to be kept constant. We
14 were going to maintain the BPA residential exchange
15 portion of the rates, the rates were going to remain
16 the way they were currently once we adjusted for some
17 PRAM differences, and then they were going to
18 increase at this one to one and a half percent over
19 this time period. They were being given stable
20 rates.

21 The only way the company could maintain
22 those rates is to go out and find the savings that
23 were necessary to get our costs down so that our
24 financials would still be able -- we'd still be
25 financially viable. This is one of the cost savings.

00067

1 Q. If you could turn to page two of Exhibit
2 17. Can you explain why the results on line 28 are
3 different from the results on page one?

4 A. Yes. If you look in the assumptions, you
5 can see the only change there is the CO2 tax. And
6 what we did to estimate an impact of a CO2 tax is we
7 took the low figure from one of the studies that we
8 had and applied it in the year 2008, and that \$10 a
9 ton tax shifted the cost of Colstrip enough compared
10 to market, because it also -- if you do a \$10 a ton
11 tax on CO2, it also impacts the natural gas and
12 everything else. But the impact on coal is so much
13 greater that the benefits are much more favorable to
14 market.

15 Q. Do you believe it's likely that a \$10 per
16 ton CO2 tax will be implemented in the year 2000?

17 A. I believe there's a chance that there could
18 be a tax implemented. We don't know the time frame,
19 we don't know the amount. We're showing the impact
20 if there is one applied. There's been a lot of
21 discussion on that, yes.

22 Q. Did you consider the impact of a Btu tax,
23 if it were adopted, instead of a CO2 tax?

24 A. Btu tax, the way a Btu tax has been defined
25 in the past is a different kind of tax. Like in

00068

1 1994, a Btu tax was proposed, and that was a revenue
2 tax. This is an environmental tax, and a cleanup tax
3 that's -- it's a slightly different animal, so we did
4 not look at a Btu tax, no.

5 Q. If a CO2 tax was implemented, do you
6 believe that it would have any impact on the
7 Company's cost of replacement power for Colstrip?

8 A. Yes, like I mentioned earlier, it does
9 impact natural gas, but at a rate much lower than
10 carbon -- coal.

11 Q. Did you factor that in to the numbers on
12 the market costs of power?

13 A. Yes, we did.

14 MR. VAN CLEVE: I don't have any further
15 questions.

16 JUDGE SCHAER: All right. Mr. Manifold.

17 MR. MANIFOLD: First of all, Your Honor, I
18 just realized we had one more page that should have
19 been in the exhibits for cross that we passed out
20 earlier.

21 JUDGE SCHAER: Okay. Why don't you pass
22 that out. Would you like this added to your other
23 exhibit or is this a separate exhibit?

24 MR. MANIFOLD: It doesn't matter to me.
25 Maybe separate would be good.

00069

1 JUDGE SCHAER: Separate, okay. Then let's
2 mark this for identification as Exhibit 19.

3 C R O S S - E X A M I N A T I O N

4 BY MR. MANIFOLD:

5 Q. Mr. Story, do you have before you what was
6 previously marked as Exhibit 15, which was a thick
7 pad of responses by the Company to Public Counsel
8 data requests?

9 A. Yes.

10 Q. And will you verify that that includes the
11 Company's responses to Public Counsel Data Requests
12 Numbers 12, 17, 31, 33, 52, 53, 55, 59, 75, 76, and
13 portions of 81? Will you accept that, subject to
14 your check?

15 A. Yes, I'll check it.

16 Q. And are these responses true and correct,
17 to the best of your knowledge?

18 A. Yes.

19 MR. MANIFOLD: Your Honor, I'd move for the
20 admission of Exhibit 15.

21 JUDGE SCHAER: Any objection?

22 MR. HARRIS: No.

23 MR. MANIFOLD: I would also like to note,
24 Your Honor, that we put in this portion of exhibit,
25 PC Data Request 81, and we have the complete one with

00070

1 us. If, after looking at this, the Company decides
2 that it would wish to have the rest of it, we'd be
3 happy to do that. These were just portions we felt
4 were relevant.

5 JUDGE SCHAER: I will admit that document
6 at this time, and you may check with Mr. Harris or
7 Ms. Harris at the break and see if they want to have
8 any additional portions added.

9 Q. Mr. Story, what's the current anticipated
10 closing date for the proposed Colstrip sale
11 transaction?

12 A. We were just informed this was probably
13 going to be October 1st.

14 Q. What does that do to when the Company would
15 need an order in this case in order to continue with
16 the transaction? And I think either your or Mr.
17 Gaines' testimony was originally that you were
18 seeking an order by August 1st. I presume that
19 shifts that date back by some period of time?

20 A. I couldn't answer that. It shifts it a
21 little bit. I would have to --

22 Q. Do you want to defer that to Mr. Gaines?

23 A. Yes. Do I get to do that?

24 Q. Is it correct that, at its most recent
25 annual meeting, Puget Sound Energy reported record

00071

1 earnings?

2 A. In what way?

3 Q. In their words, record earnings?

4 A. I wasn't at the annual meeting, so I don't
5 know if those were the words used or not.

6 Q. Would you accept that, subject to your
7 check?

8 A. I mean, what's the context?

9 JUDGE SCHAER: How would he check that, Mr.
10 Manifold?

11 MR. MANIFOLD: Just a moment.

12 JUDGE SCHAER: Mr. Story, you're going to
13 have to speak a little louder. Remember you're
14 speaking to the Commissioners, not to Mr. Manifold.

15 THE WITNESS: Okay.

16 Q. Is part of the function of the annual
17 meeting to report to stockholders on how the
18 Company's been doing?

19 A. I believe so, yes.

20 Q. And there typically are presentations by
21 the senior management of the Company, both orally and
22 in writing?

23 A. Yes. One thing I might just suggest is I
24 was not at the meeting. I know Mr. Gaines was. You
25 might want to talk to him.

00072

1 Q. That's two. Referring to your Exhibit 17,
2 which is the JHS-6, which Mr. Van Cleve was
3 questioning you about?

4 A. Yes.

5 Q. You indicated that this was prepared by you
6 along the lines of the exhibits of Mr. Lazar; is that
7 correct?

8 A. That's correct, and using the allocation
9 between 2001 and 2002, yes.

10 Q. Okay. A difference between this
11 presentation and Mr. Lazar's would be the discount
12 rate, which on yours is shown as 11.83?

13 A. That's correct.

14 Q. And is it correct that the change in the
15 discount rate of a couple of percentage points has a
16 significant effect upon the bottom line numbers?

17 A. It does when you're doing present value
18 analysis. That's why you've got to look at it with
19 sort of what are you looking at that analysis -- I
20 mean, from what point of view are you looking at it.

21 Q. Did you do this analysis using any other
22 discount rates besides 11.83 percent?

23 A. The equivalent type of analysis would have
24 been done with the 7.69, because they would have had
25 the Montana tax change, NERC plan availability and

00073

1 CO2.

2 Q. What were the results of that analysis, and
3 would those have had CO2 tax or no CO2 tax?

4 A. I believe you have the results of that
5 analysis in that -- didn't we provide it with a data
6 response as to -- I'm not sure I have it with me. I
7 take it back. There is one provision in here. The
8 annuity starts 2002, so I'm not sure if we've
9 provided that or not. That would have been one
10 change that would have been different.

11 Q. So do you know what your analysis showed
12 for the 7.69 percent discount rate and no CO2 tax
13 that would be equivalent to your exhibit that shows
14 the cumulative pre-2002 result of roughly \$72 million
15 and a cumulative post-2001 --

16 A. I'm sorry, you've lost me. Could you tell
17 me the assumptions you want run?

18 Q. No, I'm trying to find out what's in the
19 one you ran. My question was -- let's go back. On
20 your JHS-6, page one --

21 A. I have that.

22 Q. Okay. On the -- I guess it's line 28 on
23 the far two right-hand columns, the 72 million and
24 the minus 27 million. You don't have a piece of
25 paper that looks like mine. I'm looking at your

00074

1 JHS-6, which was attached to your rebuttal testimony.

2 A. Sorry. I thought you were asking about
3 scenario six. Okay.

4 Q. Which is Exhibit 17.

5 A. Right.

6 Q. And page one, which is the page Mr. Van
7 Cleve was asking you questions about.

8 A. Yes.

9 Q. On line 28, the last two columns, which
10 show, first of all, the pre -- well, the during the
11 rate plan cumulative present value and the post-rate
12 plan cumulative value. Are we together now?

13 A. Yes.

14 Q. And this analysis that you've shown was
15 done at the discount rate of 11.83 percent?

16 A. Yes.

17 Q. I understood your answer earlier to be that
18 you had done a similar analysis using a 7.69 percent
19 discount rate.

20 JUDGE SCHAER: Is that correct?

21 THE WITNESS: I retracted that, in that
22 there's one assumption on here that I'm not sure we
23 ran with the 7.69, which is the annuity starting
24 2002. We can run that, if you would like it. I
25 mean, it's easy to run.

00075

1 Q. Yes, if you could.

2 A. I'll provide that.

3 JUDGE SCHAER: Record requisition number
4 one?

5 MR. MANIFOLD: Yes. And since this is our,
6 presumably, only hearing date, I'd also like to make
7 a provision to have that come in as an exhibit.

8 JUDGE SCHAER: Let's mark that at this time
9 as Exhibit 20. And we will follow the standard
10 practice, Mr. and Ms. Harris, that you will have 10
11 days after that document is produced, or anyone else
12 here will have 10 days to make any objection as to
13 its entry. Otherwise, it will be entered into the
14 record.

15 And since that's now an exhibit and not
16 just a record requisition, Mr. Story, you will need
17 to provide that to the bench and Commissioners, as
18 well as to the parties.

19 THE WITNESS: All right.

20 MR. CEDARBAUM: Your Honor, could I just
21 ask a clarifying question? Given the briefing date
22 in this case is two weeks from tomorrow, once the
23 record requisition is provided, and add 10 days to
24 that, I don't know how much use that will be in terms
25 of briefing. If we could agree to a shortened

00076

1 turnaround time --

2 THE WITNESS: We can provide it today. I
3 have a copy of the model with me on the computer. We
4 just need a way of printing it out.

5 JUDGE SCHAER: If that can be provided
6 today, should we give you a week from today to
7 object, if anyone objects?

8 MR. HARRIS: I hate to step over my
9 witness. Can we provide that tomorrow and --

10 JUDGE SCHAER: Yes, you may, but I'd like
11 it provided as an e-mail attachment or somewhat
12 provided electronically, so it can be distributed as
13 soon as it's received.

14 MR. MANIFOLD: Tomorrow's fine.

15 JUDGE SCHAER: Would that work for you, Mr.
16 Manifold?

17 MR. MANIFOLD: Yes, and to be clear, it
18 would be provided tomorrow, and then the parties
19 would have five working days from tomorrow to object?

20 JUDGE SCHAER: You'll have till next Friday
21 to indicate if you object to it.

22 THE WITNESS: The only thing you want
23 changed is the discount rate?

24 Q. Yes, so the annuity would be as shown on
25 your exhibit.

00077

1 A. Okay.

2 JUDGE SCHAER: How much more do you have,
3 Mr. Manifold?

4 MR. MANIFOLD: Ten or 15 minutes.

5 JUDGE SCHAER: I was wondering if this
6 would be a good time to break, if that might let you
7 get some of these details we've been running into
8 wrapped up to go a little smoother afterwards.

9 MR. MANIFOLD: Fine.

10 JUDGE SCHAER: Okay. Let's take our
11 morning recess at this time. We'll be off the
12 record.

13 (Recess taken.)

14 JUDGE SCHAER: Let's be back on the record
15 after our morning recess. Want to continue with your
16 questions, Mr. Manifold?

17 MR. MANIFOLD: Yes, thank you.

18 Q. Mr. Story, does Puget's current capital
19 structure have lower cost debt and less equity than
20 capital structure that the Company had and was
21 approved in the last rate case, in UE-921262?

22 A. I think if you look at the actual capital
23 structure, it does, yes, and the equity includes some
24 write-offs from nonsubsidiary type activities.

25 Q. Nonsubsidiary?

00078

1 A. Or non-utility.

2 Q. Non-utility subsidiaries.

3 A. I'm sorry.

4 Q. Do you disagree -- well, you do. Do you
5 disagree with Mr. Lazar on the concept of applying
6 the current debt and current capital structure to an
7 analysis that uses the discount rate? You disagree
8 with the concept of it?

9 A. No, I don't disagree with it. I think it's
10 just another element of information. I mean, if you
11 use a lower discount rate, you get a different
12 answer. It's what do you believe that's going to
13 happen going out into the future. Do you believe
14 those interest rates are going to stay down there? I
15 have no idea. I would guess not.

16 Q. If I understand your testimony, you haven't
17 raised any problem with his arithmetic; it's the
18 concept of which discount rate to apply?

19 A. I'm not even raising a problem with that.
20 I think it's useful information for anybody.
21 Everybody has a different discount rate, and there's
22 all sorts of theoretical books as to what is the
23 appropriate one to use.

24 Q. In your rebuttal testimony exhibit we were
25 just looking at, you have two analyses, both of them

00079

1 use the 11.83 discount rate. One is with a carbon
2 tax and one is without?

3 A. That's correct.

4 Q. Is the 11.83 percent discount rate the 7.69
5 net of tax discount rate with the equity portion
6 grossed up for taxes?

7 A. That's correct. That's the rate that the
8 customer actually pays to the Company so that the
9 Company can earn a 7.69 percent rate.

10 Q. Is it correct that in Puget's last
11 integrated resource plan presented to the Commission
12 in 1992, that Puget used an overall rate of return?

13 A. Puget Power?

14 Q. Yes.

15 A. I believe so.

16 Q. Puget Power, yes.

17 A. Right.

18 Q. And an overall rate of return would be
19 lower than the 11.83 percent that you've used?

20 A. It wouldn't be after you grossed it up for
21 taxes.

22 Q. Would you look at Exhibit 15, pages 15 and
23 16?

24 A. Pages?

25 Q. Fifteen and 16. That's our

00080

1 cross-examination exhibit, Exhibit 15. And pages 15
2 and 16, which is the Company's response to Data
3 Request PC-77?

4 A. Yes.

5 Q. Aren't all of the rates indicated here
6 lower than the 11.83?

7 A. Yes, but they haven't been adjusted for
8 taxes.

9 Q. These were the discount rates that the
10 Company used in both analyses?

11 A. I believe so, yes.

12 Q. Do you know or can you accept, subject to
13 check, that Washington Natural Gas, then Washington
14 Natural Gas, in its last integrated resource plan,
15 which was in 1995, and its most recent one, used a
16 net of tax discount rate rather than an overall rate
17 of return?

18 A. Yes.

19 Q. Can you also confirm that Puget's witness,
20 Dr. Pearl, in Cause U-8354, used a net of tax
21 discount rate and rebutted the Public Counsel witness
22 who had used an overall rate of return?

23 A. Yes, and actually he was, to some extent,
24 rebutting Staff's witness, who had relied on
25 underlying exhibits that used different discount

00081

1 rates for all sorts of different parties, but I think
2 that part of the testimony was struck.

3 Q. Is there any certainty that there will be a
4 carbon tax?

5 A. There's no certainty on any of these
6 assumptions.

7 Q. You have cited a Northwest Power Planning
8 Council as a basis for your carbon tax estimates?

9 A. That's where we got the rate from, yes.

10 Q. Okay. And that was from the council's
11 March 13th, 1996 draft, Fourth Northwest Conservation
12 and Electric Power Plan?

13 A. Mine says adopted on March 13th, 1996.

14 Q. All right. Do you know what discount rate
15 was used by the Northwest Power Planning Council in
16 that plan?

17 A. For what purpose?

18 Q. For -- do you have the plan with you?

19 A. I've got a section of it, Chapter Five.

20 Q. It's Chapter Six, of course.

21 A. I would accept, subject to check, whatever
22 it is.

23 Q. Okay. Would you accept, subject to check,
24 that they used -- in their calculation of
25 distribution of energy savings for alternative

00082

1 futures, they used a 4.75 percent real. And if one
2 took inflation as about two percent, that would
3 result in a roughly seven percent nominal?

4 A. That sounds about right. I would accept
5 it, subject to check.

6 Q. Okay. And page 6-4 would be a cite for
7 that. Do you maintain that the gain on sale being
8 amortized over five years, roughly half of which is
9 during the rate plan and half of which is after the
10 rate plan, represents an equal sharing of the gain
11 between the stockholders and ratepayers?

12 A. No. I think I've already answered that
13 with Mr. Van Cleve.

14 Q. You think it's all going to ratepayers?

15 A. I think there is some sharing in there. I
16 think you can't determine it by looking just at those
17 numbers. The customers have had lower rates during
18 this two and a half years so far, they're going to
19 have lower rates during the next two and a half
20 years, and we're looking for savings to cover our
21 cost increases.

22 Q. Could you turn, please, to what's been
23 marked as Exhibit 19, which is the one-page piece of
24 paper I distributed.

25 MR. MANIFOLD: Your Honor, I've discussed

00083

1 this a little bit with Counsel for the Company and
2 the Staff, and my intent in this document, which I
3 think I will offer as an illustrative exhibit, rather
4 than an exhibit, is to capture, to the extent
5 possible, the positions of the parties on a number of
6 issues in this case to hopefully clarify where the
7 agreements and disagreements are.

8 And so with that understanding, Mr. Story,
9 what I'd like to do is to go through with you as much
10 as you can do, and then, with Mr. Gaines, the column
11 on this marked PSE, and see if we can add values to
12 these and if the values that are there are accurate.

13 JUDGE SCHAER: Mr. Harris, did you have any
14 comment?

15 MR. HARRIS: Well, I don't know if he's
16 offering it yet.

17 MR. MANIFOLD: No, I'm not.

18 JUDGE SCHAER: I don't believe so. I
19 believe he was offering the means that he hopes to
20 use to fill in the blanks and then offer this at some
21 later point as an illustrative exhibit.

22 MR. HARRIS: We don't have any objection to
23 him questioning the witness using this exhibit.

24 JUDGE SCHAER: Using this, okay. Why would
25 it be an illustrative, rather than an exhibit, Mr.

00084

1 Manifold?

2 MR. MANIFOLD: Because Mr. Harris suggested
3 that.

4 JUDGE SCHAER: I won't deal with that now,
5 but please be thinking about how it could be more
6 useful to the Commission, if there were something in
7 here that actually looked like we might want to use
8 it.

9 MR. MANIFOLD: Okay.

10 Q. Mr. Story, are Staff and the Company and
11 Public Counsel all using the same gain on sale for
12 the proposed sale of Colstrip? In other words, is
13 there any disagreement among the parties on what the
14 amount of gain on sale is?

15 A. Well, it's changed.

16 Q. It's changing. It's a moving target, I
17 understand.

18 A. We've all started with 37.6, I believe,
19 yes.

20 Q. Okay. So there's no disagreement among the
21 parties on what the amount of the gain is;
22 disagreements occur on who gets it and how to
23 distribute it?

24 A. Right.

25 Q. Okay. In addition to the gain on sale,

00085

1 there is the issue of what the power cost to the
2 Company will be with and without Colstrip. Would you
3 agree that Staff, Public Counsel and the Company, all
4 three agree that an analysis of power costs with and
5 without the sale needs to be included in the analysis
6 of whether or not this -- on how the dollars work out
7 in this transaction?

8 A. Yes, I believe we all used the same model,
9 which the Company had developed.

10 Q. Okay. Does the Company believe -- well,
11 the Montana property tax changed around the time the
12 Company filed its testimony, or shortly thereafter?

13 A. Yes.

14 Q. The Company and Public Counsel has used the
15 new tax rate in its presentation?

16 A. Right.

17 Q. Does the Company believe it's appropriate
18 to use the new tax rate?

19 A. I believe that it's an appropriate piece of
20 information. And like I say in my rebuttal, you've
21 also got to look at what was behind that tax and
22 you've got to decide whether that tax is going to go
23 up in the future. We've had tax increases constantly
24 in Montana since we've had these plans. I believe
25 the tax went down currently. I personally do not

00086

1 believe that it will stay down. I have no idea when
2 it will go back up again, but they're trying to make
3 up that tax difference out of the general fund, and
4 Montana just does not have a big tax increase.

5 Q. Would it be appropriate, under the PSE
6 column, next to "must include new Montana tax," to
7 put a Y, for yes?

8 A. There's one problem that I've got with your
9 analysis. It's almost like you're saying this is an
10 assumption that must be taken or will have an impact.
11 They all have an impact. Any one of these
12 assumptions can happen. I would say yes, you've got
13 to take into consideration the Montana tax went down.
14 It's a piece of information. Whether it's going to
15 stay that way or not is the important thing. So I
16 would say yes, you can include it. But must include,
17 I don't know.

18 Q. Would you prefer should?

19 A. I think it should be presented. I think it
20 was.

21 Q. Okay. Is it the Company's position that
22 the effect on rates -- or the effect on the Company
23 and effect on rates, both pre- and post-rate plan, is
24 not something that needs to be taken into account?

25 A. I don't really consider that appropriate,

00087

1 no.

2 Q. Okay. So no in the first -- on that line
3 is accurate for the Company?

4 A. Yeah, but it's not because it's a rate plan
5 and post-rate plan. I think we're -- I'm sort of a
6 traditionalist, if you would, under rates anyway.
7 Just because you're not in rates doesn't mean the
8 customer isn't getting the benefit. If you're not
9 coming in for rates, they have a benefit, but a lot
10 of assumptions attached to that.

11 Q. On the next item, under analytical
12 disagreement, was whether to use the Company's base
13 scenario for analysis. What is your or the Company's
14 position on which scenario to use for analyzing this
15 transaction?

16 A. I think all of them have to be used. It
17 shows a wide range of results, and everybody has a
18 different idea what's going to happen in the future.
19 None of these scenarios are meant to be a definitive
20 analysis of what will happen. The base is sort of
21 status quo, if you would, and we know that some of
22 these things are out there and this is the impact it
23 can have on the decision.

24 I think really, when you're looking at this
25 type of analysis, it's much more -- it's way more

00088

1 important to look at the early years than the later
2 years, because as you get out on these kind of
3 analyses, you get into forecast error.

4 And there's been a lot of economists in the
5 paper here just recently about this trillion dollar
6 benefit we have instead of the -- our budget, you
7 know, the country's budget, or surplus. They all say
8 that, you know, just a minor change can make huge
9 differences. The early years are important.

10 Q. So would it be accurate in this column to
11 put, for the company, use all, as opposed to any one?

12 A. I think they all have to be considered.

13 Q. And then, the next one is number of years
14 to analyze power costs. We've put 10 to 20 there
15 because, in your testimony, you use 10, but in some
16 of the charts and exhibits, you use 20. So I wasn't
17 sure what you thought the right time frame to use is.

18 A. I think, as you start getting further out
19 in any analysis, you start running into forecast
20 error, and it would be hard to predict what would be
21 the most appropriate years. We did a 20-year
22 analysis, saying these are some of the impacts under
23 these assumptions. If you get those later years, to
24 rely on those later years and not look at the study
25 in total would be an error. I think you concentrate

00089

1 more on what's happening in the five to 10-year
2 range.

3 Q. So is this accurate to say that the Company
4 looks at 10 to 20 years, or would you say five to 20?

5 A. With that explanation, I don't have a
6 problem with the way you have it here.

7 Q. Okay. Under the next item, under numerical
8 disagreements, we have a line called discount rate
9 for present value purposes. Is it correct that you
10 use 11.83 percent?

11 A. No, we used 7.69, we used 11.83, we used
12 10, and we used 12. We just gave an impact of the
13 discount rates.

14 Q. And you don't prefer one of those over
15 another?

16 A. If I were doing the study, I would use
17 7.69.

18 Q. And that's what's shown on the next line as
19 the carrying cost of Colstrip?

20 A. That's our net of tax rate of return.

21 Q. So your preference would be to use the 7.69
22 as the discount rate for present value, as well as
23 for the carrying cost of Colstrip?

24 A. If I was doing it strictly from an
25 analytical point of view, trying to make a decision

00090

1 as to which way is the best way to go, I would use
2 7.69, or whatever the discounted rate would be.

3 Q. But what I'm understanding from what you're
4 saying is that the Company has used 7.69, 10, 12, and
5 11.83 percent, and your personal preference, if you
6 chose one, would be to use 7.69?

7 A. Yeah. I would also want to know what the
8 impact of discount rates are, because if you get an
9 answer, say a 7.69 on an analytical study, and you
10 get one answer that seems to support your decision
11 and you would expect it to carry out through the
12 different discount rates, you would want to know what
13 caused that answer to go to a negative, if it were to
14 go to a negative in the future. You'd want to make
15 sure your analytical support and numbers were
16 appropriate.

17 Q. So you do a sensitivity analysis?

18 A. Yeah.

19 Q. I didn't mean to interrupt.

20 A. It's sort of that. It's more of a check of
21 the underlying assumptions, to some extent.

22 Q. End effects. The Company's position is
23 that that should not be considered?

24 A. I don't know what he did.

25 Q. What is the Company's position on whether

00091

1 end effects themselves should be considered?

2 A. I think they should and I think we did.

3 Q. Okay. So instead of an N there, I should
4 have a Y, for yes?

5 A. Yes. I'm not sure what Mr. Lazar did.

6 Q. Where did you consider end effects in your
7 analysis?

8 A. To me, end effects is --

9 Q. Beyond the 20 years?

10 A. Well, if you're calling end effects what
11 happens to the balance at the end of a time period,
12 that's not what I call end effects. End effects is,
13 to me, and the way it's been used in rate-making
14 before, is you have two resources. They may have
15 different lives. You have to put those resources on
16 a comparable basis. If one is 20 years and one is 10
17 years, you've got to assume what's going to happen in
18 that 10-year period beyond the first resource that
19 was ten years.

20 By comparing to market, that is our second
21 resource. We did that throughout the study. We just
22 had to have -- we happened to have a balance on
23 Colstrip at the end of our study that had to be
24 recovered, and that's what we -- we amortized that --
25 we did it two ways. We amortized it over the

00092

1 remaining life of the plan, which included this sale
2 period, and we also did it as a lump sum at the end
3 of that time period. The reason we used 2018 was
4 it's sort of the mid-range of the retirement dates of
5 those plans.

6 Q. Does your analysis implicitly assume that
7 the plant has zero salvage value at the -- or market
8 value at the year 2018?

9 A. I think the analysis, the way it was done,
10 does lend one to go to that assumption. We did not
11 do any major upgrades to the plan. We did not do any
12 rewinds. We used a normal budget. We basically,
13 under that analysis, are running that plant into the
14 ground. And to go beyond 2018, there would have to
15 be major upgrades done to it.

16 We actually, on One and Two, we extended it
17 way beyond its life. We used -- its coal contract is
18 up in 2009, and we went to market coal, which would
19 be required under the contract, and we extended it
20 out to 2018, which is -- and just using normal budget
21 dollars, no major upgrades. So basically, we were
22 running those plants, for this analysis, into the
23 ground.

24 Q. In real life, do owners typically run
25 plants into the ground or do they make improvements

00093

1 in the out years in order to prolong the life of the
2 plant?

3 A. It depends on the plant. The coal, like in
4 this particular plant, we would have to look and see
5 what the availability of coal is. By the time 2019
6 rolls around, we've used the cheap coal that's
7 available in Montana. You're now dealing with the
8 coal that has a much heavier burden on top of it,
9 much more expensive to mine, get out, and use in the
10 plant. We would have to look at replacement fuel for
11 it.

12 I think you would maintain the plant to get
13 the most out of it, and if that included extending
14 the life, then you would have to do some major
15 upgrades. But if it just meant to run it until the
16 end of your coal contracts, you would do something
17 else.

18 Q. Carbon tax is the next line. You think the
19 possibility of a carbon tax should be taken into
20 account as part of the analysis?

21 A. I think the impact of a carbon tax, if it's
22 put into place, has to be taken into consideration,
23 what is the impact on that carbon tax on this type of
24 plant versus market, and that's what we did. To get
25 that impact, we used the \$10 rating out of that plan,

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1 which is a \$95 rate, and we didn't adjust it. We
2 started using it in 2008, which is well into this --
3 what everybody's saying is where you're going to have
4 to take into consideration carbon dioxide. So we
5 just wanted to show the impact if that is started up.
6 I mean, if that tax is passed, it has a major impact
7 on coal.

8 Q. So the answer to my question is yes?

9 A. Yes.

10 Q. Okay.

11 A. It's an important piece of information.

12 Q. In analyzing the net benefit, the company
13 uses a present value analysis, as opposed to a
14 nominal value analysis?

15 A. Actually, you can look at both. Present
16 value is there, nominal is there also.

17 Q. What would be your preferred? If you're
18 doing the analysis, what would be the way you would
19 look at it?

20 A. I would look at both.

21 MR. MANIFOLD: Your Honor, that concludes
22 my questions. I don't think I'm going to try and
23 populate the bottom part of this chart, because it's
24 taking so long to get yeses and nos that I'm not sure
25 it's of value at this point. If the bench or the

00095

1 Commissioners have some use for this and find it
2 useful, I'd be happy to slog ahead, but under the --
3 I think, with the additional exhibit we're going to
4 be getting, which will assist in populating the
5 bottom, that I would stop my questions.

6 JUDGE SCHAER: Okay. So Exhibit 19 will
7 continue as being identified. Are you saying you're
8 not going to offer it or --

9 MR. MANIFOLD: Not at this time.

10 JUDGE SCHAER: Not at this time, okay.
11 I'll just continue to leave it in exhibit limbo,
12 then. Commissioners, did you have questions for Mr.
13 Story?

14 COMMISSIONER HEMSTAD: I have a couple.

15 E X A M I N A T I O N

16 BY COMMISSIONER HEMSTAD:

17 Q. I take it from your testimony, and perhaps
18 Mr. Gaines also, that the fact of the merger having
19 occurred would not have affected your decision to
20 make this sale?

21 A. I think this opportunity was a good
22 opportunity. I think we would have made the sale if
23 everything else being equal, yes, or tried -- I mean,
24 we would be proposing this.

25 Q. So the consequence of the transaction would

00096

1 have been whether the merger would have occurred or
2 not?

3 A. I believe so, yes.

4 Q. But at the same time, it's the Company's
5 position that the benefits of the sale should be
6 taken into account in the context of the efficiencies
7 from the merger?

8 A. I believe so. The difference between not
9 being under the merger plan and, you know, basically
10 under regulation is that we, most probably, during
11 these last couple years, would have been coming in
12 for rate increases. I mean, the rate pressures were
13 there. And I think it would have been a whole
14 different mechanism as to how we handled this.

15 Right now, the customer rates are already
16 lower, and what we're trying to do is apply savings
17 to costs.

18 Q. If the merger hadn't have occurred, would
19 you still be applying a five-year amortization plan?

20 A. I believe so.

21 COMMISSIONER HEMSTAD: That's all I have.

22 COMMISSIONER GILLIS: No.

23 E X A M I N A T I O N

24 BY CHAIRWOMAN SHOWALTER:

25 Q. I have one question, and that is about

00097

1 deferred accounting that -- one of the suggestions is
2 that this be approved, but accounting deferred, and
3 I'm not too certain of your rebuttal testimony. Is
4 it that that would deprive the Company of that money,
5 or would it have the use of a deferred account before
6 the next rate case?

7 A. Well, the impact of a deferral is to
8 actually hit us on the financial income statement.
9 The gain that is here, plus the lower power costs,
10 would not be reflected in our financials. And with
11 the cost increases that we're trying to cover with
12 some of this, that would be quite a financial impact
13 on the Company.

14 Deferral means to take everything out of
15 your income statement, put it on your balance sheet
16 till sometime in the future. The way Staff has
17 proposed to do that is not what I would call
18 traditional rate-making, you know. That label has
19 been put on it. I have never seen a case where
20 you've taken one power contract out of a portfolio
21 and defer the difference between that power cost
22 contract and the market value based on forecasts.

23 There are different ways of handling
24 deferrals, and I mean, we've done some research as to
25 what's been happening around the country.

00098

1 Commissions vary all over the place as to what is the
2 appropriate deferral and amortization of something
3 like a gain. They vary widely, but three to five
4 years seems to be quite common.

5 Q. So am I right you're drawing a distinction
6 between cash flow or the use of the money versus
7 where it goes or doesn't go on your income statement,
8 and that that, the latter, is a major concern of
9 yours?

10 A. Yes, the cash actually involved in this
11 deal is quite different than the gain. The gain is
12 just a -- it's a calculation as to profit or loss.
13 The actual cash associated with a deal like this is
14 much different. And what we're arguing about is
15 really how it's going to impact the income statement.

16 JUDGE SCHAER: Anything further from
17 Commissioners?

18 COMMISSIONER GILLIS: No.

19 JUDGE SCHAER: I have a few questions, Mr.
20 Story.

21 E X A M I N A T I O N

22 BY JUDGE SCHAER:

23 Q. How have excess deferred taxes been treated
24 by Puget, and now PSE, since the Tax Reform Act of
25 1986?

00099

1 A. They've been turning around under the
2 normal schedule. Under normalization, you put the
3 difference between your straight-line depreciation
4 and your accelerated depreciation basically on your
5 balance sheet, and as the plant goes through its life
6 and gets out into the years where you can't take
7 accelerated depreciation, those taxes turn around.
8 So they're on the balance sheet right now and they're
9 turning around under the normal schedule.

10 Q. And that would be normalized deferred
11 taxes?

12 A. Yes.

13 Q. Would you tell me what you've been doing
14 with the excess deferred taxes?

15 A. Same thing. They still follow the plant
16 life; they're just at a rate that's different than 35
17 percent.

18 Q. Are you aware of any normalizations of
19 excess deferred taxes over a short span, say five to
20 ten years?

21 A. I would be surprised if there were, because
22 that would be a violation of normalization rules.
23 And violation of normalization rules carry a severe
24 penalty from the IRS.

25 Q. So in looking at short-span normalization

00100

1 periods, do you believe that those violate the IRS
2 normalization rules?

3 A. I would have to see the example exactly as
4 to what's going on, but if you return normalized
5 taxes quicker than rateably, you violate the
6 normalization rules.

7 Q. Mr. Story, you were a witness in the merger
8 case, were you not, sir?

9 A. Yes.

10 Q. Are you familiar with the order in that
11 case?

12 A. Yes, I am.

13 Q. And that order assigns several tasks to the
14 merged company that should take place after the
15 merger was approved; is that correct?

16 A. Yes.

17 Q. And one of those tasks that the Company was
18 told to undertake was to prepare and file an
19 integrated resource plan; is that correct?

20 A. I believe so, yes.

21 Q. And has the Company done that?

22 A. I could not tell you.

23 Q. Okay. Between filings of plans with the
24 Commission, does the Company keep that kind of
25 analysis ongoing in its own work?

00101

1 A. Most probably not in the format it gets
2 filed. We have analytical work going on constantly
3 as to what's happened. A lot of that's used to put
4 the plan together. So I'd say the type of work is
5 being done. It may not be in the right format for
6 that type of filing.

7 Q. Okay. Well, if you would accept as a
8 hypothetical that you have not filed an integrated
9 resource plan since the time of the merger, is there
10 some kind of in-house document like that that Puget
11 used to analyze the idea of whether or not it should
12 sell its Colstrip assets?

13 A. What we used was the Morgan Stanley
14 analysis as to the appropriateness of the price and
15 we've used this model that we've been talking about
16 to show benefits, and I think Mr. Gaines would have
17 to address any other type of items that may have been
18 used elsewhere. That's what I was involved in. I
19 wasn't really involved with the Morgan Stanley, but I
20 was with the scenario.

21 Q. Would you tell me a little bit more about
22 the analysis that you were involved in?

23 A. What we did is we estimated the cost of
24 Colstrip going out to the year 2018, using pretty
25 basic assumptions. We knew what the plant value was

00102

1 now, we knew what our budgets were going out into the
2 future, we have an idea of what our transmission is
3 and the costs associated with that. We came up with
4 a weighted cost of Colstrip going out those 20 years.

5 Then we ran some models that were sort of
6 Northwest-oriented as to what we thought the market
7 prices would be, and we compared the Colstrip value
8 to the market prices. And that's -- these present
9 values that we've been talking about for the last
10 hour or so are the results of those studies.

11 Q. Okay. And so those are the studies that
12 you have filed with your testimony already in this
13 proceeding?

14 A. They're actually filed with Mr. Gaines'
15 testimony, but yes.

16 Q. Okay. When you were discussing what's been
17 marked for identification as Exhibit 19 with Mr.
18 Manifold, you were discussing a sensitivity analysis,
19 and you were saying that what you really had done was
20 not a sensitivity analysis, but a recheck of
21 underlying assumptions. Did I understand your
22 testimony on that correctly?

23 A. I think what I was talking about there is
24 discount rates. And you know, if you get a result
25 with one discount rate that seems to give you one

00103

1 answer, yes, no, and you get a difference with a
2 different discount rate -- and it's not unusual to do
3 that. I mean, the answer may go no-yes, you know,
4 just the opposite of what the first one gave you. I
5 think when you get that result, you do take a look at
6 your underlying assumptions and see if there's
7 anything in there that causes that switch just
8 because of discount rates. That's the context of
9 that.

10 Q. And what was your analysis that you did on
11 that?

12 A. On this? We did run this at different
13 discount rates. I think we -- what we look at is we
14 didn't segregate it the way Staff and Public Counsel
15 would do it. We looked at the benefit of the
16 customers over the five, 10, 15-year period, and
17 actually, almost all the studies, the nominal
18 difference changes right about 2004. That's where
19 Colstrip, under these studies, becomes cheaper than
20 market.

21 The other thing we did is we look at what
22 is the present value buildup of the benefit to the
23 customer over this time period, and that generally
24 stretches the benefit for the customer out well
25 beyond that, because they have this cumulative

00104

1 benefit built up, and you look at that. You look at
2 the underlying assumptions as to how strongly do you
3 feel that a certain item will change.

4 I think what Mr. Lazar did on the interest
5 rate is fine. If you believe interest rates are
6 going to go down and stay down over this 20-year
7 period, it's most probably appropriate. We gave
8 several scenarios showing different interest rates in
9 effect.

10 It's all to give somebody a broad idea as
11 to the range of answers you can get when you look at
12 an analysis like this. I think under all of them, as
13 you get out into the later years, you start running
14 into forecast error. So we tend to weight a little
15 bit heavier to the front years.

16 Q. Okay. Now, you talked to me about the
17 Morgan Stanley analysis that was done when you were
18 looking at price under the possibility of sale. What
19 kind of analysis was done before that to determine
20 whether Colstrip should be for sale at all or not?

21 A. I think you'd have to talk to Mr. Gaines.
22 He was involved in those discussions.

23 Q. And you were not?

24 A. No, I was not.

25 Q. Okay. And do you know whether those

00105

1 discussions took place in an atmosphere of looking at
2 longer term planning, either with an IRP or with the
3 Company's business plan?

4 A. No, I don't. I can look at the results of
5 the studies and, you know, some of them are done on
6 DCF, you know, basically trying to give us a value of
7 the plant to market. I'm not sure what was done with
8 the IRP or anything like that. I know that there was
9 a lot of different looks and cuts taken on this
10 transaction to see if it was potentially a good sale,
11 and once we started down the road that it was a good
12 sale, we did even more analysis to say this really is
13 a benefit. I mean, it's a decision process that
14 builds up over time.

15 Q. Now, you've discussed quite a bit this
16 morning that Puget has been looking for savings that
17 it can apply to its costs; is that correct?

18 A. Right.

19 Q. And you would view the outcome of this sale
20 as producing savings for Puget that it could apply to
21 its costs; is that correct?

22 A. Yes.

23 Q. Because I'm a little bit concerned, because
24 it seems to me that you're starting to sell your
25 capital instead of just dealing with expenses, and so

00106

1 something my grandfather said to me once is probably
2 what's leading to my disturbance about that. But do
3 you think that these really are savings when you're
4 selling something that's part of your capital?

5 A. I think Mr. Gaines really addressed that in
6 his testimony, but no, that's one of the items you
7 have to look at as to when you start giving up
8 capacity and start relying on the market, what are
9 the trade-offs. I think the Company feels that it --
10 and I feel, too, that for this particular
11 transaction, we do have other alternatives that are
12 most probably more cost effective.

13 Where you get to the point of giving up so
14 much capacity that you become weakened in the market,
15 I'm not sure that we're near that point. It can
16 happen, I think.

17 Q. I guess what's -- excuse me, go ahead.

18 A. I think one thing you see in the trading
19 right now, you know, a lot of marketers are out there
20 buying capacity, because they want to have something
21 that will back up their trades. We still have a lot
22 of capacity, hard generation.

23 Q. I guess what I'm wishing that we had seen
24 in this testimony was some kind of analysis of your
25 capacity long-term and how much you could sell and

00107

1 what you should sell and what you should keep, and
2 that's, again, why I'm looking for the IRP or
3 something else that you did saying we should sell
4 this or not sell this.

5 Do you know of anything like that that
6 exists that could guide the Commission in examining
7 this sale, or proposed sale?

8 A. I was just trying to think of anything that
9 I was involved with. I can't speak -- I guess I
10 can't answer that question, because I wasn't involved
11 in anything like that.

12 Q. Okay. And one last question. If one were
13 to look at the merger order and look at what that
14 order says about the kinds of savings that result
15 from the merger, like getting rid of duplicate
16 substations and duplicate business offices and then
17 were to read the next provision as saying that all
18 other sales are to be treated like the settlement
19 agreement for property sales, and we're to conclude
20 from that that this sale should be treated like
21 those, would that change Puget's analysis of whether
22 the sale was a good idea?

23 A. Well, part of the question is settlement
24 agreement on the property sales. That settlement
25 agreement deals strictly with non-depreciable

00108

1 property, and that's all.

2 Q. Well, I understand that that's the position
3 the Company is taking. I'm just trying to ask you a
4 hypothetical question. If one were to read that as
5 meaning that all other sales that weren't
6 duplications and savings from combining the two
7 utilities were to be treated in a manner consistent
8 with that settlement, and that was how the Commission
9 decided to treat this sale, would the sale still be
10 attractive to Puget, PSE?

11 A. I've not done that analysis. What we've
12 presented here is the way the Company would like to
13 have this reflected in the income statement. And
14 what you're saying is we wouldn't allow that in the
15 income statement that way. That becomes a board of
16 directors decision as to whether the sale was
17 beneficial or not.

18 It's kind of a hypothetical that I really
19 can't answer, because under our reading of that order
20 and the reading of the property stipulation, it
21 specifically says non-depreciable property, and it
22 was written that way because we knew that depreciable
23 property was already handled under the accounting
24 guidelines, and so was operating units. There was
25 specific rules for those. There was no specific rule

00109

1 for basically non-depreciable real property as land.

2 Q. So as far as you know, the Company has not
3 discussed what their reaction would be if the sale
4 were approved, but accounting petition were not the
5 one that you had requested -- accounting treatment
6 were not the one you had requested?

7 A. I think the Company would have to look at
8 it in the environment of that order. To sit here and
9 try to figure out exactly what that order means to
10 the Company, I can't do right now, but, you know, the
11 board of directors has reserved the right to the
12 final approval of this, and it's not -- I think they
13 would have to make that decision. And we would do it
14 under the conditions of the order, that we would look
15 at it.

16 If it was to say none of these -- none of
17 this gain or, to adopt Staff's position of deferring
18 everything like it was deferred, I can't speak for
19 the board, but I would find that very hard to accept.

20 Q. By that, you mean you probably would not
21 recommend they go through with the sale?

22 A. I wouldn't be the one recommending it one
23 way or the other.

24 Q. Okay.

25 A. I personally would find it hard to accept.

00110

1 JUDGE SCHAER: Any redirect for this
2 witness?

3 MR. HARRIS: Very short.

4 R E D I R E C T E X A M I N A T I O N

5 BY MR. HARRIS:

6 Q. Four or five brief subjects. You were
7 asked a number of questions, Mr. Story, about your
8 exhibit, which is now in the record as Exhibit 17.
9 It's JHS-6. It's a two-page exhibit.

10 A. Yes.

11 Q. And in that exhibit, you included an
12 assumption about a CO2 tax, and I think the testimony
13 was a little unclear about when the CO2 tax was
14 assumed to start.

15 A. It was assumed to start in the year 2008.

16 Q. And the amount of the CO2 tax, was that set
17 in dollars, assuming that it had been increased over
18 time to 2008?

19 A. No, it's using the \$10 rate, which, out of
20 that study, was the 1995 \$10 rate.

21 Q. And do you believe that's a conservative
22 estimate of what a CO2 tax could be?

23 A. I believe it's very conservative, yes, if
24 it was to be --

25 Q. Next subject. You were asked a number of

00111

1 different questions about the Company's earnings and
2 its financial performance during this time period.
3 You mentioned cost pressures. Can you identify any
4 of the unexpected cost pressures the Company has
5 faced during this rate plan period, or anticipates
6 facing through the end of it?

7 A. Yes, one of them is mentioned in Mr.
8 Gaines' testimony. And it may not have been
9 unexpected from the merger order or the stipulation,
10 but it was unexpected from the time we filed the
11 merger, and that was the carrying of BPA residential
12 exchange in excess of what we're getting from the
13 BPA. Over this time period, the five-year time
14 period, that's looking about \$303 million of
15 additional expense. Part of that is offset against
16 the rate increase, I would assume, but it's still a
17 sizable number.

18 The merger costs were estimated to be
19 around \$30 million, and turned out to be \$59 million.
20 Some of our systems that we thought we could combine,
21 like computer systems and -- actually, as you get rid
22 of the employees, cut back on the work force through
23 the merger, we were expecting computer system
24 savings, and it did not happen. The expenses
25 actually went up several million dollars. That's a

00112

1 capital item, but the depreciation still hits the
2 books.

3 Y2K has been much more expensive than we
4 anticipated, and even upgrading our accounting
5 systems so they will get through Y2K became a very
6 expensive project. We actually had to throw out the
7 two old accounting systems, and we put in a new
8 accounting system, which is SAP. There were quite a
9 few surprises.

10 Q. Next subject. You were asked a number of
11 questions about Mr. Flaherty, who was a witness
12 during the merger proceeding. Was he the merger
13 synergy savings witness?

14 A. Yes, he was.

15 Q. Was he asked to analyze power cost savings
16 in any way?

17 A. No.

18 Q. Was he asked to analyze the Company's power
19 portfolio in any way?

20 A. No, he didn't have the availability to do
21 that.

22 Q. Was that an area of expertise that he had?

23 A. No.

24 Q. Next subject. Let's turn to KLE-3, which
25 is Exhibit 18. It's Mr. Elgin's exhibit, but do you

00113

1 have that?

2 A. Yes, I do.

3 Q. Okay.

4 JUDGE SCHAER: Just a moment, Counsel.

5 What are you referring to?

6 MR. HARRIS: Exhibit 18 is what I have it

7 down as. It's KLE-3.

8 JUDGE SCHAER: I don't believe Mr. Elgin's

9 exhibits have been admitted.

10 MR. HARRIS: I'm sorry, you're right. It's

11 KLE-3, and it's not admitted yet.

12 JUDGE SCHAER: I don't believe it's even

13 been marked for identification, because Exhibit 18 is

14 JHS-7.

15 MR. HARRIS: I had anticipated the wrong

16 exhibit number when I was doing this. My apologies.

17 It's just KLE-3, and it's a single page.

18 JUDGE SCHAER: And that's an exhibit that

19 may be offered in this proceeding at this point?

20 MR. HARRIS: Yes, that's correct.

21 Q. Do you see the page that starts Exhibit D

22 on the top?

23 A. Yes.

24 Q. Can you describe what that is, please?

25 A. The top portion was actually an exhibit out

00114

1 of our merger filing, which was CEL-3. Ms. Lynch had
2 this in her exhibit. What it does is it takes our
3 power costs, as projected into the future, puts them
4 into a unit cost basis so that we get the impact of
5 growth and revenues due to kilowatt hour growth, and
6 we take the difference between these unit costs, and
7 that's the piece that's not covered by rate increases
8 or rate that's coming in from growth and customer
9 usage, and it calculates the increase in our power
10 cost over the five-year rate stability period on a
11 revenues not to cover that type of cost, and it's
12 \$322 million.

13 Q. And I think you made clear in your
14 testimony that this exhibit, which was used to
15 support the merger stipulation, in part, that it does
16 not reflect the sale of Colstrip facilities or the
17 savings associated with the sale of the Colstrip
18 facilities; is that correct?

19 A. No, it wouldn't have.

20 Q. Does it reflect any of the power cost
21 savings that were achieved in the Tenaska
22 renegotiation?

23 A. No, it doesn't.

24 Q. Does it reflect any of the power cost
25 savings achieved as the result of the Montana Power

00115

1 litigation negotiation?

2 A. No, it wouldn't.

3 Q. Does it reflect any of the power cost
4 savings that were anticipated as of the time of the
5 merger?

6 A. No, it wouldn't.

7 Q. Last subject. You were asked some
8 questions about whether this sale or this potential
9 sale, this opportunity would have arisen absent the
10 merger, and whether the savings, possible savings,
11 would have arisen absent the merger. Would the
12 Tenaska Power contract renegotiation, would that
13 opportunity have arisen absent the merger?

14 A. I believe so.

15 Q. Was that dependent in any way on the
16 merger?

17 A. Not that I'm aware of.

18 Q. And what about the Montana Power litigation
19 negotiation? Was that dependent on the merger?

20 A. No.

21 Q. Would that opportunity have arisen absent
22 the merger?

23 A. I believe so.

24 MR. HARRIS: No further questions.

25 JUDGE SCHAER: Is there anything further

00116

1 for this witness?

2 MR. CEDARBAUM: I just have three or four
3 questions.

4 JUDGE SCHAER: Go ahead.

5 R E C R O S S - E X A M I N A T I O N

6 BY MR. CEDARBAUM:

7 Q. Mr. Story, you may have misspoken during
8 your earlier testimony, but I believe I heard you
9 refer to the Colstrip facility's power contract.
10 It's not a purchase power contract. These are
11 production facilities that Puget Sound Energy owns,
12 in part?

13 A. Yeah, that's correct. I was thinking of an
14 analytical term.

15 Q. You also referred a while ago this morning
16 to a \$74 million rate filing, and I believe that was
17 with respect to a filing the Company would have made
18 absent the rate plan; is that right?

19 A. That's correct.

20 Q. That was a filing you said the Company
21 would have made subject to analysis by Staff and
22 other parties; is that right?

23 A. Right. And that's one thing that we were

24 --

25 Q. Excuse me, your answer was yes?

00117

1 A. Yes, that's correct. And just to go beyond
2 that a little bit --

3 JUDGE SCHAER: Go ahead, Mr. Cedarbaum.

4 Q. Mr. Story, the question, I think, has been
5 answered.

6 A. Okay.

7 Q. And that would have been subject to
8 suspension by the Commission and setting for hearing,
9 as well?

10 A. Yes.

11 Q. So it's not your testimony that the
12 Commission would have approved that \$74 million?

13 A. No, generally, the rate that you file is
14 not the rate that you get, but it could cause you to
15 file again.

16 Q. It could have been -- the Commission could
17 have approved nothing?

18 A. Right, and I think the Company would have
19 turned around and filed again.

20 Q. Finally, with respect to your testimony,
21 Mr. Flaherty, as I recall, his job in the merger was
22 to quantify and identify savings solely attributable
23 to the combination of Washington Natural Gas and
24 Puget Power Sound and Light; is that right?

25 A. Right.

00118

1 Q. He did not look at savings that would have
2 been gained by either company separately?

3 A. I don't believe so.

4 MR. CEDARBAUM: Thank you.

5 JUDGE SCHAER: Anything further, Mr.

6 Manifold?

7 MR. MANIFOLD: Yeah, just, I think, one
8 question.

9 R E C R O S S - E X A M I N A T I O N

10 BY MR. MANIFOLD:

11 Q. In response to the Chairwoman's questions,
12 you were talking about the cash -- the difference
13 between cash versus effect on income statement. What
14 is the amount of cash due the Company from this
15 proposed transaction?

16 A. Oh, I don't have that number with me, but
17 it's most probably over \$300 million.

18 MR. MANIFOLD: Okay. Thanks.

19 JUDGE SCHAER: Mr. Van Cleve?

20 MR. VAN CLEVE: I have one question.

21 R E C R O S S - E X A M I N A T I O N

22 BY MR. VAN CLEVE:

23 Q. Have the Company's revenues from sales
24 under Schedule 48 been significantly higher than was
25 anticipated at the time the rate plan stipulation was

00119

1 entered into?

2 A. I'd have to ask you where in my testimony
3 you're getting that from.

4 Q. I'm not getting it from your testimony; I'm
5 just asking if you know.

6 A. I have no knowledge of that.

7 MR. VAN CLEVE: I don't have any other
8 questions.

9 JUDGE SCHAER: Okay. Anything further for
10 Mr. Story? Commissioners? Thank you for your
11 testimony. Let's be off the record for a moment.

12 (Discussion off the record.)

13 JUDGE SCHAER: Let's be back on the record.
14 We're going to take our luncheon break right now and
15 would ask everyone to be back promptly at 1:15, and
16 I'd ask you to have Mr. Gaines set up to be sworn in
17 and all exhibits for Mr. Gaines to be distributed at
18 that time, please. We're off the record.

19 (Lunch recess taken.)

20 JUDGE SCHAER: Let's be back on the record
21 after our lunch break. Just before the lunch break
22 concluded, Mr. Story left the stand, and I realized
23 that I had a couple of a bench requests for Mr. Story
24 that I did not get asked before the break, so I would
25 like to ask them now.

00120

1 Mr. Story, if you wouldn't mind either just
2 speaking from where you are or walking up next to Mr.
3 Gaines just to let me know if there are any problems
4 you have understanding these. I'll remind you that
5 you're still under oath.

6 I'm going to go ahead and give these bench
7 request responses an exhibit number, since this is
8 our only hearing. So these will be Exhibit Number
9 21. And I am going to ask you, also, how quickly
10 these can be provided. So when you hear them, think
11 about that, please.

12 The first request is please provide a copy
13 of IRS letter ruling, dated November 13th, 1998,
14 which is referenced on page five, paragraph eight of
15 your testimony.

16 MR. STORY: We can provide that right now,
17 if somebody would make a copy.

18 JUDGE SCHAER: Okay. Well, why don't you
19 have that provided and get copies made at the break.
20 The second request is please provide the calculations
21 arriving at the accumulated deferred tax amount for
22 the Colstrip facility. Please provide calculations
23 for regular accumulated deferred and excess deferred
24 taxes.

25 MR. MANIFOLD: Is that the same number?

00121

1 MR. STORY: Is that Exhibit 22?

2 JUDGE SCHAER: Oh, no -- yeah, let's make
3 that Exhibit 22. We'll give them all separate
4 numbers.

5 MR. STORY: I currently have that with me.
6 I'm just not sure which scenario it was run off of.
7 And the date's been changing, from July 1 to
8 September 1. I can provide the one I have right now.

9 JUDGE SCHAER: Okay, thank you. And then
10 the third question is please provide a calculation
11 for the Montana tax decrease of \$2,340,000. That
12 would be 23.

13 MR. STORY: I can provide that right now,
14 too.

15 JUDGE SCHAER: All right. So I will expect
16 those to be provided during our next break through
17 your counsel.

18 MR. STORY: Where can I get copies?

19 MR. HARRIS: We'll work that out at a
20 break.

21 JUDGE SCHAER: We'll work that out off the
22 record, all right. So Mr. Harris, are you ready to
23 call your next witness, then?

24 MR. HARRIS: Sure. PSE calls William
25 Gaines as its second and final witness.

00122

1 JUDGE SCHAER: Mr. Gaines, would you raise
2 your right hand, please.
3 Whereupon,

4 WILLIAM A. GAINES,
5 having been first duly sworn by Judge Schaer, was
6 called as a witness herein and was examined and
7 testified as follows:

8 JUDGE SCHAER: Your witness is sworn, Mr.
9 Harris.

10 D I R E C T E X A M I N A T I O N

11 BY MR. HARRIS:

12 Q. Good afternoon, Mr. Gaines. Do you have
13 with you what's been marked previously for
14 identification as Exhibit T-6, which is your direct
15 testimony?

16 A. Yes, I have.

17 Q. And do you also have Exhibits WAG-1 through
18 WAG-5, which have been pre-marked as Exhibits 7
19 through 11?

20 A. I have.

21 Q. And do you also have Exhibit WAG-16, your
22 rebuttal testimony?

23 A. Yes, I have.

24 MR. HARRIS: Could we have that marked for
25 identification, Your Honor?

00123

1 JUDGE SCHAER: I'm marking for
2 identification at this time Exhibit T-24, which would
3 be Mr. Gaines' rebuttal testimony.

4 Q. Do you have any corrections to make to
5 Exhibit T-6, your direct testimony?

6 A. No.

7 Q. Do you have any corrections to make to
8 Exhibit 24, your rebuttal testimony?

9 A. No.

10 Q. Is Exhibit T-6 complete and accurate, to
11 the best of your knowledge?

12 A. Yes, it is.

13 Q. And is Exhibit 24 complete and accurate, to
14 the best of your knowledge?

15 A. Yes, it is.

16 MR. HARRIS: At this time, Your Honor, PSE
17 would offer Exhibits T-6, Exhibits 7, 8, 9, 10, 11,
18 and Exhibit -- I believe -- I'm sorry, it's T-24.

19 JUDGE SCHAER: Yes. Any objections? Those
20 documents are admitted.

21 MR. HARRIS: Mr. Gaines is available for
22 cross-examination.

23 JUDGE SCHAER: Mr. Cedarbaum.

24 MR. CEDARBAUM: Good afternoon, Mr. Gaines.
25 Your Honor, if I could have marked for identification

00124

1 the three exhibits that I pre-distributed this
2 afternoon.

3 JUDGE SCHAER: Certainly. Mr. Cedarbaum
4 has pre-distributed this afternoon, and you'll find
5 in front of you, Commissioners, a document entitled
6 Data Request Number 15, which we'll mark for
7 identification as Exhibit 25. A document entitled
8 Data Request Number 22, which we will mark for
9 identification as Exhibit 26. And the 14th
10 Supplemental Order Accepting Stipulation, Including
11 Merger, in Dockets Numbered UE-951270 and 960195,
12 which we'll mark as Exhibit 27.

13 MR. CEDARBAUM: Thank you.

14 C R O S S - E X A M I N A T I O N

15 BY MR. CEDARBAUM:

16 Q. Mr. Gaines, referring you to Exhibits 25
17 and 26 for identification, do you recognize those as
18 your responses to Staff Data Requests 15 and 22?

19 A. Yes, I do.

20 MR. CEDARBAUM: Your Honor, I would offer
21 Exhibits 25 and 26.

22 JUDGE SCHAER: Any objections?

23 MR. HARRIS: No.

24 JUDGE SCHAER: Those documents are
25 admitted.

00125

1 Q. Referring you to Exhibit Number 27, Mr.
2 Gaines, do you recognize that as the Commission's
3 14th Supplemental Order in the merger proceeding with
4 the attached stipulation?

5 A. Yes, I do.

6 Q. This is the order that various witnesses
7 have been discussing in their testimony?

8 A. That's correct.

9 MR. CEDARBAUM: Your Honor, I would offer
10 Exhibit 27, which we thought would just be for the
11 convenience of the Commissioners and the parties to
12 have that in the record.

13 JUDGE SCHAER: Thank you. So did you offer
14 that document?

15 MR. CEDARBAUM: Yes.

16 JUDGE SCHAER: All right. Any objection?
17 It's admitted.

18 Q. Mr. Gaines, at the time that the merger
19 proceeding was pending before the Commission, what
20 was your position with Puget Sound Power and Light
21 Company?

22 A. My position was manager of power supply.

23 Q. Did you submit testimony in the merger
24 proceeding?

25 A. No, I did not.

00126

1 Q. Did you participate in the negotiations
2 between Staff, Public Counsel and the Companies,
3 which resulted in the stipulation?

4 A. No, I did not.

5 Q. At page six of your rebuttal testimony,
6 Exhibit T-24, starting at line 14, you discuss the
7 public interest standard, and you refer to the
8 Commission's order and the four factors that the
9 Commission set out in the merger order that's now
10 Exhibit 27. Is it your testimony in the current case
11 that the Commission, in the merger proceeding,
12 established the standard that would be applied for
13 the sale of a facility like Colstrip?

14 A. It's my position that in the merger order,
15 the Commission went to some length to lay out what it
16 felt were the factors that should be considered in
17 applying a standard about meeting the public
18 interest.

19 Q. I guess my question's more detailed than
20 that. Is it your testimony in this case that the
21 merger order established the standards to judge the
22 Colstrip sale?

23 A. Well, I'm not sure that I'm qualified to
24 draw conclusions about legal standards, but
25 generally, yes.

00127

1 Q. Okay. So we're bound, in your opinion --
2 I'm not calling for a legal conclusion by you, but
3 you believe that the Commission established the
4 standard to be applied in this case when it issued
5 its merger proceeding in the 14th Supplemental Order?

6 A. I believe that the Commission, in the
7 merger order, was talking about the public interest
8 standard, and went to some length to outline what it
9 felt, at least at that time, were the factors that
10 should be considered in the application of that
11 standard.

12 Q. Do you think that there are any cases where
13 it would be appropriate to apply a net consumer
14 benefits test with respect to transfers of property?

15 A. I don't know that I have an opinion about
16 that.

17 Q. You don't know whether or not it's a good
18 idea or a bad idea or whether it would be allowed or
19 not allowed?

20 A. I'm not sure whether my view on that is
21 very relevant here, to be honest with you.

22 Q. You have provided rebuttal testimony and
23 direct testimony about a standard to be applied in
24 this case, and you've testified that you believe
25 you've met that standard, so you appear to have some

00128

1 ability to testify as to standards. I'm asking you,
2 do you think that there are cases in which a consumer
3 benefits test can be applied?

4 MR. HARRIS: Objection. The question's
5 been asked and answered.

6 JUDGE SCHAER: Overruled.

7 MR. CEDARBAUM: Thank you.

8 Q. You can answer.

9 A. I don't have an opinion about that.

10 Q. The application that was filed by the
11 Company in this proceeding is not actually an exhibit
12 in the case, but would you accept, subject to your
13 check, that at page two of the application it states,
14 The sale of Colstrip is characterized as an
15 above-market resource that raises potential stranded
16 cost issues?

17 A. I'll accept that, subject to check, yes.

18 Q. Thank you. Oh, I'm sorry. I do have one
19 last question. In Mr. Elgin's testimony, he
20 indicated that on June 23rd, 1999, the shareholders
21 of Puget voted on the formation of a holding company?

22 A. Yes.

23 Q. Is it correct that the shareholders voted
24 to approve that recommendation?

25 A. Yes, that's correct.

00129

1 MR. CEDARBAUM: Thank you. Those are all
2 my questions.

3 JUDGE SCHAER: Okay. Mr. Van Cleve.

4 MR. VAN CLEVE: Your Honor, I have two
5 exhibits that I distributed for cross-examination,
6 and I'd like to get those marked. And the first is
7 an informal request of Commission Staff, Data Request
8 2-B, and the second one is Request 4-A.

9 JUDGE SCHAER: 2-B will be identified as
10 Exhibit 28 for identification, and 4-1 will be
11 identified as Exhibit 29 for identification. Let's
12 go off the record for one moment.

13 (Discussion off the record.)

14 JUDGE SCHAER: Let's be back on the record.
15 While we were off the record, copies were provided to
16 the Commissioners of certain proposed exhibits. Go
17 ahead, Mr. Van Cleve.

18 Q. Mr. Gaines, is Exhibit 28 a data request
19 response that PSE made in this case?

20 A. I believe it is, but only a portion of the
21 materials that were provided are attached here.

22 Q. And is Exhibit 29 also a data request
23 response that PSE made in this case?

24 A. I'll accept that it is, although I haven't
25 had a chance to review this response.

00130

1 MR. VAN CLEVE: Your Honor, I would offer
2 these two as Exhibits 28 and 29.

3 JUDGE SCHAER: Any objection?

4 MR. HARRIS: No objection, Your Honor,
5 although we will, during the break, review the entire
6 response to Exhibit 28 and see whether it's
7 appropriate to offer the entire response. If we do
8 believe it's appropriate, we'll offer it at a later
9 time.

10 JUDGE SCHAER: All right. Do that on
11 redirect. Were you able to check the other exhibit
12 you were going to check from this morning?

13 MR. HARRIS: We're fine with the other
14 exhibit from this morning.

15 JUDGE SCHAER: Thank you. Those documents
16 are admitted. Go ahead.

17 Q. Mr. Gaines, on page two of your direct
18 testimony, you state that the company is seeking two
19 orders in this case; is that correct?

20 A. That's correct.

21 Q. And can you explain how these two orders
22 are tied together? In other words, is the company
23 willing to go forward with the sale of Colstrip if
24 only one of the orders is granted?

25 A. Well, the company views these as tightly

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1 interrelated. And so we've, as you can see from page
2 two of the testimony, requested an order that allows
3 the transfer of the generation property. We've also
4 requested an accounting order that deals with the
5 gain. We view them as very tightly related.

6 Q. If the Commission approves the transfer,
7 but defers the allocation of gain issue to the next
8 rate case, would the Company go forward with the
9 sale?

10 A. I think in another data response, we've
11 made clear that the Company's board of directors has
12 reserved the right to review the outcome of this
13 regulatory proceeding and will make a determination
14 on that question based on that outcome.

15 Q. And what would you recommend to the board
16 if the Commission approves the sale, but defers the
17 gain issue?

18 A. Oh, I think, you know, any kind of a
19 regulatory outcome that's different than the one
20 that's requested here would require that the Company
21 review the particulars of the order and the other
22 circumstances surrounding the sale at the time. And
23 so I don't know that I could make a recommendation
24 without knowing those things.

25 Q. Are you aware that the board resolutions

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1 approving the sale were conditioned upon, quote,
2 acceptable regulatory treatment?

3 A. Yes, I am aware of that.

4 Q. And do you have an understanding of what
5 was meant by acceptable regulatory treatment?

6 A. I know that the application and testimony,
7 as filed, was reviewed with the board, and that was
8 determined to be acceptable by them.

9 Q. Do you know if there are any other outcomes
10 that would be acceptable, other than the one proposed
11 by the Company?

12 A. There was no discussion at any board
13 meeting that I was present in of any alternative
14 regulatory treatment.

15 Q. If you could refer to page three of your
16 direct testimony. At line 11, it states that the
17 Colstrip facilities are an above-market resource.
18 Could you explain what you mean by that?

19 A. Yes. I think it's shown by the first
20 exhibit to my direct testimony. That was the purpose
21 of those analyses.

22 Q. Is it your belief that the Colstrip
23 facility is an above-market resource on a long-term
24 basis?

25 A. Our analyses show generally that it's an

00133

1 above-market resource in the near term and in the
2 intermediate term, and that in the long-term, whether
3 it's in or out of the market is very sensitive to the
4 assumptions that are made, particularly assumptions
5 about the future market price in power.

6 Q. Doesn't the fact that you are able to sell
7 the resource at a price above book value indicate
8 that the market believes that it has value?

9 A. No, I don't think it does indicate that. I
10 don't think that the premium to book is directly
11 related to whether the resource is in or out of the
12 money. It is more a function of what the history of
13 the depreciation has been.

14 Q. But it does indicate that the asset has a
15 value in excess of its cost, doesn't it, a market
16 value in excess of its cost?

17 A. Well, I mean, I think it indicates a lot of
18 things. I think it indicates that the market for
19 something like this is not a point number; it's a
20 range, and I think it indicates that different market
21 participants probably have different perceptions of
22 the value of the project. We certainly learned that
23 through the auction process, as there was quite a
24 wide range of bid prices.

25 So there are a number of factors that come

00134

1 into the pricing of an asset like this. There are
2 strategic factors that a buyer would consider in
3 attempting to gain a strategic foothold in a new
4 marketplace. There are the various forward price
5 forecasts that bidders would have, all of them
6 different. There are a number of factors.

7 Q. Has the Company obtained replacement power
8 supplies to replace the output of Colstrip?

9 A. It has for a little more than half of the
10 output that's being sold.

11 Q. I think on page 13 of your direct
12 testimony, line 17, you refer to the Company
13 analyzing optimum power replacement products. And
14 what's the status of that analysis?

15 A. It's ongoing, and actually is always
16 ongoing, but we have undertaken some effort to look
17 at the remainder of our supply portfolio and also our
18 load requirements and the pricing characteristics.
19 These analyses are intended to determine what the
20 optimum replacement power products would be.

21 Q. But you haven't signed any contracts
22 related to those replacement products?

23 A. We've signed one contract with PP&L Global.

24 Q. Is it your position that the sale of the
25 Colstrip assets is implementing the power stretch

00135

1 goals in the merger rate plan?

2 A. We believe that the sale of the Colstrip
3 project is consistent with the challenge that the
4 Company was presented with in the merger rate order
5 to find savings broadly. And whether it fits in any
6 particular bucket that was identified in the merger
7 order is, in my mind, not terribly relevant.

8 Q. Well, Mr. Story testified this morning that
9 there were three categories identified in the rate
10 plan, merger synergies, best practices, and power
11 stretch?

12 A. Uh-huh.

13 Q. And do you believe that the sale of the
14 Colstrip assets fits into one of those categories?

15 A. I think that if it's necessary for you to
16 categorize it, it probably makes no sense to put it
17 in the power cost bucket. But again, I'm not sure I
18 accept the premise.

19 Q. Do you have an understanding of what the
20 terms power stretch goals mean?

21 A. Generally, yes.

22 Q. Why don't you explain your understanding?

23 A. It was an amount of dollar savings
24 expressed annually that the Company was expected to
25 achieve during the merger rate plan period.

00136

1 Q. I think you refer in your rebuttal
2 testimony, at page three, lines five to seven, to
3 cost-cutting efforts. Is the cost-cutting effort the
4 same thing as a power stretch savings?

5 A. I'm sorry, I'm not sure I've found the
6 right line.

7 Q. Lines five to seven.

8 A. And the question is whether the Colstrip
9 transaction is a cost-cutting effort?

10 Q. No, it's whether a cost-cutting effort is
11 the same thing as a power stretch savings?

12 A. I would say that a power cost savings is a
13 subset of a cost-cutting effort.

14 Q. Do you anticipate selling any other
15 generating assets during the term of the rate plan?

16 A. Yes, at least one. Our interest in the
17 Centralia project.

18 Q. And have you determined what type of
19 accounting treatment you'll ask for with respect to
20 that transaction?

21 A. No, we have not.

22 Q. Do you believe that it would be appropriate
23 to apply the same five-year amortization if there is
24 a gain?

25 A. No, as Mr. Story -- not necessarily. As

00137

1 Mr. Story explained this morning, we would examine
2 the nature of that transaction and the economic
3 environment that the Company finds itself in at the
4 time as we're determining what amortization period to
5 propose.

6 Q. I'd like to refer you to Exhibit 29, which
7 is the Data Request Response 4-A. If you could turn
8 to page 44 of that document, is it your understanding
9 that this is hearing testimony from the merger
10 proceeding?

11 A. I have not had an opportunity to review
12 this document.

13 Q. Do you know who Mr. Torgerson is?

14 A. I do.

15 Q. And what was his role at the time of the
16 merger?

17 A. He was the chief financial officer of
18 Washington Natural Gas.

19 Q. In the middle of the page on 47, about nine
20 lines up, I'll just quote a sentence out of Mr.
21 Torgerson's testimony. He says, We need to
22 communicate to individual analysts some of our
23 strategies and some of our goals, but not specific,
24 like best practices or power stretch goals, which
25 rely on, you know, litigation in the future and

00138

1 renegotiating power contracts.

2 Is it true, Mr. Gaines, that the primary
3 power stretch goals envisioned in the merger rate
4 plan were reducing the costs of power contracts?

5 A. I don't know that. I know that out of the
6 merger proceeding resulted some annual dollar savings
7 goals.

8 Q. Do you know what those goals were based on?

9 A. I understand, through conversations, that
10 they were based on savings related to PURPA and NUG
11 contracts.

12 Q. Were you involved in any of the
13 presentations to rating agencies regarding the power
14 stretch goals or other cost saving measures?

15 A. No, I was not.

16 Q. Have you seen any testimony from the merger
17 proceeding that suggests that generating asset sales
18 were included in power stretch goals?

19 A. I haven't seen any testimony from the
20 merger proceeding that suggests that there was any
21 particular limitation on what would be included in
22 the power stretch goals or any of the other cost
23 saving objectives that are laid out in the order. In
24 fact, just the opposite. I think if you look at page
25 26 of the merger order, the Commission was fairly

00139

1 explicit in its expectation that the Company would
2 find savings wherever possible.

3 Q. I'd like to refer you to page 27 of your
4 direct testimony. In lines 18 through 20, you state
5 that 50 percent of the gain will be amortized after
6 the end of the rate stability period. Do you mean
7 that 50 percent in nominal terms?

8 A. I think it's meant to be an approximation.

9 Q. Do you believe that, on a net present value
10 basis, that 50 percent of the gain will be amortized
11 at the end of the rate stability period?

12 A. I haven't done that math.

13 Q. And can you tell me what you think the
14 effect of amortizing the gain after the rate
15 stability period is?

16 A. Yes, I think the effect of it is, in many
17 ways, the same as the effect during the rate period.
18 The customers are receiving savings as a result of
19 the merger rate order. The Company needs to fund
20 those savings in some way. This Colstrip transaction
21 is one mechanism for doing this. To the extent that
22 the amortization continues to run beyond the
23 termination of the rate plan period, the customers
24 presumably would continue to enjoy benefits, whether
25 or not a rate case is filed at that time.

00140

1 Q. And what benefits would they continue to
2 receive?

3 A. The benefits of low rates.

4 Q. But --

5 A. The absence of increase of rates.

6 Q. But they wouldn't see any benefit if a rate
7 case wasn't filed from sale of the asset?

8 A. No, I'm not sure that that's correct. I
9 think that the amortization of the gain post the rate
10 plan period would serve to offset increases in other
11 of the Company's costs, and thereby could lead to a
12 reduction or elimination of what might otherwise be a
13 rate increase.

14 Q. If you could look at page nine of your
15 rebuttal testimony, in lines six to seven, you state
16 that the application does not raise stranded cost
17 issues, nor does it seek an order addressing stranded
18 cost issues; is that correct?

19 A. That's correct.

20 Q. Is it your position that a sale of a major
21 generating asset does not impact future stranded cost
22 recovery?

23 A. The issue of stranded costs arises in the
24 context of a move to retail access for commodity
25 supply. And it is in that context that costs may

00141

1 become stranded, and that is not what this proceeding
2 is about.

3 Q. Does the sale of the Colstrip facilities
4 have any relationship to stranded costs?

5 A. Not in and of itself.

6 Q. If you could look at Exhibit 28, were you
7 present at the presentations by Morgan Stanley?

8 A. For some of them, yes.

9 Q. Were you present at the one on March 24th,
10 1998?

11 A. I don't recall the particular meetings that
12 I was involved in.

13 Q. And what was Morgan Stanley's role in this
14 transaction?

15 A. Morgan Stanley acted as an adviser to the
16 Company, and essentially to its board and senior
17 management, on the appropriateness of the auction
18 process and on the fairness of the valuations that
19 came out of the auction process.

20 Q. If you could look at the document in
21 Exhibit 28, the last page that has the number PSEC
22 00029 at the bottom. And do you know what the
23 purpose of this document was?

24 A. Yes, generally.

25 Q. And what was that?

00142

1 A. Generally, Morgan Stanley was reviewing for
2 the Company's board of directors some strategic
3 alternatives having to do with the evolution of a
4 competitive generation market in the country, and the
5 question of being a player, if you will, in the
6 unregulated generation market versus not doing that.

7 Q. On the page I referred you to, the last
8 page of Exhibit 28, the right-hand column is entitled
9 Value of Generation Disposition, and the second point
10 that's noted is crystallize stranded cost exposures.
11 Is that one reason that a company would dispose of
12 its generation assets?

13 A. It might be one reason, but it would be
14 done in the context, as I mentioned before, of a move
15 towards open access, retail access to commodity
16 supply. Much of the rest of the Morgan Stanley
17 presentation, if you look at it, is based on
18 precedent generation, sale transactions elsewhere in
19 the country that are done in connection with a move
20 to open retail access.

21 Q. Do you understand how the sale of a
22 generating asset would crystallize stranded cost
23 exposure?

24 A. I can understand that in the context of a
25 move to retail access, yes.

00143

1 Q. But you can't understand it in a context of
2 the Company's sale of Colstrip?

3 A. No.

4 MR. VAN CLEVE: That's all the questions I
5 have.

6 JUDGE SCHAER: Mr. Manifold.

7 MR. MANIFOLD: Yes.

8 C R O S S - E X A M I N A T I O N

9 BY MR. MANIFOLD:

10 Q. Good afternoon, Mr. Gaines. Please keep
11 that one right in front of you. This presentation by
12 Morgan Stanley in March of 1998, do you know when
13 Morgan Stanley was retained by the company?

14 A. I don't remember exactly when it was.

15 Q. Was Morgan Stanley retained for the purpose
16 of this -- what has turned out to be Colstrip
17 transaction that is in front of us?

18 A. Yes. It was only shortly before this
19 presentation was made.

20 Q. Okay. So this was not a generic
21 presentation on the advantages of being in the
22 generation business or not?

23 A. No, to put this in context a little bit,
24 Montana had announced their sale of their generation
25 assets in December of '97. And shortly after that,

00144

1 the other participants, including PSE, were offered
2 an opportunity to participate in the sale
3 transaction. And when Puget made a determination
4 that it would at least consider participating in the
5 sale, Morgan Stanley were retained at that time to
6 advise the Company on that particular activity.

7 Q. Reading your direct testimony on the events
8 leading up to the proposed sale, am I correct that
9 Puget initially decided not to include its share in
10 the auction process that Montana Power was beginning,
11 but only did so only after Water Power withdrew its
12 share?

13 A. I'm not sure that we made a definitive
14 decision not to participate. We were involved in
15 some litigation and negotiation with Montana Power at
16 the time, which may have made difficult participation
17 by Puget, probably better to say that it would be
18 cleaner for those negotiation and litigation items to
19 get cleaned up before there was a participation by
20 Puget. So largely, that was, I think, the reason for
21 the lag in Puget's decision to participate in the
22 sale.

23 Q. Well, let me phrase the question this way.
24 When the first solicitation went out by Montana Power
25 and Water Power and Pacific Power and Light -- excuse

00145

1 me, Portland General Electric participated in that
2 with their shares, was Puget a participant with its
3 share?

4 A. No, it was not. It was offered an
5 opportunity to participate, but it did not at that
6 time.

7 Q. Okay. And after Water Power withdrew its
8 share subsequently, that's when Puget put its share
9 into the mix?

10 A. That's correct.

11 MR. MANIFOLD: Your Honor, I've distributed
12 two documents, one is on white paper, is one page,
13 and the top right-hand portion says Appendix H,
14 Detailed Scenario Planning Description.

15 JUDGE SCHAER: We'll mark that for
16 identification as Exhibit 30.

17 Q. Okay. Mr. Gaines, do you recognize this to
18 be a page as indicated from Puget's most recent
19 integrated resource plan filed with this Commission?

20 A. It's been a while since I looked at it, but
21 I'll accept that it is.

22 MR. MANIFOLD: Okay. Your Honor, I'd move
23 for the admission of Exhibit 30.

24 JUDGE SCHAER: Any objection? The
25 document's admitted.

00146

1 Q. Mr. Gaines, do you have before you a
2 five-page document on -- I don't know what color this
3 is -- on bright pink paper that is headed -- that
4 appears to be the Company's response to Public
5 Counsel Data Request Number 64, and that is marked
6 confidential?

7 A. Yes.

8 MR. MANIFOLD: Your Honor, I'd like to move
9 to have this marked as an exhibit.

10 JUDGE SCHAER: We'll mark this for
11 identification as Exhibit C-31.

12 Q. Mr. Gaines, do you recognize this to be the
13 Company's response, as indicated?

14 A. I recognize the first page of this
15 response, and I'm not sure that I reviewed the other
16 pages, but it does appear to be what it purports to
17 be.

18 MR. MANIFOLD: Okay. Your Honor, I'd move
19 for the admission of Exhibit C-31.

20 JUDGE SCHAER: Any objection? The document
21 is admitted.

22 Q. Mr. Gaines, do you have Exhibit 15, which
23 was the cross-examination document?

24 A. No, I'm sorry, I don't.

25 Q. This is the packet we put in through Mr.

00147

1 Story.

2 A. Yes, thank you.

3 JUDGE SCHAER: Let the record show that a
4 copy has been provided to the witness.

5 Q. Can you find the page in there that's the
6 Company's response to the PC-55? That's pages nine
7 and 10.

8 A. Yes.

9 Q. This data request asked for the Company to
10 update your Exhibit 7 in light of the Montana
11 property tax change; is that correct?

12 A. Yes.

13 Q. And are pages nine and 10 the complete
14 answer from the Company?

15 A. I am not sure of how much of the detail we
16 may have provided along with this.

17 Q. Will you accept, subject to your check,
18 that this is the complete response by the Company?

19 A. Sure.

20 Q. You have with you, I presume, your Exhibit
21 7, which this asked for an update of?

22 A. Yes.

23 Q. It's a, what, 20, 30-page document?

24 A. Uh-huh.

25 Q. What is provided here with PC-57, as

00148

1 updated by the Company, is just the cover page from
2 your Exhibit 7; is that correct?

3 A. That's correct.

4 Q. Is it correct that the subsequent pages of
5 your Exhibit 7 would also change because they are the
6 detail that's behind this cover page with the new
7 Montana tax?

8 A. Yes, I believe some of them would, yes.

9 Q. And the Company has not provided those to
10 the record, that you're aware of?

11 A. Not that I'm aware of.

12 Q. And am I correct in reading this that with
13 the change in the Montana property tax, the net value
14 that is both, as we would say, to shareholders and
15 ratepayers, and as the Company would say, to
16 everybody or something, it goes from 23.8 million to
17 6.5 million?

18 A. Yes, that appears to be the change for that
19 one particular case in the 20-year MPV column.

20 Q. And is that the base scenario in your
21 presentation?

22 A. We have titled that the base scenario, yes,
23 a little unfortunately, I think.

24 Q. Mr. Story was kind enough to refer a
25 question to you regarding the sale date. In your

00149

1 direct testimony at page 14, you indicated that you
2 needed a Commission order in this case before August
3 1st. Would you care to update us on what the
4 Company's current needs would be in order to stay on
5 the timetable it's currently on in terms of getting
6 an order from the Commission?

7 A. I can talk a little bit about that. We
8 have for some time been targeting a close date for
9 the transaction of September the 1st, and one of the
10 requirements to closing is a 30-day lead in order to
11 enable the purchaser to arrange his financing, final
12 arrangement of his financing.

13 My understanding is that the target close
14 date is now sliding off September 1st. Someone
15 suggested this morning it might be sliding as far as
16 October the 1st. But all those precedential
17 requirements would be the same. There would be a
18 30-day lead for arrangement of financing. There
19 would also need to be some lead time for
20 consideration of the regulatory order by the Puget
21 board.

22 Q. So are you able to indicate today -- well,
23 are you aware that the briefing schedule in this case
24 calls for briefs to be submitted July 31st?

25 A. I am now.

00150

1 Q. Okay. And you would accept that from July
2 31st to August 1st isn't a lot of time to prepare an
3 order?

4 A. I certainly would accept that, yes.

5 Q. We may have very good ALJs, but, you know,
6 that's a lot. Well, can you provide any further
7 elucidation for the Commission on what kind of
8 timetable the Company would like -- I feel like I'm
9 doing all this friendly cross for your Counsel here
10 -- but what the Company would like, in light of
11 current expectations of closing, if this transaction
12 is to go forward?

13 A. We haven't had a lot of discussion about it
14 internally at the company, but if you consider a
15 30-day lead on the financing, two weeks or so for
16 board consideration, I suppose if we had something in
17 August, it would be fine.

18 Q. At page six of your direct testimony, you
19 assert that there is plenty of capacity in the
20 Western region on the subject of will the Company be
21 disadvantaged in terms of having electricity,
22 electrons, if it sells Colstrip? Do you recall that?

23 A. Yes, I do.

24 Q. Would you agree that the Western System
25 Coordinating Council report that you're relying upon

00151

1 measures capacity, not energy?

2 A. Oh, I think that it probably measures both,
3 although I think what is represented in the testimony
4 here is only capacity.

5 Q. Okay, fine. And the megawatts that you're
6 referring to on page six, lines 15 and 16, are
7 capacity, not energy?

8 A. That's correct.

9 Q. Would you agree that Colstrip is a baseload
10 plant, is used as a baseload plant?

11 A. Generally, yes.

12 Q. Would you either agree or accept, subject
13 to check, that, as the Company indicated on its
14 response to Public Counsel Data Request 12, its own
15 hydro has 1,581 megawatts capacity, but only 668
16 megawatts of energy, or about 42 percent of its peak
17 rate?

18 A. Numbers were 1,386 and 572?

19 Q. 1,581 and 668.

20 A. Yes, I see those numbers in the response to
21 PC-12.

22 Q. And so you accept that?

23 A. Yes.

24 Q. And so you would accept the proposition
25 that one needs to look at both capacity and energy

00152

1 availability, not just capacity?

2 A. Oh, certainly, yes.

3 Q. Okay. I guess I'm tempted to ask why, in
4 your testimony, for a baseload plant, you provide
5 information on capacity when a baseload plant
6 normally is used to provide energy?

7 A. Oh, it was only meant to be illustrative
8 and probably is not complete. Obviously, in our
9 ongoing power planning efforts, we would look at
10 energy and capacity both, probably even harder at
11 energy, given the nature of the system here in the
12 Northwest and the fact that it is generally
13 energy-constrained.

14 Q. And would you accept that the same document
15 I was just referring to, Public Counsel Data Request
16 12, the Company's response thereto, page two shows
17 that Puget's forecast is that without the Colstrip
18 facility, but with Centralia, since that's not in
19 front of us here today, the Company faces an energy
20 deficit of 887 average megawatts by the year 2003/4,
21 and a 1,533 megawatt capacity deficit?

22 A. Well, that's what the response to this
23 exhibit shows. I think it's helpful to understand
24 some of the assumptions that underlie this. One is
25 that the hydro that's shown in tables like this are

00153

1 based on worst case assumptions. So in a more normal
2 hydro year, you'd have significant amount of
3 additional energy as the difference between normal
4 speed flow and critical.

5 I think another assumption that underlies
6 this is that it's status quo with no assumptions made
7 about additional resources or power purchases or
8 changes in load, for that matter, other than what you
9 see on line 36, which is the purchase contract from
10 Global.

11 Q. In the Company's integrated resource plans,
12 does it normally present its resources on a worst
13 case scenario for stream flow?

14 A. I haven't looked at IRPs in quite some
15 time, but I would expect we'd probably present it
16 both ways, or more likely explain the whole range of
17 possibility of hydro flow in the region.

18 Q. All right. You mentioned it assumed status
19 quo in terms of new resources, and you testified a
20 moment ago to Counsel for ICNU that you -- the
21 Company had obtained replacement power, as I
22 understood you, for about half, a little over half of
23 the power that Colstrip represents?

24 A. That's right.

25 Q. How long does the Company anticipate having

00154

1 Colstrip if it doesn't sell it?

2 A. We haven't made any assumptions of that
3 sort.

4 Q. Well, in your studies, don't you look at
5 ownership of Colstrip for 10 or 20 years?

6 A. We chose that as a period of analysis, but
7 it was not meant to indicate any expectations about
8 how long the plant would last or how long the company
9 might hold it.

10 Q. You tempt me with that, but I'll go on.
11 The replacement power contract that you have is for
12 how long?

13 A. For two years.

14 Q. Okay. So when you responded that the
15 Company had replacement power for about half the
16 power, you were talking about half the power for two
17 years, as compared to all of the power for the life
18 of the project, 10, 20, whatever that period of time
19 is?

20 A. Yeah, that's correct. And we really view
21 the Global purchase contract as an interim or
22 bridging arrangement until we put some longer term
23 arrangements in place.

24 Q. Does the timing -- does the length of time
25 of the Global contract have anything to do with the

00155

1 rate plan period, which it more or less corresponds
2 to?

3 A. Well, it happens to fall into the rate plan
4 period.

5 Q. Well, did your selection of a two-year
6 bridging contract with Global, was that influenced by
7 the fact that the rate plan lasts for about two more
8 years?

9 A. Oh, we didn't actually select the term of
10 the replacement power contract. That was worked out
11 by Montana Power and the other participants in the
12 sale earlier in the process, and so as somewhat a
13 latecomer to the process, Puget just adopted the
14 terms that the other parties already had worked out
15 for this replacement purchase contract.

16 Q. Okay. New subject. You're familiar, at
17 least generally, with the Commission's least-cost
18 planning process and rule?

19 A. Generally, yes.

20 Q. Okay. And just for reference purposes,
21 it's WAC 480-100-251. Is it correct that the last
22 time Puget submitted a least-cost plan to the
23 Commission was in 1993?

24 A. I don't recall the date. I'll accept that,
25 subject to check.

00156

1 Q. Okay. And do you recall how often the rule
2 requires the Company to submit a least-cost plan?

3 A. I believe it's every two years.

4 Q. Do you know if, in its 1993 least-cost
5 plan, Puget anticipated or analyzed the potential
6 sale of Colstrip?

7 A. I don't think that it did.

8 Q. In your testimony, you refer to meetings of
9 the technical advisory committee. Just to clarify,
10 the Company has, from time to time, convened a group
11 of non-company people to assist it in its planning of
12 filing an integrated resource plan, and the name of
13 that has been the Technical Advisory Group, or TAG?

14 A. Yes, that's right.

15 Q. And do you recall when the most recent TAG,
16 that's all caps, T-A-G, was convened or met?

17 A. No, I don't.

18 Q. Would you accept, subject to your check,
19 that that was in the time period of 1997? Excuse me.
20 If you would look, please, at Exhibit 15, pages 15
21 and 16, your response to that data request indicates
22 some discussions that either you had or were aware of
23 that Puget had with the Integrated Resource Plan TAG
24 in December of '98?

25 A. Yes.

00157

1 Q. Yeah. So it was around at least then?

2 A. Uh-huh.

3 Q. Okay. Is it accurate that the TAG was --
4 Puget was meeting with the TAG after the date that
5 Puget announced its proposed sale of Colstrip?

6 A. I would assume, based on this data response
7 we just looked at, that it is. I think most of the
8 discussion that was being had with the TAG at that
9 time had to do with conservation plans.

10 Q. Did Puget discuss the proposed Colstrip
11 sale with the TAG at all?

12 A. I don't know.

13 Q. Would you accept, subject to your check,
14 that it did not discuss the proposed sale of Colstrip
15 with TAG, even after the sale was announced to the
16 public?

17 A. Yes.

18 Q. Has the Company submitted any integrated
19 resource plan-like analysis in this record to
20 demonstrate to the Commission that the sale of
21 Colstrip and its proposed move towards more
22 market-based obtaining of power will result in a
23 least-cost plan for the Company and its customers?

24 A. Well, it certainly has tried to do that
25 through the analyses that are attached to my direct

00158

1 testimony, and also through the discounted cash flow
2 and other analyses that were performed by Morgan
3 Stanley.

4 Q. The least-cost planning rule, I'll read you
5 a portion of it, in subsection two says, Definitions,
6 quote, Least-cost plan, close quote, or plan, close
7 quote, means a plan describing the mix of generating
8 resources and improvements in the efficient use of
9 electricity that will meet current and future needs
10 at the lowest cost to the utility and its ratepayers.
11 And then in subsection three, there's a lot more
12 detail about what might go into it. Do you have
13 before you Exhibit 30?

14 A. Yes.

15 Q. And we already established that this was a
16 page from the Company's last IRP. Is there anything
17 in what you've submitted to the Commission that is
18 like this?

19 A. I haven't had a chance to read this page in
20 detail, but the title of it is Scenario Analysis,
21 which is exactly the nature of the analyses that are
22 attached to my direct testimony.

23 Q. Where in your direct testimony is there an
24 explanation or analysis of the various types of
25 resources that the Company would acquire or have

00159

1 under various load forecast scenarios?

2 A. There's some discussion of that in the
3 direct testimony. We talk a little bit about market
4 purchases, we talk a little bit about distributed
5 generation, we talk a little bit about changes in
6 load going forward, which would necessitate
7 reductions in supply portfolio, we attempt to address
8 it in the testimony itself.

9 Q. So that would be the only place that you
10 would cite me to?

11 A. Yes.

12 Q. Okay. Referring, again, to Exhibit 30 --
13 strike that. I'm sorry. Am I correct, Mr. Gaines,
14 in looking at Exhibit 30, that market resources, as
15 the Company's now talking about it, was not a concept
16 or plan that was part of the Company's planning
17 process at the time that this integrated resource
18 plan was done in '92, '93?

19 A. I don't know that it was or it wasn't. You
20 know, as I recall that integrated resource plan, we
21 were talking a lot about alternate forms of new
22 long-term supply resources, but as I'm sure you know,
23 the Company has been active in the wholesale market
24 forever in order to balance its short-term surpluses
25 and deficiencies.

00160

1 And of course, the power market has evolved
2 a lot since 1993. It's much more robust, much
3 deeper, better price transparency, and the range of
4 products that are available are much broader. And so
5 a look to the market today for replacement products
6 would, I think, yield a much more robust set of
7 alternatives than you might have obtained back in
8 '93.

9 Q. I think we're in agreement on that. The
10 question is where has the Company done any analysis
11 to show that its current plans would meet the
12 integrated resource planning requirement? And I
13 understand your answer to be that it is mentioned a
14 little bit in your direct testimony, in the places
15 you've just indicated?

16 A. Yeah, I mean, in my mind, the exhibits to
17 that direct testimony are very similar to the sorts
18 of analyses that would be done in a revised and
19 updated least-cost plan.

20 Q. Looking at Exhibit 30, is there someplace
21 in your exhibits that quantifies the future resource
22 additions that would be needed, as is done in this
23 chart -- excuse me, table, under various resource
24 assumptions for the future?

25 A. No, we tried to --

00161

1 Q. No was the beginning?

2 A. No, we tried to -- we did not try to lay
3 out in our presentation, in connection with this sale
4 transaction, all of the things that we might do in
5 terms of future resource additions. Instead, we
6 tried to talk about some of the changes that are
7 happening in the power market and in the industry
8 more broadly. We've got a much more robust power
9 market, much deeper. We have the prospect of
10 transition to retail access for at least some loads
11 at least sometime in the future, which creates a lot
12 of uncertainty in the planning process.

13 And the IRP rule and process, as you know,
14 was built around the old model of the vertically
15 integrated utility supplying all of its needs through
16 long-term supply arrangements, as opposed to the
17 flexibility that we think is going to be needed in
18 order to deal with changes in load and market
19 conditions going forward.

20 So a big part of our direct testimony is
21 given over to a discussion about flexibility and some
22 of the benefits that the Colstrip sale provides in
23 that vein.

24 Q. Referring back to Exhibit 28, the last
25 page, which is the summary table from the Morgan

00162

1 Stanley presentation, I was struck by the fact that
2 Morgan Stanley, like Puget, felt that maintaining
3 flexibility was an important goal. It appears to me,
4 from this document, Morgan Stanley put retain
5 flexibility in the value of retaining generation.
6 And at this point, the Company's testimony is that
7 flexibility is maintained by disposing of generation;
8 is that -- am I correct in drawing that distinction?

9 A. I suppose that you could probably put it on
10 both sides of this table, if you like, but from our
11 perspective as a buyer and a supplier of energy
12 retail loads, yes, we believe we'll have a lot more
13 flexibility to source our supply after this
14 transaction is closed.

15 Q. Would you accept -- new subject. You've
16 testified some about what might have happened in
17 terms of company rate applications absent the merger
18 rate predictability plan. Would you accept, subject
19 to your check, that the annual rate increases
20 embedded in the rate predictability plan amount to
21 about a \$60 million annual increase by the time of
22 year five?

23 A. I'll accept that, subject to check.

24 Q. And if you want to consult with our
25 consultant on how he derived that, please -- you know

00163

1 how to do that.

2 Okay. Referring to Exhibit C-31, and
3 nearing the completion here, page four, and we're in
4 a confidential document now. Line 13 shows net
5 savings forecast by the Company for each year, 1998
6 through 2011, because it continues to the next page.
7 Can you verify that the Company has achieved a
8 significant amount of the net savings that it
9 anticipated in that forecast?

10 A. The Company has achieved at least some of
11 these savings that it laid out. I recall in the
12 Tenaska transaction that the amount of savings -- the
13 Company's at risk for the amount of savings, based on
14 the volatility of the gas market price.

15 MR. MANIFOLD: Thank you. No other
16 questions.

17 JUDGE SCHAEER: Commissioners, do you have
18 any questions of Mr. Gaines?

19 COMMISSIONER GILLIS: No.

20 E X A M I N A T I O N

21 BY COMMISSIONER HEMSTAD:

22 Q. I'm interested in the stranded cost,
23 stranded benefits question as it relates here. This
24 particular transaction, you will be selling, if
25 approved, this asset above cost?

00164

1 A. Above book, yes.

2 Q. Above book. So I suppose that could be
3 described as a stranded benefit in the jargon of how
4 those terms are used currently?

5 A. I suppose that it could be.

6 Q. How will the Company address the issue of
7 stranded cost if you next sell an asset globally?

8 A. Well, as I indicated earlier, we haven't
9 made any determinations yet about what we might
10 propose in connection with another asset sale. I
11 think the thing that's caused this issue to be
12 confused -- there are two things, in my mind. One is
13 whether or not, you know, there are stranded costs,
14 you know, in connection with this transaction. And
15 we believe that there are not, because stranded costs
16 really only arise when the Company, you know, is
17 required to take its customers to market and has
18 costs that it can't recover through market prices.

19 The other thing that I think that
20 complicates this a little is the existence of the
21 merger rate plan and this falling in and out of the
22 rate plan period. And as Mr. Story indicated
23 earlier, I believe that the Company would propose the
24 same amortization treatment on the gain associated
25 with this sale, whether or not that merger rate plan

00165

1 period were in effect. I hope that's responsive.

2 Q. Well, I'm trying to deal with the question
3 of isolated transactions over time. Will there be
4 gains or losses?

5 A. Oh, I see. This transaction and the
6 Centralia transaction that I mentioned really have
7 been opportunistic for the Company. They are not
8 part of any present broad plan to do divestiture of
9 supply resources. The Colstrip opportunity arose
10 because Montana Power elected to divest and we were
11 presented an opportunity. The Centralia opportunity
12 arose because of the decision of the plant sponsor to
13 try and market the plant and escape some of what
14 otherwise might be large environmental costs.

15 So in each of these cases, they were
16 opportunistic, and I don't think that the Commission
17 should expect that there will be a series of these
18 one-by-one divestitures brought.

19 Q. Well, assume at this point a hypothetical,
20 that Puget has in mind becoming a distribution-only
21 company and wants to get out of the generation or the
22 long-term power contract purchase arrangements, and
23 it sells those interests off at a loss five years
24 hence. How will the Company treat that in those
25 isolated transactions?

00166

1 Another way of putting it, if such a
2 company were to sell its entire portfolio, then this
3 Commission would tend to look at the issue -- well,
4 at least arguably would look at it on a wholistic
5 basis as a complete portfolio for gains and losses.
6 But how are we going to deal with it now in these
7 isolated transactions?

8 A. Well, again, the Company doesn't have, at
9 present, any plan to do a broad divestiture of its
10 resources. It's just that these opportunities have
11 presented themselves, they seem to have economic
12 benefits for the customers and for the Company, they
13 seem to remove risks for the customers going forward,
14 and that's why we're advocating them. They should
15 not necessarily be taken as the beginning of a
16 step-wise divestiture.

17 Q. Okay. I believe you responded to a
18 question that raised the issue of the relationship
19 between Colstrip and Centralia, here a five-year
20 period for amortization, but that may not be the
21 standard for Centralia, may not be?

22 A. Well, it may or may not be what we propose.
23 We haven't determined what we might propose yet.

24 Q. Well, I'm curious. Two transactions
25 relatively close in time?

00167

1 A. Yes.

2 Q. Quite similar in terms of your interests, I
3 suppose. Isn't there a reasonably objective standard
4 by which that is measured?

5 A. I'm not suggesting that five years wouldn't
6 be the period we propose; it's just that we have not
7 made a determination.

8 Q. But it might be three or it might be ten?

9 A. We just haven't -- we haven't made that
10 determination.

11 Q. But why would there be a significantly
12 different analysis there than here?

13 A. I don't mean to suggest that there could be
14 or should be.

15 Q. I'm only trying to get a handle on what
16 kind of reasonably objective standards the Commission
17 should apply in evaluating the decisions that the
18 Company makes and is recommending.

19 A. Well, as Mr. Story indicated earlier, you
20 know, we gave some consideration to the rate plan
21 period, we gave some consideration to the impact of
22 the annual amortization amounts on the Company's
23 financials, and those were probably the primary
24 considerations that were made, and would use those
25 same considerations next time around.

00168

1 COMMISSIONER HEMSTAD: I think that's all I
2 have.

3 E X A M I N A T I O N

4 BY CHAIRWOMAN SHOWALTER:

5 Q. I'm interested in a scenario analysis. Do
6 I take it that the value of doing different scenarios
7 is that there are multiple factors that could vary
8 over time, so you combine different factors in
9 different ways to get different scenarios?

10 A. Yes.

11 Q. Each of which may come to pass or each
12 scenario may not, but that you look at your proposed
13 transaction in light of those different scenarios?

14 A. Yes, exactly.

15 Q. So the first question is -- let's say you
16 generate seven scenarios. What do you do then? You
17 have several different scenarios and maybe the
18 transaction is a good idea in one scenario and a bad
19 idea in three of them, et cetera. At that point, do
20 you simply eyeball them all and do a qualitative
21 judgment about the transaction, or do you try to
22 reduce the seven down to the best one or convert it
23 to dollars or somehow arrive at some commonality
24 whereby you can get a grand judgment of yes or no on
25 your transaction?

00169

1 A. Well, I think it's probably a combination
2 of all those things. Probably the best way for me to
3 explain the way that we approached it is the very
4 first page of the analytical exhibit to my testimony,
5 where we tried to pull a summary of the results of
6 all of these quantitative analyses together in one
7 place. And if you look at that collection of
8 scenarios, certainly in the near term, there are
9 benefits in all the scenarios. In the intermediate
10 term, there are benefits in pretty much all the
11 scenarios, and in the long-term, it becomes less
12 certain.

13 In our evaluation, we've given less weight
14 to the long term because of the inherent uncertainty
15 of forecasts. So that's how we approach the
16 quantitative portion of the decision.

17 We overlaid that with some qualitative
18 considerations, which I've discussed in the testimony
19 and a little bit today. We've talked a little bit
20 about the benefits of having a flexible supply
21 portfolio as we go into a period of general
22 restructuring in the industry and changes in the
23 wholesale market. I think we've talked a little bit
24 about the benefit of removing some of the
25 environmental risks that might otherwise fall on

00170

1 customers through the ownership of a coal plant as
2 carbon taxes and mercury taxes and sulfur emissions
3 requirements increase over time.

4 And then the other thing that has been a
5 strong consideration in our evaluation is the
6 uniqueness of the opportunity that's presented here.
7 By participating with Montana in a large sale of
8 assets in that area and by selling the controlling
9 interest in the Colstrip plant, we believe that we've
10 received a premium price for the project, which
11 probably could not be replicated in the future.

12 So it's really the combination of those
13 quantitative factors, qualitative factors, overlaid
14 by the uniqueness of the sale price that has led us
15 to this conclusion and this recommendation.

16 Q. Okay. And then regarding the factors, all
17 of which I guess are uncertain -- taxes, price of
18 gas, load growth, load decrease -- the prospect of
19 restructuring is one of those uncertainties that you
20 are taking into account?

21 A. Yes.

22 Q. And we don't know whether it will transpire
23 or not, but it may, and it's a more uncertain time
24 than it has been in the past?

25 A. Yes, that's right. And that's very much

00171

1 the way we've looked at it.

2 Q. But if restructuring should come to pass,
3 then isn't stranded cost a part of that scenario, and
4 if so, isn't it appropriate to look at this
5 transaction in light of potential stranded costs
6 because of the various potential scenarios where that
7 would transpire?

8 A. Well, I don't know. I suppose it depends,
9 to some extent, the probability that you would assign
10 to some restructuring in the future. It probably
11 depends on when in the future we think that that
12 might happen. It probably depends a little bit on
13 the need of the Company to make this decision now.
14 The Company is faced with an opportunity and a
15 requirement to make this decision in the face of some
16 uncertainty, and in some ways, the Commission is
17 presented with that same situation.

18 Q. So that if the prospect were either slim or
19 distant --

20 A. Then I suppose it would --

21 Q. -- then stranded cost would become less of
22 an issue?

23 A. Yeah, I would think it would receive less
24 weight in the determination, yes.

25 CHAIRWOMAN SHOWALTER: I have nothing

00172

1 further.

2 E X A M I N A T I O N

3 BY JUDGE SCHAER:

4 Q. Mr. Gaines, it's my understanding that
5 Puget was supposed to file a least-cost plan as a
6 condition of its merger order; is that correct?

7 A. I don't know. I haven't reviewed the
8 merger order in that regard.

9 Q. Okay. Then I asked Mr. Story, and he
10 referred the question to you, has Puget Sound Energy
11 completed a least-cost plan since the merger?

12 A. No, we haven't. My understanding is that
13 we've committed to supply one by the end of this
14 year.

15 Q. Would a least-cost plan have been useful in
16 evaluating the Colstrip sale?

17 A. I don't really think so, and here's why.
18 This sort of thinking and supply decision-making goes
19 on continuously at the company, and the least-cost
20 plan, in my view, is just a snapshot of one point in
21 time of the current status of that thinking, and
22 putting it all into a format that is presentable in a
23 public document. So I don't think that the absence
24 of a published least-cost plan, you know, speaks much
25 at all about the sort of analysis that has gone on

00173

1 behind this decision at the Company.

2 Q. Well, that leads to my next question, which
3 is did PSE use any tools from its least-cost planning
4 to evaluate the Colstrip sale?

5 A. We've been trying to evolve our analytical
6 tools.

7 Q. Could you answer yes or no first, so I'm
8 sure I can follow where you're going with that?

9 A. Could you help me with the question again,
10 please?

11 Q. Did PSE use any tools from its least-cost
12 planning to evaluate the Colstrip sale?

13 A. No, it used some newer and better
14 analytical tools.

15 Q. So these are not tools that it would use in
16 the least-cost planning by the end of the year?

17 A. Yes, I think that it will use the new
18 Aurora tool going forward in its new plan, yes.

19 Q. Go ahead, please.

20 A. That's all.

21 Q. So you used a new tool called Aurora?

22 A. Yes, that's right.

23 Q. That's the only tool that you used for the
24 least-cost planning?

25 A. No, we used some spreadsheet analyses in

00174

1 the Colstrip work, we engaged Morgan Stanley as a
2 consultant to do some comparative analysis of other
3 transactions in generation sales. We used a number
4 of analyses.

5 Q. Regarding your scenarios analyzing the
6 sensitivity of the Colstrip sale to different
7 contingencies, when were these scenarios prepared?

8 A. When were they prepared?

9 Q. Yes.

10 A. Oh, they were prepared over time, as we
11 were getting into the transaction and completing it.

12 Q. Could you give me some range of dates or
13 approximate dates, please?

14 A. Oh, it would be a guess, but I suppose that
15 we probably began this analysis in -- oh, gosh, I
16 can't really recall.

17 Q. Looking at the scenarios that are exhibits
18 by you that are admitted in the case, when were those
19 prepared?

20 A. Well, again, we began the preparation of
21 those quite some time ago. We were refining them as
22 we were refining the presentation to the Commission.
23 So I can't tell you exactly when this particular set
24 was completed, but the forerunner analyses were begun
25 quite some time ago.

00175

1 Q. But you don't know any year or month or --

2 A. No, I just don't remember right offhand.

3 Q. Were these done before PSE made a decision
4 to pursue the sale of Colstrip?

5 A. Yes, we were doing analyses before we
6 decided to proceed.

7 Q. Who in the Company or what section of the
8 Company or what consultant prepared the scenarios?

9 A. Much of it was done in my unit, and some of
10 it was done by Morgan Stanley.

11 Q. Looking at page five of your direct
12 testimony, your testimony says that shedding Colstrip
13 would free PSE to meet load in all sorts of creative
14 and beneficial ways; is that correct?

15 A. On page five?

16 Q. Yes.

17 A. I don't find those exact words, but
18 generally, yes.

19 Q. Okay. Will some of these ways of meeting
20 demand have different costs and risks?

21 A. Oh, yes.

22 Q. How will PSE evaluate the costs and risks
23 of different ways of meeting future load that would
24 have been served by Colstrip?

25 A. It will use the techniques that it always

00176

1 has used. It will use production cost modeling, it
2 will use the sort of scenario analysis that we just
3 were talking about, it will use a variety of
4 techniques.

5 Q. I have heard, and I'm wondering if you have
6 heard, that PSE has said that it wants to be a
7 distribution-only company?

8 A. What the Company has said is that it
9 intends to emphasize and grow the distribution
10 business and streamline the energy supply business.

11 Q. And so that is a no to my question or --

12 A. Well, it's a little hard to give a yes or
13 no answer to a question like that, because it really
14 begs a lot of other questions about the form of the
15 industry structure going forward, open access, duty
16 to serve, all those things, so it doesn't lend itself
17 to a yes or no answer.

18 Q. Did Puget recently form a holding company?

19 A. The share owners have voted to approve the
20 formation of one, yes.

21 Q. And that would seem to make forming a
22 supply subsidiary relatively easy and attractive,
23 would you agree?

24 A. No, the Company has no intention to do
25 that.

00177

1 Q. So they aren't going to do it or it
2 wouldn't be easy and attractive?

3 A. All of the above.

4 Q. Okay. So it's your testimony today that
5 Puget Sound Energy has determined that it is not
6 going to form a supply subsidiary?

7 A. We have no present plans to do that.

8 Q. That's a little bit different statement
9 than I asked you. Have you made that decision yet?

10 A. We have no present plans to form an
11 unregulated supply sub.

12 Q. Okay. And have you -- I guess I asked you
13 have you decided not to form a supply sub, and you're
14 saying that, at present, you don't plan to. Does
15 that mean you've talked about it and decided not to,
16 or does that mean that maybe it's next week's topic
17 of discussion?

18 A. No, I'm not trying to hold that open. The
19 Company has expressed its strategy, and I just
20 reiterated it for you. It does not include the
21 formation of a supply subsidiary.

22 JUDGE SCHAER: Okay, thank you. Is there
23 anything further? Any redirect?

24 MR. HARRIS: Short redirect, Your Honor.

25 R E D I R E C T E X A M I N A T I O N

00178

1 BY MR. HARRIS:

2 Q. Mr. Gaines, while you were testifying about
3 the different scenarios, you said that it was --
4 unfortunately, one of the scenarios had been labeled
5 the base case. Why did you say that?

6 A. Oh, I think just that that terminology
7 tends to cause the reader to focus on that particular
8 case, and that wasn't the intention of this set of
9 analyses. It wasn't -- we didn't intend to assign
10 any greater weight to that case than any of the other
11 scenarios that we ran.

12 Q. Okay. And you were asked a number of
13 questions about what analysis you've done of
14 replacement power. Could you explain a little
15 further what you've done in that area?

16 A. Sure. We've done some production cost
17 modeling, again using the Aurora tool that we've
18 described here in connection with the Colstrip
19 evaluation. We've talked to a number of suppliers of
20 power, marketers for one, about the various forms of
21 supply arrangements that are available in the
22 marketplace going forward. We also have talked to
23 generation developers organizations who are
24 interested in developing new generation in this
25 region, primarily gas fired cogen.

00179

1 So we have this ongoing activity, really
2 always is ongoing, thinking about our future supply
3 needs.

4 MR. HARRIS: Your Honor, may I quickly pass
5 out a redirect exhibit and have it identified?

6 JUDGE SCHAER: Go ahead and distribute it,
7 and I'll look at it. Whose questions does this
8 relate to, Mr. Harris?

9 MR. HARRIS: This is the questions relating
10 to the replacement power analysis.

11 JUDGE SCHAER: You've handed me a one-page
12 document. It states at the top Proposed Pacific
13 Northwest Generation Projects. I will mark this for
14 identification as Exhibit C-32.

15 MR. CEDARBAUM: Your Honor, this is not
16 confidential; is that correct? I believe you said
17 C-32.

18 JUDGE SCHAER: Oh, I'm sorry. It's Exhibit
19 32. Thank you, Mr. Cedarbaum.

20 MR. HARRIS: Thank you. It is not
21 confidential.

22 Q. You were talking about your analysis of
23 replacement power. Could you tell us what this
24 document is?

25 A. This document shows at least some or most

00180

1 of the new gas fired generation projects that are
2 being considered or proposed by various developers
3 here in the Northwest. We've talked to many of these
4 developers about future power supply.

5 Q. Can you identify any of the developers
6 specifically that you've talked to?

7 A. Sure. We've talked to the Hermiston Power
8 Partners, we've talked to U.S. Gen, which is the
9 proponent of the Umatilla project. We've talked to
10 Florida Power and Light, who owns the development
11 rights at Everett, Plant Number 12 here. We've
12 talked to the Sumas developer.

13 There are also some plants that don't show
14 on this chart. There's a cogen project proposed in
15 the Port Angeles area in connection with the
16 Dai-Showa Mill that's being proposed by West Coast
17 Energy. We talked to them. There may be others.
18 I'm just not recalling them all.

19 MR. HARRIS: We'd offer Exhibit 32.

20 JUDGE SCHAER: Any objection? The
21 document's admitted.

22 Q. You were also asked, Mr. Gaines, about the
23 three different categories of savings identified in
24 the merger rate plan. Do you recall some of those
25 questions?

00181

1 A. Yes.

2 Q. And I believe you testified that you didn't
3 feel that PSE was limited to finding savings only in
4 those three categories?

5 A. That's right.

6 Q. And what was the basis for that statement?

7 A. Well, the primary basis is a provision at
8 page 26 of the merger order, where the Commission
9 actually is encouraging and expecting the Company, as
10 I recall it, to find savings in any and all areas
11 available.

12 Q. If I read you the sentence out of the
13 merger order, can you identify it for me? On page 26
14 -- this is in Exhibit 27, the merger order itself.
15 It says, We fully expect PSE to pursue synergy
16 savings and operating cost efficiencies aggressively
17 during the five years of the rate plan, including,
18 but not limited to what have been identified by the
19 joint applicants as best operating practice savings
20 and power stretch goals. Is that the statement that
21 you're talking about?

22 A. Yes, it is.

23 Q. And has the Company relied generally on the
24 rate plan set out in the merger order in making
25 business decisions?

00182

1 A. Well, it certainly is in the Company's mind
2 as it conducts its business on an ongoing basis, yes.

3 MR. HARRIS: I don't have any further
4 questions.

5 JUDGE SCHAER: Anything further, Mr.
6 Cedarbaum?

7 MR. CEDARBAUM: No.

8 JUDGE SCHAER: Mr. Manifold, go ahead.

9 MR. MANIFOLD: Just a couple.

10 R E C R O S S - E X A M I N A T I O N

11 BY MR. MANIFOLD:

12 Q. Mr. Gaines, you've commented that,
13 regarding the issue of projected energy deficits for
14 the Company, that the numbers that I'm reciting to
15 you were under critical water conditions and that, on
16 average, one has average water conditions, in
17 essence?

18 A. Yes.

19 Q. Okay. Do you have available to you your
20 response to Public Counsel Data Request 61? It's not
21 one of the exhibits.

22 A. I probably don't. Let me just look.

23 Q. We can show you -- I have a copy, if you'd
24 like?

25 A. Yes, please.

00183

1 JUDGE SCHAER: Let the record show that the
2 document's being provided to the witness.

3 Q. That data request or response shows the
4 Company's expected hydro -- its expected resources,
5 including hydro, at average conditions, rather than
6 critical water?

7 A. Yes.

8 Q. And is it correct that, of the roughly 887
9 megawatt deficit that we were discussing previously,
10 the differences between critical and average water
11 would make up about 200 megawatts of that difference?

12 A. That's the rule of thumb number that I
13 typically use on Puget's system, yes.

14 MR. MANIFOLD: Okay, thank you.

15 E X A M I N A T I O N

16 BY COMMISSIONER GILLIS:

17 Q. I had one question that your Counsel's map
18 reminded me of. You must at this point have
19 transmission rights for the Colstrip. How do you get
20 the power to your places you need it?

21 A. We do. It's a circuitous set of contracts,
22 but we own some transmission lines in Montana,
23 Bonneville owns some lines there that are special use
24 lines, we purchased the rights, and then the Colstrip
25 power enters the Bonneville main grid at a point

00184

1 called Garrison in western Montana and is wheeled
2 over Bonneville's main grid system. That's the
3 current lash-up for transmission.

4 Q. If you sold the Colstrip rights, then what
5 happens to those transmission rights in dollar terms?
6 I mean, the contracts, are they fixed contracts or
7 what?

8 A. The way that the transaction with PP&L
9 Global is set up is that there are two alternatives.
10 One is that Global may purchase the Company's share
11 of the owned transmission in Montana and also assume
12 the Company's Bonneville transmission rights. That's
13 one alternative. The other alternative is that PP&L
14 Global would not do that, Puget would continue to own
15 those assets and rights and would sign a long-term
16 wheeling contract with Global to move Global's new
17 Colstrip energy out of Montana towards the market.

18 Q. Would there be any losses or gains
19 associated with the transmission piece as a result of
20 the sale?

21 A. Yes, there is some gain associated with the
22 sale of the owned assets, transmission assets in
23 Montana. I think it's roughly 20 million.

24 Q. And I guess does your analysis provide an
25 offset for -- you're going to purchase power on the

00185

1 market, replacement purchase power. And do you make
2 in your estimates an offset to that? I guess you're
3 suggesting there's a gain from the sale of Colstrip
4 and that you're going to have to purchase
5 transmission rights to access alternative power from
6 these various sources on the map?

7 A. Yes, you're right. The assumption that
8 we've made there is that -- and it may or may not be
9 true, depending on the particular replacement
10 arrangements that we've made -- but we have assumed
11 that any replacement power in this analysis will
12 incur one Bonneville main grid wheel, as does the
13 Colstrip power. When it enters the main grid at
14 Garrison, we pay a Bonneville main grid wheel.
15 We've assumed that the replacement power in
16 all of these analyses would similarly incur that. So
17 there's a wash, if you will, between the with and
18 without Colstrip with respect to that Bonneville
19 wheeling charge.

20 COMMISSIONER GILLIS: Okay, thank you.

21 JUDGE SCHAER: Go ahead.

22 E X A M I N A T I O N

23 BY CHAIRWOMAN SHOWALTER:

24 Q. I just wanted to get you to analyze a bit
25 more your view of what the merger stipulation did or

00186

1 how it does or doesn't constrain us on this case or
2 treatment of this transaction. There are
3 merger-related savings and non-merger-related
4 savings, there are real property and non-real
5 property, and there's depreciable property --
6 depreciable assets and non-depreciable assets. So
7 that's three different variables.

8 A. Right.

9 Q. Now, is it your understanding that, under
10 the stipulation, if there is a property disposal
11 that's a direct result of the merger, there's a
12 specific provision in the stipulation for that?

13 A. That is my understanding, yes.

14 Q. But then if there is -- let's posit that
15 this property -- I know that a property transaction
16 is not a merger-related property transaction. Then
17 do I understand that you think that the stipulation
18 says that for property transactions that are not a
19 result of merger, they're handled in the manner that
20 the court of appeals set forth, but that when you go
21 and read that, it only relates to non-depreciable
22 property?

23 A. My understanding of this is not real
24 intimate, and therefore, probably not perfect. And
25 you might prefer to ask these questions of Mr. Story.

00187

1 But my general understanding is that this all relates
2 to real property.

3 Q. Okay. By this all, you mean?

4 A. These provisions of the merger stipulation.

5 Q. I'm not sure how that affects what my next
6 question was going to be, which is that if there's a
7 property transaction that's not related -- that's not
8 inherent or related to the merger, but also is not
9 non-depreciable property, then what?

10 A. I actually am not familiar enough with
11 these provisions that I probably should try to
12 answer.

13 CHAIRWOMAN SHOWALTER: All right.

14 JUDGE SCHAER: Is there anything further
15 for Mr. Gaines? Thank you for your testimony.

16 THE WITNESS: Thank you. I'm going to
17 suggest we take our afternoon recess at this time.
18 Please be back and ready to go at 3:10. And let's
19 clarify right now, you had prefiled testimony for Mr.
20 Champagne, Mr. Harris. Will you be calling him as a
21 witness today?

22 MR. HARRIS: No, we are not calling Mr.
23 Champagne as a witness, nor are we offering his
24 testimony in light of the stipulation reached among
25 the parties --

00188

1 JUDGE SCHAER: Okay.

2 MR. HARRIS: -- on the EWG issue, which is
3 the only issue Mr. Champagne addressed.

4 JUDGE SCHAER: So does this conclude your
5 presentation?

6 MR. HARRIS: Yes, it does, unless there's
7 any interest in recalling Mr. Story to answer that
8 last question, but otherwise we are done.

9 JUDGE SCHAER: So after the break, we'll
10 begin with the Staff's case, is that the plan?

11 MR. CEDARBAUM: That's right, Your Honor.
12 We would like to put Mr. Martin on first, followed by
13 Mr. Elgin. So if there are any cross-examination
14 exhibits for Mr. Martin, they can be distributed
15 during the break.

16 JUDGE SCHAER: I'm going to ask during the
17 break Mr. Martin take the stand and get organized.
18 I'd ask all parties to distribute any exhibits you
19 have for Mr. Martin before the end of the break. At
20 the break, I believe, Mr. Story, you were going to
21 check on access to copying and preparing responses to
22 the bench requests for Exhibits 21, 22, and 23.
23 Anything else we have put off till this break?
24 Hearing nothing, we are off the record.

25 (Recess taken.)

00189

1 JUDGE SCHAER: Let's be back on the record
2 after our afternoon recess. While we were at our
3 break, it appears that PSE has distributed copies of
4 responses to bench requests, which are Exhibits 21,
5 22 and 23, so I will ask you to look those over and
6 see if there's any objection to having them entered.
7 At this moment, they are entered in the record, but
8 if you have any objection to any portion of them,
9 let's use the date of next Friday that we're using
10 for the other exhibit and have those objections come
11 in.

12 Also while we were at break, certain
13 materials have been distributed as cross materials
14 for Mr. Martin, and Mr. Martin has assumed the stand.
15 Let's be off the record for just a moment.

16 (Discussion off the record.)

17 JUDGE SCHAER: Back on the record. Would
18 you like to call your witness, Mr. Cedarbaum?

19 MR. CEDARBAUM: Yes, Staff calls Roland
20 Martin.
21 Whereupon,

22 ROLAND MARTIN,
23 having been first duly sworn by Judge Schaer, was
24 called as a witness herein and was examined and
25 testified as follows:

00190

1 JUDGE SCHAER: Mr. Cedarbaum.

2 MR. CEDARBAUM: Your Honor, if we could
3 mark for identification Mr. Martin's prefiled direct
4 testimony and exhibit, please.

5 JUDGE SCHAER: Okay. We have marked for
6 identification as Exhibit T-33 the prefiled testimony
7 of Mr. Martin, RCM-T. I'm going to mark for
8 identification as Exhibit 34 the exhibit of Mr.
9 Martin, RCM-1. Are there any other materials for
10 this witness, Mr. Cedarbaum?

11 MR. CEDARBAUM: No.

12 JUDGE SCHAER: Go ahead, please.

13 D I R E C T E X A M I N A T I O N

14 BY MR. CEDARBAUM:

15 Q. Mr. Martin, directing your attention to
16 what's been marked as Exhibit T-33, is that your
17 direct testimony in this proceeding?

18 A. Yes, it is.

19 Q. And this was prepared by you under your
20 supervision and direction?

21 A. Yes.

22 Q. Do you have any corrections to make to the
23 exhibit at this time?

24 A. Yes, I do. On page four, line eight,
25 change the \$37.8 million to \$14,091,449.

00191

1 JUDGE SCHAER: Would you give us that
2 again, please? Page?

3 THE WITNESS: Four.

4 JUDGE SCHAER: Line eight?

5 THE WITNESS: Line eight.

6 JUDGE SCHAER: The 37,827 --

7 THE WITNESS: Yes, replace that with
8 \$40,091,449.

9 JUDGE SCHAER: And the last three numbers?

10 THE WITNESS: Four-hundred-forty-nine.

11 JUDGE SCHAER: Thank you.

12 Q. And what was the reason for that change?

13 A. This is to synchronize with the revised
14 response to DR-3, which is the same number that's
15 appearing in Exhibit 18.

16 Q. Do you have any other corrections to make
17 to your exhibit?

18 A. No, I don't.

19 Q. Looking at what's been marked for
20 identification as Exhibit 34, did you also prepare
21 this exhibit?

22 A. Yes.

23 Q. Is it true and correct, to the best of your
24 knowledge and belief?

25 A. Yes, it is.

00192

1 Q. And with the correction to your direct
2 testimony, that exhibit is also now true and correct,
3 to the best of your knowledge and belief?

4 A. Yes.

5 MR. CEDARBAUM: Your Honor, I'd offer
6 Exhibit T-33 and 34.

7 JUDGE SCHAER: Any objections? Those
8 documents are admitted. Is the witness available for
9 cross?

10 MR. CEDARBAUM: Yes, he is.

11 JUDGE SCHAER: Go ahead.

12 MR. HARRIS: Your Honor, we passed out
13 during the break two cross-examination exhibits. The
14 first is PSE Data Request Number Two at the top.
15 It's a single-page exhibit. We'd ask that be marked
16 for identification.

17 JUDGE SCHAER: I'm going to mark that
18 document for identification as Exhibit 35.

19 MR. HARRIS: And the second is a three-page
20 document. At the top of the first page, it says PSE
21 Data Request Number 14. We'd ask that be marked,
22 also.

23 JUDGE SCHAER: I'll mark that as Exhibit 36
24 for identification.

25 C R O S S - E X A M I N A T I O N

00193

1 BY MR. HARRIS:

2 Q. Good afternoon, Mr. Martin. Do you have
3 Exhibits 35 and 36 before you?

4 A. Yes.

5 Q. Do you recognize Exhibit 35 as the response
6 to PSE Data Request Number Two, prepared by you and
7 Mr. Elgin?

8 A. Yes.

9 Q. And do you recognize Exhibit 36 as your
10 response to PSE Data Request Number 14?

11 A. It's a partial response. I know that Item
12 B is not included in the exhibit.

13 Q. Okay. With that caveat, do you recognize
14 it as the Response Number 14, PSE Data Request?

15 A. Yes, I do.

16 MR. HARRIS: We'd offer both Exhibits 35
17 and 36 at this time.

18 JUDGE SCHAER: Any objection?

19 MR. CEDARBAUM: I don't have any objection
20 to the admission. I would like the opportunity to
21 decide whether or not to supplement 36 with the
22 documents that were under category B, just to make it
23 -- I don't know if this is a complete document or
24 not. I'd like the chance to check to see whether it
25 is or is not.

00194

1 JUDGE SCHAER: You certainly can have that
2 opportunity. When would you be able to tell us?

3 MR. CEDARBAUM: I'd try to do it during a
4 break today or, if we're finishing up today,
5 tomorrow. That would be after the record, I guess.
6 Can we set up some sort of a process that I can just
7 supplement this exhibit tomorrow, if necessary?

8 JUDGE SCHAER: Yes, if you'd like to
9 supplement Exhibit 36 with additional pages that are
10 part of this response, you may do so. Were you able
11 at the break, Mr. Harris, to check?

12 MR. HARRIS: Yes, we did check, and we do
13 not wish to supplement that prior exhibit.

14 JUDGE SCHAER: I'm going to admit Exhibits
15 35 and 36, then, noting that Exhibit 36 may be
16 supplemented by additional pages of the response,
17 should the Assistant Attorney General choose to do
18 so. Go ahead.

19 Q. Mr. Martin, I have a few questions for you
20 about the amortization time period. You understand
21 from PSE's application that it selected a -- or is
22 proposing a five-year amortization of the gain on the
23 sale?

24 A. Yes, that's my understanding.

25 Q. Yeah. And that's not a proposal that you

00195

1 agree with; correct?

2 A. That's correct.

3 Q. Let's assume for a moment that there was no
4 rate plan in effect. Take the rate plan completely
5 out of the picture, and assume otherwise all the
6 facts are the same. There's a gain on the sale or
7 there will be a gain on the sale of about \$40
8 million.

9 A. Yes.

10 Q. Okay. In setting the appropriate
11 amortization time period, would you consider the size
12 of the gain of the sale -- gain on the sale as one of
13 the factors?

14 A. That's one of the considerations.

15 Q. And would you also consider the effect of
16 recognizing the gain, what effect that would have on
17 the financial results of the Company and on
18 ratepayers?

19 A. Since the policy of the Commission that
20 we're relying on is that the gain for property that's
21 been supported by the ratepayers and rate base is
22 supposed to go to the ratepayers, so it will be a
23 consideration on the customers' rates.

24 Q. And would the idea be to pick an
25 amortization period that smoothed out the effect of

00196

1 the gain, spread it over a number of years, but not
2 too many years, so it didn't have any effect at all?

3 A. That's a consideration, as I mentioned
4 earlier. But in deciding what's the time frame of
5 amortization of gain or loss to that effect, it would
6 be dependent on the circumstances, I believe,
7 particularly that we are suggesting that we bring it
8 to a general rate case. In a general rate case,
9 there's a lot of considerations, and one of them
10 might not involve multi-year amortization at all.

11 Q. So it might be appropriate to recognize the
12 gain immediately?

13 A. Exactly. One example is this time it was a
14 loss, the loss on the Creston project. I believe
15 there was a proposal by both Staff and the Company to
16 amortize over a number of years, but the Commission
17 decided to flow it in one year, flow it through in
18 one year.

19 Q. Do you think it would be likely that the
20 Commission would recommend that a gain of \$40 million
21 be flowed through in a single year?

22 A. That's a possibility, because if there is a
23 regulatory asset added to offset it against, we can
24 say that it's been offset in one year.

25 Q. I think you mentioned already that it's

00197

1 your position that any gain should be deferred until
2 the next general rate case; correct?

3 A. That's our recommendation, yes.

4 Q. And you rely on -- I'm looking at Exhibit
5 36, and you point to two documents. You point to
6 page nine of the merger stipulation, which is the
7 second page of Exhibit 36; correct?

8 A. Yes.

9 Q. And on that page, you're referring to the
10 paragraph that's labeled gains from transfers of real
11 property; correct?

12 A. Which line is that?

13 Q. That's line seven on page nine of the
14 stipulation, which is page two of Exhibit 36. Are
15 you with me?

16 A. Which line is it?

17 Q. I'm talking about line seven, paragraph D.

18 A. Yes, yes.

19 Q. That's the paragraph you're relying on;
20 correct?

21 A. That's right.

22 Q. And in there, there's a reference to the
23 Washington Court of Appeals decision in Docket Number
24 29404-1. Do you see that on line 13?

25 A. Yes, I see it.

00198

1 Q. You're relying specifically on the
2 stipulation out of that Washington Court of Appeals
3 Docket Number 29404-1, are you not?

4 A. Actually, I'm relying on the principle
5 behind the Washington Court of Appeals stipulation.

6 Q. And that stipulation applied solely to non-
7 depreciable real property, did it not?

8 A. That's what the stipulation is, that's
9 correct.

10 MR. HARRIS: Okay. I don't have any
11 further questions. Thank you.

12 JUDGE SCHAER: Any questions, Mr. Manifold?

13 MR. MANIFOLD: Yes.

14 C R O S S - E X A M I N A T I O N

15 BY MR. MANIFOLD:

16 Q. Mr. Martin, the Colstrip plant is located
17 on land?

18 A. That's correct.

19 Q. Is the land it's located on part of the
20 Company's investment?

21 A. That is part of the rate base.

22 Q. And it's been in rate base?

23 A. Yes.

24 Q. And it's part of what's being sold?

25 A. Pardon me?

00199

1 Q. The land is part of what's being proposed
2 to be sold to Global?

3 A. Yes.

4 Q. Okay. Do you have a copy of what was
5 marked, but not yet admitted, as Exhibit 19?

6 A. Yes, I do.

7 Q. I'd like to ask you a couple questions
8 about it. Is Staff using the same gain on sale that
9 the Company is using as that number changes over
10 time?

11 A. Yes, though we move as their target moves.

12 Q. Okay. And does Staff, in its analysis,
13 include analyzing power costs as they go into the
14 future, both with and without the Colstrip plant in
15 the Company's possession?

16 A. Yes, it's a comparison of cost of Colstrip
17 power with market power.

18 Q. Does Staff take into account in its
19 analysis the new Montana property tax?

20 A. Not in my exhibit. I didn't take that into
21 account.

22 Q. All right. Do you think it's appropriate
23 or inappropriate to take it into account if you were
24 doing it today?

25 A. With the objective that I'm doing in my

00200

1 exhibit, it's not appropriate, in my opinion.
2 Because what I'm trying to do is to capture the
3 difference of cost and rates, the reduction due to
4 the sale of Colstrip cost. So if the current rates
5 reflect -- or does not reflect this at this point,
6 then it might be part of the benefit that's being
7 captured.

8 Q. Okay. Moving down this page, does the
9 Staff analysis look at the period of time during the
10 rate plan versus after the rate plan as separate
11 elements of the analysis?

12 A. Maybe it's a good idea to clarify this
13 point, that when you say Staff, Mr. Elgin went
14 through a different path, different from what I'm
15 doing, because I have a different purpose. So in my
16 case, you can see from my exhibit that the time frame
17 extends beyond the rate plan period.

18 Q. Would it be most appropriate to ask the
19 rest of these questions of Mr. Elgin, rather than
20 yourself, for the Staff?

21 A. As I have said, we have different
22 objectives in doing the analysis, so --

23 MR. MANIFOLD: Yeah, all right. Thank you.

24 No other questions.

25 JUDGE SCHAER: Mr. Van Cleve.

00201

1 MR. VAN CLEVE: No questions, Your Honor.

2 JUDGE SCHAER: Commissioners, do you have
3 any questions for Mr. Martin?

4 COMMISSIONER GILLIS: No.

5 COMMISSIONER HEMSTAD: No.

6 JUDGE SCHAER: I have two.

7 E X A M I N A T I O N

8 BY JUDGE SCHAER:

9 Q. What was the objective of your testimony,
10 Mr. Martin?

11 A. The objective of my testimony is to make a
12 measurement of the benefits that should go to the
13 ratepayers considering the effect of the sale of
14 Colstrip on power cost.

15 So the analysis, as presented by the
16 Company in their different scenarios, the study shows
17 that the short-term reduction in power cost is going
18 to be overwhelmed by increasing power cost in the
19 future, such that it's necessary to make a deferral
20 or not to flow through the short-term benefits so
21 that the ratepayers will not be harmed or
22 unnecessarily disadvantaged when they are going to be
23 requested to shoulder the higher costs in the future.

24 Q. Then I do have a bench request for you.

25 I'd like you to provide a calculation of the gain on

00202

1 sale of 39,403,538, which you show as being after the
2 environmental cost was removed. Do you have a work
3 paper that supports that number?

4 A. Yes.

5 Q. We'll have that be, then, Exhibit 37. And
6 when can that be provided?

7 A. Actually, the record might be helped with
8 the Exhibit 18, which is -- I believe is the later
9 version of this figure, just to make a
10 cross-reference.

11 Q. Okay.

12 A. The difference between the two numbers, as
13 was acknowledged by Mr. Story this morning, is the
14 removal of the environmental remediation cost.

15 Q. So the number that is, then, Exhibit 18 --

16 A. There are two numbers in Exhibit 18.

17 Q. Okay.

18 A. So the difference is the removal of the
19 environmental remediation cost.

20 JUDGE SCHAER: So with that, then, I will
21 withdraw the bench request and we will look that
22 number up. Is there any redirect, Mr. Cedarbaum?
23 Anything further for this witness? Go ahead.

24 E X A M I N A T I O N

25 BY COMMISSIONER HEMSTAD:

00203

1 Q. Mr. Roland, I'd like to ask you a question.
2 Assuming we did not have the background here of the
3 merger and this sale is proposed and approved, then
4 what would the Staff be recommending then as to how
5 the gain should be treated?

6 A. I would go with the treatment of the
7 stipulation, which is to defer the gain for
8 consideration in the general rate case.

9 Q. So you would also there just simply defer
10 it to the next rate case?

11 A. Yes.

12 Q. All right. Then in the next rate case,
13 then, what kind of recommendations generally would
14 the Staff be making as to how the gain should be
15 treated?

16 A. One example that I mentioned to Mr. Harris
17 is --

18 Q. This may be repeating what you've already
19 answered, I'm sorry.

20 A. Yes. One way might be to examine what are
21 the regulatory assets that are being shouldered by
22 the ratepayers in rate base. So if those regulatory
23 assets are being amortized in rates over 10 years and
24 we have this credit that can offset it, then it makes
25 sense, I believe, to offset it still, so that it's a

00204

1 wash and the ratepayers will not be burdened anymore.

2 COMMISSIONER HEMSTAD: I see. Thank you.

3 E X A M I N A T I O N

4 BY JUDGE SCHAER:

5 Q. And as part of that consideration when you
6 talk about the credit, would you be suggesting that
7 all of the benefit of the sale then flow to
8 ratepayers?

9 A. To the extent that they are paying the cost
10 that's being offset, I would say that the benefit
11 goes to the ratepayers, who are a hundred percent
12 bearing the cost of those burdens.

13 JUDGE SCHAER: Anything further for Mr.
14 Martin? Thank you for your testimony. Let's go off
15 the record for a moment and allow for a change of
16 witnesses.

17 (Recess taken.)

18 JUDGE SCHAER: Okay. Back on the record.
19 Would you like to call your next witness, Mr.
20 Cedarbaum?

21 MR. CEDARBAUM: Yes, Staff calls Kenneth
22 Elgin.

23 Whereupon,

24 KENNETH ELGIN,

25 having been first duly sworn by Judge Schaer, was

00205

1 called as a witness herein and was examined and
2 testified as follows:

3 JUDGE SCHAER: Witness is sworn, Mr.
4 Cedarbaum.

5 MR. CEDARBAUM: Thank you. If we could
6 just take a moment to mark his testimony and exhibits
7 for identification.

8 JUDGE SCHAER: Yes. I've marked for
9 identification as Exhibit T-37 the direct testimony
10 of Mr. Elgin. As 38, his Exhibit KLE-1; as 39, his
11 KLE-2; as 40, his KLE-3; as 41, his KLE-4; and as 42,
12 his KLE-5. And as part of Exhibit T-37, I have also
13 incorporated pages to be distributed at the beginning
14 of the session which correct typographical errors.

15 MR. CEDARBAUM: Thank you.

16 D I R E C T E X A M I N A T I O N

17 BY MR. CEDARBAUM:

18 Q. Mr. Elgin, referring you to Exhibit T-37,
19 does this exhibit constitute your direct testimony in
20 this case?

21 A. Yes.

22 Q. And this was prepared by you or under your
23 supervision; correct?

24 A. Yes.

25 Q. It's true and correct, to the best of your

00206

1 knowledge and belief?

2 A. Yes.

3 Q. Referring you to Exhibits 38 through 42,
4 that have been marked for identification, are these
5 exhibits attached to your direct testimony?

6 A. Yes, they are.

7 Q. And they were prepared by you or under your
8 supervision and direction?

9 A. Yes.

10 Q. They're true and correct, to the best of
11 your knowledge and belief?

12 A. Yes, they are.

13 MR. CEDARBAUM: Your Honor, I would offer
14 Exhibit T-37, and Exhibits 38 through 42.

15 JUDGE SCHAER: Any objections? These
16 documents are admitted.

17 MR. CEDARBAUM: Mr. Elgin is available for
18 cross.

19 JUDGE SCHAER: Okay.

20 MS. HARRIS: Your Honor, we previously
21 passed out a packet of cross-examination exhibits.
22 If I could stop to mark those for identification, it
23 would be helpful.

24 JUDGE SCHAER: Certainly.

25 MS. HARRIS: The first exhibit is a

00207

1 confidential exhibit.

2 JUDGE SCHAER: I'm marking for
3 identification as Exhibit C-43 --

4 MR. CEDARBAUM: Just a clarifying question.
5 Reviewing this, mine shows a TS-34, which was the top
6 secret designation from the merger proceedings. Are
7 we going to consider these as top secret or just
8 plain old confidential?

9 MS. HARRIS: It's just a plain old
10 confidential document at this time.

11 JUDGE SCHAER: Okay. Well, I do have a
12 concern, because I note that it's marked as
13 confidential per the protective order in that docket,
14 rather than this docket.

15 MR. HARRIS: I'm sorry, Your Honor, that
16 marking is actually the original marking from the
17 merger itself.

18 MS. HARRIS: We can redact that.

19 MR. HARRIS: We'll redact it to eliminate
20 confusion and re-stamp it.

21 JUDGE SCHAER: Okay. Because I do need it
22 stamped for this docket, as well, please. Thank you.
23 Go ahead, please. I have marked as C-43 a document
24 which is identified as TS-39 in the upper corner. I
25 have marked for identification as Exhibit 44 selected

00208

1 pages from the merger docket in this matter, pages
2 1068 and 1069.

3 I've marked for identification as Exhibit
4 45 a copy of a motion by Commission Staff to exclude
5 rebuttal testimony in Docket Number UE-960195. I've
6 marked for identification as Exhibit 46 a cover
7 letter -- it appears to be an application from the
8 then Washington Water Power Company in Docket Number
9 U-87-1533-AT, which that company sought an order
10 authorizing sale of a combustion turbine generator.

11 I've marked for identification as Exhibit
12 47 PSE Data Request Number Three, and response
13 thereto. Marked for identification as Exhibit Number
14 48, correspondence from Washington Water Power
15 Company to the Commission in 1986 regarding cause
16 Number FR 86-150. And was this an order from that
17 proceeding?

18 MS. HARRIS: I believe, Your Honor, this is
19 the application.

20 JUDGE SCHAER: Number 48, this sale and
21 leaseback, Number 48. Marking for identification as
22 Exhibit 49 additional pages from the merger
23 proceeding between Puget Sound Power and Light and
24 Washington Natural Gas, pages beginning at 2423.

25 And we're marking for identification as

00209

1 Exhibit 50 correspondence from Perkins Coie, Steven
2 C. Marshall, to Donald Trotter and Chuck Adams, along
3 with what appears to be a draft settlement proposal.
4 Is that all the exhibits, Ms. Harris?

5 MS. HARRIS: I hope so, Your Honor.

6 JUDGE SCHAER: All right. Go ahead,
7 please.

8 C R O S S - E X A M I N A T I O N

9 BY MS. HARRIS:

10 Q. Good afternoon, Mr. Elgin.

11 A. Hello.

12 Q. The first couple questions actually came to
13 mind listening to Mr. Martin's testimony. I'd like
14 to talk to you a little bit about the scope of your
15 analysis. In the preparation of your testimony, did
16 you or did you direct anyone else to perform an
17 analysis of the adequacy or the fairness of the price
18 being offered today for the Colstrip Generation
19 Plant?

20 A. No.

21 Q. Did you perform any analysis on PSE's
22 current costs in general?

23 A. Current costs. Did I personally?

24 Q. Or did you ask anyone to perform that
25 analysis in preparation for your testimony?

00210

1 A. No, I assumed that those analyses would be
2 done in the context of the Company's ongoing
3 semi-annual reports and operations, but specifically
4 related to this transaction, no.

5 Q. Did you perform any analysis on any costs
6 being absorbed by the Company during the rate plan
7 period?

8 A. I don't understand the question.

9 Q. Did you perform any sort of analysis just
10 looking at those costs that are specifically absorbed
11 by virtue of the rate plan by the Company during the
12 rate plan period?

13 A. I still don't understand the question.

14 Q. Did you perform any analysis on any costs
15 absorbed by the Company?

16 A. I don't --

17 MR. CEDARBAUM: Your Honor, I guess I'll
18 object. I know the witness is going to say he
19 doesn't understand the question. I guess I'm not
20 clear on the question, either, in part because I
21 don't understand the word absorbed.

22 MS. HARRIS: That's fair.

23 JUDGE SCHAER: Are you willing to restate
24 the question, then? Go ahead, please.

25 MS. HARRIS: I'll try it one more time.

00211

1 Q. Did you perform any analysis of any costs
2 that the Company is incurring during the rate plan
3 period?

4 A. Yes.

5 Q. And what type of analysis did you do?

6 A. I regularly look at the Company's operating
7 results that they report on their quarterly
8 statements and annual statements, and I regularly
9 examine the Company's costs with respect to how they
10 report those and management discussion of those
11 continuing in ongoing operations in providing
12 electric and gas service to its shareholders.

13 Q. Did you use that regular monitoring in your
14 analysis and preparation of your testimony?

15 A. Not specifically. It was in the context
16 that it's part of my job to know where the Company's
17 at, so in that sense, yes, I did. But to say that it
18 specifically related to I took that analysis and
19 applied it directly to the testimony I prepared in
20 this docket, I did not do that.

21 Q. Okay. On page three of your testimony, you
22 give what I have termed Option A, where you recommend
23 that the Commission reject the proposed transaction
24 because PSE's proposed accounting treatment, in
25 conjunction with the continued operation of the rate

00212

1 plan, may prove to harm customers.

2 A. That's correct.

3 Q. Is that a fair reading?

4 A. That's correct.

5 Q. Later in your testimony, you seem to take
6 two different approaches to the rate plan, and focus
7 in on that. One approach is that the sale or the
8 proposed transaction is not within the power stretch
9 savings. Is that an accurate reading of your
10 testimony?

11 A. I'm saying -- I'm not sure I understand
12 your question in terms of where you want me to go to
13 later in my testimony and where I say that. So if
14 you could maybe point me to something so I have a
15 little context. I don't understand your question
16 quite fully. It seems like you're asking a couple of
17 things. I'm having difficulty connecting with that.

18 Q. On page 14 of your testimony, line 18, you
19 state that Colstrip was never factored into the
20 analysis of any power stretch savings?

21 A. That's correct.

22 Q. Is the term power stretch savings defined
23 in the merger order?

24 A. No, it's not, and it was not defined in the
25 stipulation, either. But I think in the context of

00213

1 an analysis of the record and what the Commission was
2 presented with respect to testimony from primarily
3 Mr. Torgerson, is that -- and the general
4 understanding was that power stretch savings in that
5 docket were related to the Company's PURPA resources,
6 and testimony from Mr. Sonstelie regarding the
7 Company's need to manage those cost pressures during
8 the five years of the Company's initially-proposed
9 rate plan from the merger case.

10 So I think it was generally understood, by
11 everybody who was involved, at least from Staff's
12 perspective, that power stretch savings were related
13 to those purchase power contracts, and what the
14 Company could do to alleviate the pressures that were
15 anticipated and the increasing costs that were
16 expected in the next five-year period from those
17 contracts.

18 Q. Now, in your deposition, you identified
19 certain documents that were used in the merger
20 proceeding as -- I believe you said the best
21 statement of your position?

22 MR. CEDARBAUM: Your Honor. Sorry, were
23 you finished with the question? I was just going to
24 ask that we have been given notice that Mr. Elgin's
25 deposition was going to be offered into evidence. If

00214

1 it is, let's do it, so he can at least have it in
2 front of him to refer to.

3 JUDGE SCHAER: Were you planning to --

4 MS. HARRIS: Offer it into evidence?

5 JUDGE SCHAER: -- to offer his deposition
6 into evidence, Ms. Harris?

7 MS. HARRIS: We can mark the deposition for
8 identification and offer it into the record, yes.

9 JUDGE SCHAER: Well, is that part of the
10 Company's plan?

11 MS. HARRIS: Yes.

12 JUDGE SCHAER: Do you need to have it
13 entered in as part of your --

14 MS. HARRIS: We would like to have the
15 deposition in the record.

16 JUDGE SCHAER: Have you pre-distributed
17 that to the Commission?

18 MR. HARRIS: Can I address that, Your
19 Honor? I sent out notice that we were going to be
20 offering both of the depositions in an effort --
21 under the provision of the rule that allows entering
22 the depositions to avoid having to repeat questions
23 and answers. We distributed them electronically. We
24 brought the paper copies with us and we have them
25 here.

00215

1 JUDGE SCHAER: Because I don't believe I
2 received a copy of it yet. I don't believe those
3 copies have been distributed through the Commission,
4 so I'm going to ask that -- I wish they'd been
5 distributed with the other materials here, but they
6 should be distributed now, please.

7 MR. HARRIS: Okay. We can do that quickly.

8 JUDGE SCHAER: I guess I should say, as a
9 reminder, certain things are sent in electronically
10 as a first step so that they reach people quickly.
11 You always need to follow up with paper copies by
12 overnight messenger or something else.

13 MR. HARRIS: I'm sorry for the
14 misunderstanding.

15 JUDGE SCHAER: Probably, in part, my
16 misleading statements or confused statements, Mr.
17 Harris, so just for future reference, please keep
18 that in mind.

19 I'm going to mark as Exhibit 51 for
20 identification the deposition transcript of Mr.
21 Elgin.

22 THE WITNESS: Do you have the reference? I
23 have my copy, so if you could just tell me the page?

24 MS. HARRIS: Are we ready, Your Honor?

25 JUDGE SCHAER: Do you want to offer this?

00216

1 MS. HARRIS: I'd offer -- or I'd mark for
2 identification --

3 JUDGE SCHAER: I've marked it for
4 identification as Exhibit 51.

5 Q. Mr. Elgin, do you have in front of you a
6 copy of your deposition?

7 A. Yes.

8 Q. And do you recognize that to be your
9 deposition?

10 A. I have, yes.

11 MS. HARRIS: I offer the deposition of Ken
12 Elgin as Exhibit 51.

13 JUDGE SCHAER: Any objection?

14 MR. CEDARBAUM: No.

15 JUDGE SCHAER: That document is admitted.
16 Now, could you refer us all to the page, please?

17 MS. HARRIS: Sure.

18 Q. Mr. Elgin, I'm actually looking at page 45
19 of your deposition.

20 A. Yes, I have that.

21 Q. And I believe -- and I have a small version
22 -- at approximately line five, you state -- Mr.
23 Harris asked you, "Did you assemble a file of records
24 for the merger proceedings." And line five, you
25 stated, "The most significant document was the rating

00217

1 agency presentation in the merger proceeding."

2 A. Yes.

3 Q. Were you referring to the power stretch
4 savings at this point in your deposition?

5 A. Well, I think there was some confusion in
6 the deposition as to what specific document that we
7 were referring to, but there was a document that I
8 reviewed that the Company provided where it
9 identified specifically its estimate of power stretch
10 savings as a line item and best practices as a line
11 item in the presentation as what were the targets for
12 the Company during the five-year period in an effort
13 to discuss with them what the merged company was
14 anticipating to do. But I wasn't sure whether it was
15 Exhibit 107 or 34 or 35, but I think we all had in
16 mind what specific document I was referring to.

17 Q. Mr. Elgin, can you turn to what has been
18 marked for identification as C-43?

19 JUDGE SCHAER: Before you do that, Counsel,
20 I'm looking at the deposition, at the page you
21 suggested, and it appears to refer to some other
22 documents. Were those exhibits to the deposition or
23 --

24 MS. HARRIS: I don't believe so.

25 JUDGE SCHAER: -- what are those

00218

1 references?

2 MS. HARRIS: I do not believe so, Your
3 Honor.

4 JUDGE SCHAER: Okay. Do you know what
5 those references are?

6 MS. HARRIS: TS-34 and TS-107, Your Honor?
7 In the deposition, I think they were referring to
8 documents, top secret documents that are in the
9 merger docket.

10 JUDGE SCHAER: Okay. So that is referring
11 to other documents that were in that docket, but were
12 not made exhibits to this deposition; is that
13 correct?

14 MS. HARRIS: Yes, Your Honor.

15 JUDGE SCHAER: Okay. Go ahead, please.

16 Q. Mr. Elgin, could you turn to page five of
17 what has been marked C-43?

18 A. I have that.

19 Q. In the fourth bullet point, could you
20 please read the fourth bullet point?

21 A. Achieving power stretch goals will result
22 in 152 million savings for the study period.

23 Q. And then, on the next page, page six of the
24 document, would you note the last line item is the
25 power stretch cost goals?

00219

1 A. Yes, I see those.

2 Q. Is this the document you were referring to
3 in your deposition?

4 A. This was one of the documents, but this is
5 the one -- at this particular point, I think Mr.
6 Harris and I were discussing this, as I clarified,
7 the document that laid out the specific numbers as a
8 specific line item.

9 Q. Does this document define power stretch
10 goals?

11 A. No, other testimony provided by other
12 witnesses define -- at least suggest that -- as I
13 said, it's not explicit, but suggest that power
14 stretch savings were, in fact, related to the
15 Company's reformation and of the PURPA resources.

16 I would add that if you notice that these
17 documents quite explicitly go through in detail Puget
18 Sound Power and Light, and one of the other things
19 that's compelling about this document is that any of
20 these financial parameters, should Colstrip be sold
21 during the rate plan period through 2001, these
22 figures -- for example, depreciation and
23 amortization, interest charges -- many of these
24 financial ratios on the second page would also change
25 dramatically as the Company were to sell major assets

00220

1 and what that impact would have on the financial
2 model of the Company going forward.

3 So I think that if you look at this, this
4 document pretty much, even though it doesn't say
5 explicitly Colstrip or something isn't in there, it's
6 pretty clear that Colstrip, on an ongoing basis, is
7 in here. These financial ratios unequivocally
8 demonstrate that Colstrip is part of the Company's
9 analysis for the rate plan period.

10 Q. Do any of these line items portray any
11 major restructuring of power purchase contracts?

12 A. No, that's what -- when the Company -- if
13 you turn to page six, power stretch goals were in
14 there. And in Staff's case, we attempted to include
15 those in our analysis, as specific line items in our
16 analysis. As a going forward basis, what would be an
17 appropriate rate plan for the Company as a merged
18 entity. So even though the Company did not, Staff
19 did put those in there in its direct case in the
20 merger.

21 Q. But those costs are not included in this
22 document?

23 A. No, but I'm saying -- I'm saying that if
24 power stretch savings were something like the sale of
25 Colstrip, this document would look different, and

00221

1 that's what I'm trying to say, is I looked for
2 something that would show what the impact of a sale
3 of Colstrip would have on the Company's financials,
4 and everything that I looked at in the merger,
5 particularly this document, is very compelling that
6 Colstrip is included in the analysis and that these
7 savings suggest and -- at least it's my
8 understanding, when I reviewed the record and when I
9 was involved in the case, that these power stretch
10 goals were, in fact, for reformation of the PURPA
11 contracts.

12 Q. Could you show me in this document, though,
13 where the restructuring of Tenaska is shown in this
14 document?

15 A. Well, the restructuring of Tenaska would
16 theoretically be embedded in the figures on page six,
17 power stretch goals of 27 million, beginning in 1997
18 and twenty-eight-five in 1998. And then, if you look
19 at -- I don't have that right in front of me, but if
20 you look at a previous exhibit that was just
21 distributed, you can see a calculation of the Tenaska
22 savings. That would be part and parcel of that
23 twenty-eight-million-five-hundred that was stretch.
24 So I think they're there.

25 I mean, this was, again, prepared in 1996,

00222

1 on a prospective basis, and this is what we
2 understood that those savings were to represent.

3 Q. But nowhere in this document does it
4 actually state what is in a power stretch goal?

5 A. That's correct.

6 Q. Mr. Elgin, I'd refer you to page 12 of your
7 testimony.

8 A. One second, please. Yes.

9 Q. On page 12 of your testimony, you state
10 that the merger order will not apply because Colstrip
11 clearly falls within a category which I believe you
12 identify as a property transfer not directly related
13 to the merger?

14 A. That's correct.

15 Q. Could you please turn to page 22 of the
16 merger order?

17 A. Yes.

18 Q. Page 22 of the merger order, it says, Gains
19 from transfers of the real property that are not a
20 direct results of the merger will be deferred as set
21 forth in the stipulation and order of dismissal dated
22 May 26th, 1992, Washington Court of Appeals, Number
23 29404-1; is that correct?

24 A. Yes, that's an accurate reading of the
25 order.

00223

1 Q. And do you believe that the Colstrip
2 transaction represents a gain from a transfer of real
3 property?

4 A. No, that's not my testimony. I would go to
5 the next sentence on page 22, that says, Gains and
6 losses from property transactions that are directly
7 merger-related will be included in current earnings
8 rather than deferred.

9 That statement, that sentence in the order
10 states for the proposition that the savings that were
11 identified directly related to the merger, which were
12 included in Mr. Flaherty's analysis, will be used to
13 -- or will be recognized in current earnings, and
14 that any other property transaction, whether it be a
15 gain or a loss, shall be deferred. That's the way I
16 read what the Commission said in this order. That
17 sentence.

18 So the first sentence deals just with
19 property that's non-depreciable. I agree with Mr.
20 Story in that respect. That's what this stipulation,
21 is my understanding of what that piece refers to,
22 because there's property -- ongoing property that the
23 Company has held, primarily plant held for future
24 use. And as those properties come in and out of rate
25 base, this stipulation applies and will continue to

00224

1 apply.

2 Q. Okay. Then do you believe that the gain
3 from Colstrip was not a result, a direct result of
4 the merger?

5 A. Yes, the gain from Colstrip, I agree that
6 it was not identified by Mr. Flaherty, nor was it
7 identified by the Company. It was assumed to be
8 included in the ongoing results of the Company, and
9 so therefore, the gain or the loss associated with
10 its sale shall be deferred, what this order says.

11 Q. Mr. Elgin, in your testimony, you state
12 that it has been presented by the Company that they
13 have the -- I would say the strategy to become a
14 distribution company?

15 A. Yes.

16 Q. Do you think it's consistent with becoming
17 a distribution company, or primarily a distribution
18 company, to take advantage of opportunities to
19 streamline your energy portfolio?

20 A. Absolutely.

21 Q. Do you think that the Company had the
22 strategy of becoming a distribution company at the
23 time of the merger?

24 A. Yes, I believe it had that.

25 Q. So in effect, would it be fair to say that

00225

1 streamlining the energy portfolio would be a direct
2 result of a merger to become a distribution company?

3 A. Yes, I think that that's what my preferred
4 option that I'm recommending to the Commission be, is
5 that if -- if the merger stands for the proposition
6 that, at the end of the rate plan period, Puget has
7 effectively managed its cost and has managed its
8 supply portfolio, captured all the synergy savings
9 and best practice savings and, at the end of the rate
10 plan, can go forward and offer open access, which was
11 at least my understanding of what one of the elements
12 of the strategies surrounding the merger would be,
13 and that stranded costs are no longer an issue, then
14 I think that that's a fair reading of what the merger
15 stood for and what the Company's strategy at the time
16 of the merger was on an ongoing basis.

17 Q. Do you think contemplation of open access
18 is a fair reading of the merger order?

19 A. I think, based on the testimony of Mr.
20 Sonstelie and I think basically with the introduction
21 of Schedule 48 during the merger proceedings, I think
22 open access was a very real possibility and was
23 contemplated by the Commission in terms of approving
24 the combination.

25 Q. My question, though, is open access

00226

1 addressed in the merger order?

2 A. It is not explicitly addressed. No, it's
3 not.

4 Q. Do you think that something along the
5 magnitude of open access for a company would be
6 addressed in a Commission order?

7 A. Yes.

8 Q. Mr. Elgin, will you please refer to what
9 has been marked as 44?

10 A. This is transcript from cite 1055 going
11 forward? Yes.

12 Q. Do you recognize that document?

13 A. Yes.

14 MS. HARRIS: I offer what has been marked
15 as Exhibit 44.

16 MR. CEDARBAUM: I guess I'd object on
17 relevance. I don't know what's -- you can put a
18 bunch of paper in, but it needs to be relevant paper.

19 JUDGE SCHAER: The objection is relevance,
20 Ms. Harris.

21 MS. HARRIS: The relevance, Your Honor --
22 if I could have some questioning that would show the
23 relevance of the document.

24 JUDGE SCHAER: Would you like to withdraw
25 your offer, then, and provide some foundation?

00227

1 MS. HARRIS: Well, the relevance of the
2 document, Your Honor, is questioning regarding the
3 power stretch goals.

4 JUDGE SCHAER: So would you like to provide
5 some foundation on that?

6 MS. HARRIS: I withdraw my offer. I'll
7 provide some foundation, if that would help you.

8 JUDGE SCHAER: All right.

9 Q. Mr. Elgin, could you please refer to or
10 turn to page, what is 1069, please, the third page of
11 the document? And the question is that there's been
12 some confusion about whether power stretch goals, in
13 fact, are forecasts or something else, targets or
14 goals.

15 JUDGE SCHAER: What page are you on, Ms.
16 Harris?

17 MS. HARRIS: The last page, Your Honor,
18 the third page. It is 1069.

19 JUDGE SCHAER: What line number, please?

20 MS. HARRIS: I have the witness directed at
21 line five.

22 JUDGE SCHAER: Thank you.

23 THE WITNESS: Well, that's not a statement;
24 that's a question from Mr. Harris to Dr. Lurito in
25 the case. So I don't know if that's a statement or

00228

1 is it a question.

2 Q. I just read the question, Mr. Elgin. I
3 would like to direct you to the answer, if you could
4 please review that answer starting at line five. Is
5 this a fair statement of the testimony during the
6 merger proceedings?

7 A. This is what Dr. Lurito testified to
8 regarding a question from Mr. Harris whether or not
9 Staff actually looked at the probability of the power
10 stretch goals and the best practices goals being
11 realized by the Company in the context of whether
12 they were appropriate to include in the development
13 of the Staff rate plan.

14 Q. And I'm sorry, you identified -- who did
15 you say the witness was?

16 A. Oh, excuse me. I thought it was Dr.
17 Lurito.

18 Q. At the top of the page?

19 A. It's Ms. Linnenbrink, excuse me.

20 Q. Would Ms. Linnenbrink be testifying on
21 behalf of the Staff?

22 A. That's correct.

23 MS. HARRIS: I offer 44.

24 JUDGE SCHAER: Okay.

25 MR. CEDARBAUM: No objection.

00229

1 JUDGE SCHAER: No objection?

2 MR. CEDARBAUM: No objection.

3 JUDGE SCHAER: It is admitted. Did you
4 intend to offer 43?

5 MS. HARRIS: I could offer 43 at this time,
6 Your Honor.

7 JUDGE SCHAER: Well, it's up to you.

8 MS. HARRIS: I'll offer 43 at this time.

9 JUDGE SCHAER: Is there any objection?

10 That document is also admitted.

11 Q. Mr. Elgin, will you please turn to what has
12 been marked as 45?

13 A. Yes, I have that.

14 Q. Mr. Elgin, did you participate in the
15 drafting of this motion of Commission Staff to
16 exclude rebuttal testimony?

17 A. I don't remember. Let me look it over for
18 a second and I can see if it jogs my memory. I
19 believe I had some involvement in this. To what
20 extent and what specifically I did -- but I'm sure I
21 reviewed it before it went out.

22 MS. HARRIS: I offer 45.

23 JUDGE SCHAER: Any objection?

24 MR. CEDARBAUM: I guess I -- it's kind of a
25 long document, although it seems familiar to me.

00230

1 JUDGE SCHAER: It's particularly
2 well-written.

3 MR. CEDARBAUM: It's very convincing. But
4 all kidding aside, again, I'll object on relevance.
5 I mean, I recall the document, I understand the topic
6 of the document, but I'm not sure of its relevance in
7 the context of this case.

8 MS. HARRIS: The relevance of the document,
9 Your Honor, is that Mr. Elgin has testified to
10 different merger testimony and what was presented,
11 what was rejected, and what was moved to strike in
12 different references in his testimony and during his
13 testifying here today.

14 JUDGE SCHAER: Why don't you show us a
15 couple of those references?

16 MS. HARRIS: For instance, this specific
17 document goes to, on page five -- I'm sorry.

18 JUDGE SCHAER: Page five of his testimony
19 or page five of the motion?

20 MS. HARRIS: One moment, Your Honor.

21 JUDGE SCHAER: Thank you.

22 MS. HARRIS: On page five, Your Honor, in
23 the second full paragraph.

24 JUDGE SCHAER: Page five of which document,
25 please?

00231

1 MS. HARRIS: Of 45. It states that Staff
2 accepted the companies' proposal to diverge from
3 traditional ratemaking in favor of a five-year rate
4 plan that would similarly challenge management to
5 achieve expected merger savings and savings
6 associated with best practices and stretch goals.

7 JUDGE SCHAER: And how does that relate to
8 Mr. Elgin's testimony, please?

9 MS. HARRIS: Mr. Elgin has testified the
10 different -- the testimony that was in the merger and
11 what was proposed by the Company in showing power
12 stretch goals.

13 JUDGE SCHAER: I asked you for the
14 reference in Mr. Elgin's testimony to that.

15 MS. HARRIS: He testified here today of Mr.
16 Torgerson.

17 JUDGE SCHAER: I'm not recalling any
18 testimony today by Mr. Elgin about Mr. Torgerson, I'm
19 sorry. Do you recall such testimony, Mr. Elgin?

20 THE WITNESS: I think I referenced Mr.
21 Torgerson in the context of a response to a question,
22 Your Honor, but it had to do with, as I recall, what
23 supported the notion of what is a power stretch goal,
24 what was included, and what was not.

25 JUDGE SCHAER: I'm having trouble finding

00232

1 any relevance to this motion, Ms. Harris. Perhaps if
2 you wanted to try to provide some more foundation.
3 The paragraph you've referred me to in here --

4 MS. HARRIS: Refers to Company testimony,
5 Your Honor, regarding power stretch savings goals.

6 JUDGE SCHAER: Okay. And so --

7 MS. HARRIS: And Staff's motion to strike
8 such testimony.

9 JUDGE SCHAER: Okay. So is there certain
10 testimony that the Company offered in the merger
11 proceeding that you're wishing to put forward today?

12 MS. HARRIS: It's actually Staff's position
13 in this motion that we wish to offer today.

14 MR. CEDARBAUM: Your Honor, I guess that
15 just strengthens my objection on relevance. This
16 document was prepared by me because, in the rebuttal
17 case of the Company in the merger, we received a pile
18 of documents that suggested a number of traditional
19 rate-making, known and measurable type of concepts,
20 as opposed to the Company's direct case, in which a
21 rate plan, a nontraditional kind of scenario was
22 proposed.

23 So we filed a motion to strike because we
24 were basically getting a new case on rebuttal.
25 That's what happened here. My recollection actually

00233

1 is that the motion was denied. So I don't -- that
2 was the point of the motion, and it's a real stretch
3 to me to see how that's relevant to this case.

4 JUDGE SCHAER: My recollection is that --
5 I'm not sure if it was done orally or in writing --
6 that much of this motion was granted and parts of it
7 were not granted. But I do not see any relevance of
8 this document to your description of what Mr.
9 Torgerson said in the merger.

10 If you wanted to bring in -- if you had
11 wanted, in your testimony, to bring in his testimony
12 or parts of his testimony that were stricken, I could
13 see you might be able to build some relevance to
14 that, but to get to a motion written by Mr. Cedarbaum
15 in another case through Mr. Elgin's testimony does
16 not appear to relate to this document to me. It's
17 just too tenuous. So I'm going to exclude the
18 exhibit at this point.

19 Q. Mr. Elgin, in your testimony, you give the
20 option to defer the gain for the treatment of the
21 Colstrip transaction, and you rely on two
22 proceedings, one being the Water Power/Othello
23 proceeding. Could you please turn to what has been
24 marked as Exhibit 46?

25 A. Yes, I have that, but I think that that's a

00234

1 mischaracterization. Your question mischaracterizes
2 my testimony.

3 Q. What is your testimony on that subject?

4 A. Let me find the page here.

5 JUDGE SCHAER: I am going to ask, Ms.
6 Harris, when you ask questions about a witness'
7 testimony, you provide the page and line numbers, so
8 that all of us can follow along, please.

9 THE WITNESS: My testimony on page seven,
10 line 12, Your Honor, is that whether or not the
11 Commission has had similar rate base issues, and if
12 so, how has the Commission ruled on them.

13 And I'm saying that the Colstrip case is
14 similar, but because of Colstrip, I think the
15 Commission has to go a step further. And that gets
16 to the previous discussion I have, beginning on page
17 four, under standard approval, and specifically
18 regarding the prior rate treatment for Colstrip
19 Facilities One, Two, Three and Four, and the
20 Commission including those in the Company's rate base
21 in the first year capital costs.

22 So I'm saying that while these are good for
23 illustrative purposes, the Commission needs to go one
24 step further because of the major impacts that
25 Colstrip's had on consumer rates today.

00235

1 JUDGE SCHAER: Well, you do mention this
2 case in your testimony, do you not, Mr. Elgin?

3 THE WITNESS: Yes, that's correct.

4 JUDGE SCHAER: Where is that reference?

5 THE WITNESS: That's on page eight, line
6 six.

7 JUDGE SCHAER: And what was your question
8 there, Ms. Harris?

9 MS. HARRIS: I just asked if he relied on
10 the Othello decision in his testimony.

11 JUDGE SCHAER: And I think I asked you for
12 the page reference, and now we're there, page eight,
13 line six. Are you saying yes or no to that, Mr.
14 Elgin?

15 THE WITNESS: Yes. I didn't rely on it; I
16 looked at these.

17 Q. Mr. Elgin, could you please refer to
18 exhibit -- what has been marked as Exhibit 46?

19 A. I have that.

20 Q. And do you recognize this -- I realize you
21 haven't had time to look at it, but do you recognize
22 this as the application of Water Power in the Othello
23 transaction?

24 A. I'll accept it, subject to check, that it
25 is a copy of that application.

00236

1 Q. And in your testimony, you stated that the
2 Commission was faced with an issue almost identical
3 to the sale of Colstrip; is that correct?

4 A. That's my testimony.

5 Q. And are you referring to this Othello
6 application?

7 A. Yes.

8 Q. And further in your testimony, on page
9 eight, line seven, you state that the Washington
10 Water Power Company requested approval to sell its
11 Othello combustion turbine facility; is that correct?

12 A. Yes.

13 Q. Further, you state that the Commission
14 rejected the Company's proposed treatment that it
15 would pass the gain on to shareholders; is that
16 correct?

17 A. Yes.

18 Q. Could you please turn to page five of what
19 has been marked Exhibit 46?

20 A. I have that.

21 Q. Do you see, under heading Roman Numeral V,
22 proposed accounting treatment?

23 A. I see that.

24 Q. Could you please review that heading, or
25 review that paragraph?

00237

1 A. Yeah, okay. I've reviewed it.

2 Q. Is it fair to state that, in its proposed
3 accounting treatment, in fact, Water Power gives the
4 Commission a couple of proposals?

5 A. That's correct.

6 Q. And one of those proposals would be to
7 defer the treatment of the gain until the context of
8 Water Power's next general rate filing?

9 A. That's correct.

10 Q. So in fact, the Commission didn't reject
11 the proposed Company's treatment regarding the gain,
12 but just opted to take a different proposal?

13 A. Well, this is the application. I'll refer
14 to the order in terms of what the Commission did, and
15 this is -- I think is consistent with my testimony,
16 is that the order granting the application provided
17 for this treatment, which begins on line 12 and ends
18 on line 18. It says what it says.

19 Q. Would it be fair to state, though, that
20 your testimony admits that Water Power proposed that
21 the Commission could defer the gain to the general
22 rate case?

23 A. Well, it provided in its application an
24 alternative, but I think what my testimony is is that
25 it would not pass -- it would not accept the

00238

1 accounting treatment on page -- that was proposed on
2 page five, but instead said we will defer the gain.
3 I don't know what else -- I mean, I don't understand
4 what you're getting at here.

5 Q. I guess my simple question is did Water
6 Power propose to defer the gain to the general rate
7 case?

8 A. Well, it appears that what this is -- what
9 it says is that this is an alternative for the
10 Commission to do. It says what it says.

11 MS. HARRIS: Okay. Your Honor, I'd offer
12 46.

13 JUDGE SCHAER: Any objections?

14 MR. CEDARBAUM: No.

15 JUDGE SCHAER: It's admitted.

16 Q. Mr. Elgin, if you'll turn to what has been
17 marked as 47. Do you recognize that as your response
18 to PSE Data Request Number Three?

19 A. Yes.

20 Q. And in your response to Data Request Number
21 Three, you reference another Water Power docket, FR
22 86-150?

23 A. That's correct.

24 Q. If you'll turn to Exhibit 48?

25 A. Yes.

00239

1 Q. Upon review of that document, would you
2 recognize that as the application of Water Power in
3 Cause Number FR 86-150?

4 A. Yes.

5 MS. HARRIS: Your Honor, I offer 47 and 48.

6 JUDGE SCHAER: Any objections?

7 MR. CEDARBAUM: I have no objections, but
8 47 is incomplete. The order of the Commission in
9 Docket FR 86-150 was attached to our response and
10 it's not included in the exhibit, so we'd like to
11 supplement.

12 JUDGE SCHAER: So you would like to provide
13 that order as a supplement or would you just like the
14 Commission to take notice of that order?

15 MR. CEDARBAUM: I can provide it. It's
16 usually easier to have it in the record.

17 JUDGE SCHAER: Thank you, Mr. Cedarbaum.
18 Please plan to provide that. Did you also want to
19 provide Mr. Martin's response to Data Request 16,
20 which is referenced in this response, or is that not
21 necessary?

22 MR. CEDARBAUM: I would have to check what
23 that response is.

24 JUDGE SCHAER: If you would like to make
25 this complete, you may do so.

00240

1 Q. Mr. Elgin, could you turn to what has been
2 marked Exhibit 49?

3 A. Yes.

4 Q. Do you recognize this document?

5 A. I'll accept that it's the copy of the
6 application that the Water Power company filed in
7 this docket.

8 Q. I'm sorry. I've moved on to Exhibit 49.

9 A. Oh, I'm sorry.

10 JUDGE SCHAER: That's the transcript pages?

11 MS. HARRIS: Correct.

12 THE WITNESS: Okay. I have that.

13 Q. Do you recognize this as your testimony?

14 A. Well, it's not just my testimony. It's the
15 testimony of myself, Mr. Davis, and Mr. Lazar and Mr.
16 Manifold.

17 Q. And what were you testifying to that day?

18 A. We were responding to questions about the
19 stipulation in the merger case.

20 MS. HARRIS: Your Honor, I offer 49.

21 JUDGE SCHAER: Is this a complete copy of
22 that volume of the transcript?

23 MS. HARRIS: I don't believe so, Your

24 Honor.

25 MR. HARRIS: We have complete copies, Your

00241

1 Honor, if you'd prefer.

2 JUDGE SCHAER: I would like you to put a
3 complete copy into the record, because I think that
4 would be a useful document.

5 MR. HARRIS: We'll provide that, Your
6 Honor.

7 JUDGE SCHAER: We're going to then rename
8 Exhibit 49 as Volume 16 of the transcript from the
9 Puget Power/Washington Natural Gas merger proceeding.

10 Q. Mr. Elgin, I'll refer you to what has been
11 marked Exhibit 50. You've had quite a few questions
12 today regarding the stipulation in the Court of
13 Appeals Docket Number 29404-1-I. Upon review, do you
14 recognize this as a draft stipulation and order of
15 dismissal?

16 A. I'll accept it, subject to check.

17 Q. Have you ever seen this document before?

18 A. Yes.

19 MS. HARRIS: I offer 50.

20 JUDGE SCHAER: Any objections?

21 MR. CEDARBAUM: Maybe just a representation
22 of Counsel. This is what was signed amongst the
23 parties or this was a draft?

24 MS. HARRIS: This is what I understand that
25 was signed by the parties.

00242

1 MR. CEDARBAUM: This was the final, signed
2 version?

3 MS. HARRIS: Yes.

4 MR. CEDARBAUM: I have no objection to it.
5 I just would note for the record, I think there's a
6 page missing. Paragraph two from the stipulation
7 appears to be missing, so maybe you can just
8 supplement it.

9 MR. MANIFOLD: Looks like it may be every
10 other page, because the bottom of paragraph five is
11 not contained, as well.

12 MR. CEDARBAUM: Maybe it's a problem with
13 every other page copied.

14 MS. HARRIS: We'll follow up with a
15 complete copy.

16 MR. MANIFOLD: Could I address this, also?

17 JUDGE SCHAER: Go ahead, Mr. Manifold.

18 MR. MANIFOLD: I'm not sure which parts you
19 intend to use, but the numbers pages are illegible in
20 the copy, and if you don't plan on using those, I
21 don't have a problem with that, if all you want is
22 the first part, but if you intend to use in some way
23 the number pages, I'd like a copy that I can read.

24 MS. HARRIS: No, I don't plan on using the
25 number pages, and unfortunately, my copy's not any

00243

1 better, Rob.

2 JUDGE SCHAER: Should we remove those
3 pages, then? Since we can't read them, let's not
4 have them hanging up here waiting to come back and
5 haunt us some day. I do have a signed copy of the
6 stipulation, but it is not a clean copy. I hang on
7 to certain things. And I would make this available
8 to the parties, if you want to try to block out some
9 of the notes and then make a complete copy from this.
10 It does have the page that's missing from your
11 copies.

12 MS. HARRIS: I have no further questions
13 for Mr. Elgin.

14 JUDGE SCHAER: Do the Commissioners have
15 questions for Mr. Elgin? I'm sorry. You get me
16 confused here and I stay confused. Okay. Mr.
17 Manifold, did you have questions?

18 MR. MANIFOLD: I'm happy to defer to the
19 Commissioners. I had a couple of questions.

20 C R O S S - E X A M I N A T I O N

21 BY MR. MANIFOLD:

22 Q. Mr. Elgin, looking at your KLE-2, which is
23 Exhibit 39?

24 A. Yes.

25 Q. Should there be any changes in this to

00244

1 reflect the Montana property tax law change?

2 A. Well, it could be changed, but the purpose
3 of this exhibit is not to be precise. The purpose of
4 this exhibit is to show that, in the early years of
5 the transaction, there are clear and substantial
6 benefits that are very certain, and those flow to
7 shareholders. So whether you put the property tax
8 adjustment in there or not, the result of this
9 exhibit would stay the same, and that it shows in the
10 out years that ratepayers have significant exposure
11 to higher costs of power. So again, this exhibit
12 wasn't to be intended to be precise in terms of what
13 are the benefits; it's just to show -- make that
14 point.

15 Q. If this were modified with the change in
16 the Montana property tax, which direction would it
17 go? Would it become even more beneficial in the
18 short run?

19 A. Yes.

20 Q. Okay. Am I correct that you've done no
21 present value calculation, so the disagreement
22 between the Company and Public Counsel on what value
23 to use for present value, what discount rate to use
24 for present value does not involve Staff?

25 A. No, it does not, and that's precisely

00245

1 because, in my testimony, I view that the gain on the
2 sale and the cost of these short-term benefits, the
3 Column D, arguably could be considered to be carrying
4 a return at a shareholder rate of return in that one
5 could consider those benefits.

6 So I kept this all in nominal dollars to
7 reflect the possibility that different perspectives
8 had different carrying costs and different discount
9 rates, and that, you know, from a shareholder's
10 perspective, this is a very attractive transaction.

11 Q. Turning to your direct testimony, T-37,
12 page six, line seven --

13 A. Page six, line seven?

14 Q. Yes.

15 A. I have that.

16 Q. I understand you're saying that, in the
17 early years to date, with Colstrip, the cost of power
18 from Colstrip has been above market?

19 A. That would be one way to characterize it,
20 but I mean, market is a moving thing, so -- the point
21 is that, though, first year capital costs and the
22 impact that these facilities had on Puget rates were
23 fairly dramatic.

24 Q. And is it correct that through a series of
25 rate cases, all of the costs of Colstrip were put

00246

1 into rates that were paid by ratepayers?

2 A. That's correct.

3 Q. High initial years costs are an expected
4 aspect of a new plant, balanced by lower costs in
5 later years, due to the capital costs waning?

6 A. Not all facilities, but these facilities,
7 in particular.

8 Q. Okay. At page 14 of your testimony, were
9 you the lead Staff person in negotiating a merger
10 stipulation?

11 A. Yes.

12 Q. Was the sale of generating resources ever
13 discussed, to your knowledge, as an element of power
14 stretch goals?

15 A. In the settlement discussions?

16 Q. Yes.

17 A. No, they were not.

18 Q. Okay. Was there any discussion of the sale
19 of Colstrip?

20 MS. HARRIS: Your Honor, I object to
21 friendly cross.

22 JUDGE SCHAER: On what grounds?

23 MS. HARRIS: On the grounds that it's
24 friendly cross-examination on Mr. Elgin's
25 interpretation of what was in the merger and what was

00247

1 not in the merger.

2 JUDGE SCHAER: Mr. Manifold, the objection
3 is that you're being friendly. What's your response,
4 please?

5 MR. MANIFOLD: Well, I can be more hostile,
6 I guess, but seriously, we have, obviously, a good
7 deal of commonality with Staff. We have a number of
8 differences, as well. So I don't think it's fair to
9 characterize any questions I ask of Staff as being
10 hostile -- or friendly, excuse me.

11 JUDGE SCHAER: I'm not concerned about the
12 questions being friendly. I'm a little bit concerned
13 about the Commission's rule on settlements, and
14 you're getting into settlement discussions. I don't
15 believe that was considered necessarily appropriate.
16 Can you try to tailor your questions to address that
17 concern, please? Go ahead.

18 MR. MANIFOLD: Sure. Was the last question
19 okay?

20 JUDGE SCHAER: Why don't you restate the
21 last question.

22 Q. Okay. Mr. Elgin, in your various roles
23 during the merger proceeding, were you ever apprised
24 by the Company that there was any anticipation of
25 selling Colstrip?

00248

1 A. No, I was not.

2 Q. Looking at your KLE-3 again, which is
3 Exhibit 40.

4 A. Yes.

5 Q. The bottom part, the net power cost
6 forecast, Column F, would -- well, first of all, this
7 is a document from the merger case; right?

8 A. Yes, this was attached to the stipulation,
9 and it's part of the merger that's in another exhibit
10 in this case, too.

11 Q. Right. Would the values in Column F for
12 year 2000 be different if one had anticipated any
13 sales of facilities such as Colstrip?

14 A. Yes, my testimony refers to that. If
15 Colstrip were contemplated, a sale of Colstrip, for
16 example, because fuel would look dramatically
17 different in any one of the out years, particularly
18 2000 and 2001, because Colstrip is 35 to 40 percent
19 of the Company's fuel cost.

20 Q. Who prepared this exhibit?

21 A. This exhibit was prepared by Ms. Lynch for
22 the Company, but I believe that the numbers came from
23 Mr. Story.

24 Q. Okay. Referring, finally, to Exhibit C-43,
25 the confidential one, which was TS-34 in the merger.

00249

1 A. Yes, I have it.

2 Q. Whose document was that? I don't think
3 anybody mentioned that earlier.

4 A. This document was provided by --

5 Q. Excuse me. May I just -- it might assist
6 you in looking at the bottom left-hand corner of it.

7 A. Well, mine just says rating agency
8 presentation. It's my understanding this was
9 provided by the Company in response to a Staff Data
10 Request.

11 MR. MANIFOLD: Okay, thank you.

12 JUDGE SCHAER: Anything further?

13 MR. MANIFOLD: I have no other questions.

14 JUDGE SCHAER: Any questions from the
15 Commissioners?

16 MR. VAN CLEVE: Your Honor, I just have a
17 couple questions.

18 JUDGE SCHAER: Oh, Mr. Van Cleve. I'm
19 sorry. Go ahead.

20 MR. VAN CLEVE: Real quick.

21 C R O S S - E X A M I N A T I O N

22 BY MR. VAN CLEVE:

23 Q. Mr. Elgin, looking at your Exhibit KLE-2,
24 and comparing that to Exhibit C-43, page six, which
25 is the forecast for the power stretch goals.

00250

1 A. Yes.

2 Q. Is it fair to say that the gain that would
3 be realized by the Company during the years 1999,
4 2000, and 2001 together are in excess of the power
5 stretch goals which were forecasted for the rating
6 agencies, assuming if you add Columns C and D
7 together?

8 A. Yes.

9 Q. And are you aware of any other actions that
10 the Company's taken to implement the power stretch
11 goals?

12 A. Yes, there's been several to date.

13 Q. Can you name those?

14 A. The first had to do with the restructuring
15 of a contract with Montana Power, who's the primary
16 operator of the facility. And the second one is
17 exhibit -- the previous confidential exhibits, the
18 one on the pink paper, that had to do with the
19 Tenaska restructuring.

20 JUDGE SCHAER: Exhibit C-31.

21 THE WITNESS: Exhibit C-31. And to date
22 and -- strike that. The Company was unsuccessful to
23 date in its March Point litigation, it's my
24 understanding, and -- let's see. There may be some
25 ongoing benefits from fuel for some of the PURPA

00251

1 contracts, but I'm not sure. I'm just -- I'm
2 guessing now, but I think that there's some others.

3 Q. I asked Mr. Story this morning whether he
4 knew if the Company's revenues from Schedule 48
5 during the rate plan had exceeded the Company's
6 forecasts of what the Schedule 48 revenues would be.

7 A. I recall that question.

8 Q. And he didn't know the answer. Do you know
9 the answer?

10 A. Yes.

11 Q. What is it?

12 A. They far exceed what the Company expected
13 to realize.

14 MR. VAN CLEVE: That's all I have.

15 JUDGE SCHAER: Okay. Anything from the
16 Commissioners?

17 E X A M I N A T I O N

18 BY CHAIRWOMAN SHOWALTER:

19 Q. I just have one question of what you were
20 testifying on Exhibit Number 27.

21 A. Twenty-seven.

22 Q. That's the merger order.

23 A. Oh, okay.

24 Q. And you were testifying about page 22.

25 A. Yes, ma'am.

00252

1 Q. And at one point, you said, As to the first
2 sentence, I agree with Mr. Story. Were you referring
3 to the second to the last sentence of the page there?

4 A. Yes.

5 Q. Okay.

6 A. Yes, that the gains from the transfers of
7 real property that are not a direct result of merger
8 will be deferred, as set forth in the stipulation,
9 and that is for non-depreciable property. In the
10 1985 case, there was a -- if I can give you a little
11 history, there's a significant issue about property
12 held for future use, where the Company buys property
13 in anticipation of growth and whatnot and they hold
14 it, but they don't use it, and they include that in
15 rate base. In subsequent periods, they determine,
16 for whatever reason, that the property's no longer
17 useful, they were transferring out of rate base to a
18 subsidiary and selling it at a gain.

19 So there was -- the Commission ordered
20 studies and ordered the issue to be brought back.
21 And then, ultimately, in terms of the appeal and
22 where this thing went on appeal, there was an
23 agreement for non-depreciable property, and primarily
24 it's property held for future use, that those gains
25 should be deferred. And then, to the extent that

00253

1 there's gains or losses, they're amortized over the
2 period of time that they were in rate base.

3 So if a piece of property, for example, was
4 in Puget's rate base for five years and they gained
5 \$500,000, let's say, then that 500,000 would be
6 amortized over a five-year period, it's my
7 understanding of what this stipulation's about. Real
8 property, non-depreciable.

9 Q. Okay. So does that mean that the second
10 sentence of property transactions that are directly
11 related to the merger is also constrained by
12 non-depreciable property?

13 A. No, no, because Mr. Flaherty identified
14 specific properties that were directly
15 merger-related, and some of those properties could
16 very well be land.

17 Q. Okay. So then, I'm trying to get a sense
18 of the universe here. Transactions that are related
19 to the merger could be property that either was or
20 wasn't or is or isn't depreciable?

21 A. Right.

22 Q. And we know how to treat those from this
23 statement?

24 A. That's correct.

25 Q. If a transaction is not related to the

00254

1 merger and is not non-depreciable?

2 A. Is depreciable.

3 Q. Yes. What is your view about how that is
4 treated?

5 A. Well, I can tell you what at least I
6 understood the parties to the settlement -- if we go
7 to the stipulation.

8 Q. Which is?

9 A. It's attached, page nine. In the merger
10 case, there was an issue regarding some property that
11 was also sold, and that had to do with the parking
12 lot and the OBC land. The Company sold that property
13 and did not file an application for transfer of
14 property. So the first thing we did is we carved
15 that out and said, You will file that application,
16 and the parties agreed to that.

17 The second thing in the rate plan that we
18 contemplated was that there were properties that Mr.
19 Flaherty identified and they were specifically
20 related to the merger. For example, in Olympia,
21 Washington Natural Gas had an office on Martin Way,
22 and that property, that facility would be closed and
23 the property would be sold. That transaction and the
24 benefit from that sale were part and parcel of Mr.
25 Flaherty's identified \$370 million savings. We said

00255

1 those, you can keep. Anything that's strictly
2 related to the merger, consolidations, you know,
3 selling a warehouse and consolidating, selling other
4 property that, you know, for whatever reason, because
5 you are merged, one of the other pieces of property
6 was the headquarters of Washington Energy Company on
7 Mercer Street, you know, the old blue flame building,
8 that was part. So we said, yes, that's merger
9 savings.

10 Anything else needs to be carved out and
11 deferred, but particularly Colstrip, because it's so
12 big and it had such a big impact on rates up to now,
13 there is no way that Staff would have said, You can
14 sell Colstrip and have that flow to your bottom line,
15 those benefits. It's just too big.

16 Q. I guess I'm asking, though, for you to
17 refer to these documents and show me, of these
18 different categories, related to the merger or not,
19 real or not, depreciable or not, where do these
20 different provisions apply?

21 A. Okay, here it is. On line 13, for property
22 transactions during the rate plan period that are as
23 a direct result of the merger, associated gains or
24 losses shall be included in PSE's current earnings,
25 rather than deferred.

00256

1 Q. That's what they are.

2 A. They are. And such transactions shall be
3 reported to the Commission and Public Counsel before
4 they're formally recorded, and we have the right to
5 object, whereupon the rate management treatment of
6 the transaction being classified as being directly
7 related to the merger will be subject to examination
8 in a subsequent PSE general rate proceeding.

9 So I guess what we're trying to say is we
10 tried to define specifically the transactions that we
11 knew would occur. We know that there's going to be
12 sales of property merger-related.

13 Q. Yes.

14 A. And we know that there's going to be sales
15 of property continued to be under the stipulation,
16 and we know there's this issue with the parking lot,
17 and anything else you have to come and ask for
18 treatment. You can't just flow to your bottom line.
19 That's what page nine, subparagraph D stands for. We
20 tried to be specific in terms of what it is we were
21 identifying and what could go to the Company's
22 earnings. That's the best that I can explain it. We
23 tried to be very explicit.

24 And then I guess when I looked at what --
25 when the Commission accepted the stipulation, and

00257

1 then I go to the language that we previously
2 discussed on page 22, this is the way that I
3 interpreted what the Commission did. This statement,
4 this last sentence says that if it's not directly
5 merger-related, you can flow it to your bottom line
6 rather than deferring it, deferring any gain or loss.

7 Q. If it's not merger-related?

8 A. Gains that are direct -- yeah, if it's not
9 directly related to the merger. If it's not the
10 stuff that's identified in Mr. Flaherty's \$370
11 million savings.

12 MR. CEDARBAUM: I think you're misspeaking.

13 Q. You just said twice if it's not
14 merger-related. You mean if it is merger-related?

15 A. Oh, it is merger -- excuse me, if it is
16 merger-related, yes.

17 Q. Okay. If it is merger-related. But if
18 it's not merger related, then --

19 A. Defer.

20 Q. Because?

21 A. Because it has impact on earnings, and
22 particularly Colstrip, because this was the issue
23 that Mr. Story was talking about this morning. This
24 whole issue --

25 Q. But because in terms of what are in these

00258

1 documents or because of longstanding principles or
2 opinion?

3 A. No, because of the rate plan, what we were
4 trying to accomplish. We were trying to say, Here
5 are power stretch savings, best practices, synergy
6 savings. The Company can manage those and keep
7 those, and there are these kinds of things. But in
8 my mind, selling Colstrip, which is a piece of
9 property that's been on their books for a substantial
10 period of time, and sell it for above book value and
11 flow that gain to their bottom line, that's not a
12 power stretch saving.

13 Q. I think the premise of my question was
14 assume it's not related to the merger. Assume the
15 transaction is not related to the merger, then do
16 these documents direct or constrain how a
17 non-merger-related transfer is treated, and why?

18 A. Yes, because the stipulation, what we
19 agreed to, defined what could be flowed to the bottom
20 line.

21 Q. And then, by implication, if it's not in
22 that list, then what?

23 A. Then it's deferred.

24 Q. Because of the language in the rest of the
25 stipulation?

00259

1 A. Let me go back to the stipulation. Yes,
2 because of the stipulation, because of the bounds
3 that we put on the nature of property transactions
4 during the merger and what would be the treatment.
5 By what we said, we specifically -- we said, This is
6 merger-related bottom line, but for there's an
7 opportunity for Staff and Public Counsel to object.
8 Property held for future use, stipulation, continued
9 treatment, that you file for the parking lot and the
10 OBC sale land, you file an application. Everything
11 else is deferred.

12 Q. And because -- where in the stipulation is
13 it saying that everything else is deferred?

14 A. It doesn't explicitly say that. I think --
15 is that your question?

16 Q. I think it may be that's an ultimate
17 question, but I was trying to find out the answer to
18 that question.

19 A. Right. We did not, in this document,
20 specifically say what should be deferred. What we
21 did is provide the specific treatment for the
22 property and the transactions that we knew would
23 occur.

24 CHAIRWOMAN SHOWALTER: Thanks.

25 E X A M I N A T I O N

00260

1 BY JUDGE SCHAER:

2 Q. Okay. Mr. Elgin, staying with that topic
3 for a minute, when I look at the order on page 22, it
4 appears to me that those last two sentences, and
5 actually, the section of the order, is simply the
6 Commission's statement of what its understanding is
7 of what's included in the stipulation. Is that your
8 understanding, as well?

9 A. Yes.

10 Q. And looking at the stipulation again on
11 page nine, I read the first sentence, and it notes
12 that current amortization levels and current policy
13 authorizing deferral of gains shall continue through
14 the rate plan period subject to the exceptions set
15 forth below for property disposed of as a direct
16 result of the merger. Do you see that sentence?

17 A. Yes.

18 Q. So would you see that sentence as setting
19 the general policy and then the allowance later in
20 this paragraph for Puget to take the gains from
21 certain sales that are merger-related to be an
22 exception to the general rules set out in the first
23 statement?

24 A. Yes. I think that's what I was trying to
25 say, is that.

00261

1 Q. Then looking at this, this paragraph is
2 headed Gains and Transfers of Real Property; is that
3 correct?

4 A. Yes.

5 Q. And is part of what exists at Colstrip real
6 property?

7 A. Yes.

8 Q. And is that real property part of this
9 transaction?

10 A. Yes.

11 Q. And then, looking at the depreciable assets
12 at Colstrip; is that directly addressed here?

13 A. No, no, it's not.

14 Q. You have cited in your testimony two other
15 instances -- first of all, in the Puget sales
16 adjustments that you discussed previously with the
17 Chairwoman, was Puget taking the parcels that had
18 been in rate base and were determined -- called used
19 and useful, and then declaring them not to be used
20 and useful before it sold them?

21 A. Yes.

22 Q. Is the Colstrip plant still used and
23 useful?

24 A. Yes, I testified to that. It's still in
25 the rate base and still used.

00262

1 Q. So this is, to some extent, a different
2 kind of case, would you think, because they're
3 talking about sale of an asset that is currently used
4 and useful?

5 A. Yes.

6 Q. Have you presented the information that you
7 were familiar with from past utility company sales,
8 energy company sales, of assets which are used and
9 useful?

10 A. Yes, but I guess that's what I was trying
11 to get at, Your Honor, is that the Commission has
12 never dealt with the sale of a major generation
13 asset, I mean, of Colstrip, and I think that this is
14 -- although the Commission has treated them before,
15 that it's instructive, but I think, because of
16 Colstrip and the unique characteristics of Colstrip,
17 I think you have to go one step further. Look what's
18 happened in the past, but really set out new ground,
19 and the standard should be not only not in the public
20 interest, but because of the rate impacts of
21 Colstrip, there has to be an affirmative showing that
22 consumer rates will be lower and there's explicit
23 benefits from the transactions for ratepayers.

24 Q. So you're saying that this exception to the
25 general rule that would allow merger-related property

00263

1 sales to flow to the bottom line just doesn't relate
2 to a sale of Colstrip?

3 A. That's my testimony.

4 Q. Okay. In looking a at your testimony, is
5 it your overall recommendation to the Commission that
6 Puget should keep Colstrip?

7 A. If it means that -- if it's an unseverable
8 package, if acceptable regulatory treatment means
9 that they have to have this accounting and have these
10 short-term benefits flow to their income statement
11 immediately, I think, in the long run, they're better
12 off keeping it.

13 But I think to the extent that this Company
14 is faced with stranded costs and that if we -- if
15 they sell it and defer all the benefits and the gains
16 and we use it as an offset for some future stranded
17 cost liability, I would say that we can probably,
18 given the other qualitative factors that Mr. Gaines
19 discussed, I think Colstrip probably should be sold,
20 for the reasons that he's described in his testimony.

21 Q. So looking at the two orders that Puget has
22 requested, you would say that, in your opinion, the
23 Commission should grant the first order, which would
24 authorize the sale of Colstrip and its transmission
25 facilities, and then should not grant the second

00264

1 order, seeking five-year amortization beginning now,
2 but should, instead, defer till the next general rate
3 case any treatment of gains of the sale?

4 A. Well, it's not just the gains; it's also
5 the short -- because of the rate plan, defer the
6 short-term power supply benefits, because embedded in
7 rates are Colstrip costs, and I think that those need
8 to be removed from -- that those costs need to be
9 removed from PSE's rates.

10 Q. Have you looked at Commission orders in
11 other utilities besides energy and treatment of
12 assets, sale of used and useful assets?

13 A. Not in preparing this testimony directly.

14 Q. Are you familiar with the Commission's
15 declaratory order that required US West to bring its
16 proposed sale of its one share ownership in Bellcore
17 before the Commission in a property transfer
18 application?

19 A. I'm aware of their requirement, but the
20 specifics of the transaction, I'm unaware of, Your
21 Honor.

22 Q. Are you aware that the Commission deferred
23 treatment of any gain from that sale to US West's
24 next general rate case?

25 A. I'm not aware of that.

00265

1 Q. All right. Or of the testimony of Mr. Shaw
2 in that case that would support US West that that
3 property had been in rate base, then he would agree
4 that all the gain should go to ratepayers, but since
5 it had not been in rate base, he disagreed?

6 A. Right. I think that that is the general
7 proposition that what I'm suggesting that those prior
8 orders in energy stood for, is that if facilities are
9 in rate base and they're used and useful, that
10 somehow ratepayers have this ongoing risk of
11 ownership. And as I've testified, providing
12 shareholders a fair rate of return on and of the
13 investment is the benefit. And then, to the extent
14 that that moves out and there is a gain, I believe
15 that gain belongs to ratepayers. And as a general
16 proposition, I would agree with that.

17 JUDGE SCHAER: Is there any redirect for
18 Mr. Elgin?

19 MR. CEDARBAUM: Yes. From a scheduling
20 point of view, I didn't know if we were coming back
21 tomorrow or not.

22 JUDGE SCHAER: Well, if there is redirect,
23 let's go off the record for a moment and discuss how
24 we want to proceed. We're off the record.

25 (Discussion off the record.)

00266

1 JUDGE SCHAER: Back on the record. While
2 we were off the record, we decided we'd try to finish
3 Mr. Elgin today, and we'll start with Mr. Lazar in
4 the morning.

5 Also during that time, four exhibits were
6 distributed by Mr. Cedarbaum on behalf of his
7 redirect. We're going to mark for identification as
8 Exhibit 52 the response to PSE Data Request Number
9 Eight. I'm going to mark for identification as
10 Exhibit 53 the response to Record Requisition Number
11 45 in Docket Number UE-960195.

12 MR. CEDARBAUM: Your Honor, before you
13 continue, Exhibit 53, at least the attachment, came
14 from the merger and was provided in that docket
15 confidentially, so I don't know if it still is
16 confidential. I can go either way on that. It's up
17 to the Company on that one.

18 JUDGE SCHAER: Why don't you look that
19 over, Mr. Harris, and when we are on the record, let
20 me know how you would like that treated.

21 Marking for identification as Number 54 --
22 how does Number 54 differ from Number 52, Mr.
23 Cedarbaum?

24 MR. CEDARBAUM: Fifty-two is our original
25 response, and 54 is a supplement to that response.

00267

1 JUDGE SCHAER: Okay. This is the
2 supplemental response to PSE Data Request Number 8,
3 and Exhibit 55 is -- is this confidential?

4 MR. CEDARBAUM: I don't consider it to be,
5 but there might be argument from the Company that it
6 is.

7 JUDGE SCHAER: Exhibit 55, for
8 identification, says at the top, Residential Exchange
9 Rate, and I'm going to ask you again, Mr. or Ms.
10 Harris, to let me know if the Company would like this
11 to have confidential treatment.

12 MS. HARRIS: Your Honor, the Company would
13 like this to remain confidential.

14 JUDGE SCHAER: Okay. So this is going to
15 be C-55, and I'm going to ask you guys to get
16 together and do different color photocopying and all
17 that good stuff. How about Number 53?

18 MR. MANIFOLD: Excuse me, Your Honor, could
19 I be heard on Exhibit 55? It appears that the first
20 page had been marked confidential, the second page
21 not. In interest of keeping as little confidential
22 as possible --

23 MR. CEDARBAUM: Let me explain, just in
24 fairness to the Company and so the record's clear,
25 the first page of Exhibit 55 is a document that was

00268

1 used by Staff, Public Counsel and Washington Natural
2 Gas and Puget Sound Power and Light in coming up with
3 the stipulation. So it was stamped confidential
4 while we were looking at it. And again, if the
5 Company wants to make an argument that it's
6 confidential, but it's also privileged, we can deal
7 with that.

8 The second page of the exhibit is
9 confidential to the extent that the first page might
10 be confidential, because some of the numbers on page
11 two come from page one. So I should say for the
12 record that my understanding is that all of the
13 numbers on both pages are publicly available. The
14 confidentiality of it is not -- I don't think so much
15 in terms of that, but how this document was
16 originally used by the parties in the merger.

17 JUDGE SCHAER: Is that true, that that
18 information is publicly-available?

19 MS. HARRIS: I guess the question is to the
20 extent this was used in the settlement proceedings.

21 JUDGE SCHAER: Let's deal with that when he
22 offers it, but right now, let's just find out if it's
23 confidential.

24 MS. HARRIS: I do not know, by just looking
25 at the document, whether they're publicly-available.

00269

1 I can check on that.

2 JUDGE SCHAER: Yeah, would you find out
3 whether those numbers are publicly available? Okay.
4 Go ahead with your redirect, Mr. Cedarbaum, please.

5 R E D I R E C T E X A M I N A T I O N
6 BY MR. CEDARBAUM:

7 Q. Mr. Elgin, before we get to the exhibits,
8 let's cover a couple of topics. The first one, in
9 your deposition -- and for the record, page five this
10 happens -- and also this morning, you talked about
11 Colstrip being in the Company's rate base?

12 A. Yes.

13 Q. Can you provide -- and I think in your
14 testimony, you also discuss the prior rate cases, in
15 which Colstrip One and Two and Colstrip Three and
16 Four were included in the Company's rates and a
17 couple of prior general rate cases. Do you recall
18 that?

19 A. Yes.

20 Q. Can you provide some more detail with
21 respect to the inclusion in rates of Colstrip One and
22 Two, the docket number, the amounts, stuff like that?

23 A. Turning to page five, line 17, I reference
24 U-7601. And in that case, Puget Sound Power and
25 Light filed for a 25 percent increase in its general

00270

1 rates, and the driver for that was exclusively
2 Colstrip One and Two.

3 And as a result of that case, the
4 Commission did authorize a 19 percent increase in
5 general rates, so that's the kind of impact that I'm
6 talking about in my testimony that these specific
7 facilities had on consumer rates when they first
8 went into effect. And shareholders were provided a
9 fair rate of return on and of these facilities since
10 then, and I think that that is sufficient with
11 respect to the benefits that should flow to
12 shareholders.

13 And it corroborates my testimony that these
14 kinds of facilities, particularly Colstrip One and
15 Two, have had a dramatic impact on consumer rates,
16 and therefore, all the benefits and the gains from
17 the sale should flow to ratepayers.

18 Q. Okay. Can you be a little more specific as
19 to how this ties in with your testimony about early
20 year capital costs?

21 A. Well, it's because when a company builds a
22 large central station, it takes a significant amount
23 of time and there's capitalized costs and they're
24 just very expensive. And when they go into rates,
25 the incremental costs of these new resources are

00271

1 significantly above the embedded costs of existing
2 resources.

3 So you know, as I said, the Company filed
4 and requested a 25 percent increase in rates in that
5 docket, and the Commission ultimately approved a 19
6 percent, and it was exclusively caused by the first
7 year capital costs and O&M costs of Colstrip One and
8 Two going into the Company's rate base.

9 Q. Switching to a different topic, at page 13
10 of your deposition, which is in Exhibit 51, there's
11 some discussion about open access. Do you recall
12 that?

13 A. Yes.

14 Q. Can you clarify in your mind what open
15 access is in that testimony?

16 A. Well, open access, as I use that term,
17 could be a range of scenarios to where it's fully
18 unbundled distribution and transmission services or
19 to where open access is in the context of we regulate
20 Puget as a distribution company and we look at
21 purchased power as a -- like we look at their gas
22 operations as purchased gas expense. So it's
23 unclear, but the idea is to move to a scenario where
24 customers have choice about their energy suppliers.

25 Q. You were also asked some questions in your

00272

1 deposition, at page 29, and there was discussion
2 today from other witnesses about stranded costs. Is
3 it your opinion that the issue of stranded cost only
4 arises in the context of open access?

5 A. No, it does not. I mean, the Company, you
6 know, in this deposition was asking, Well, by
7 definition, if you fully unbundle, you have an issue
8 of stranded cost, but that doesn't necessarily mean
9 that you can't have an issue related to stranded cost
10 even though there isn't full open access.

11 Q. And you believe there are issues of
12 stranded cost in this proceeding?

13 A. That's correct. And that's because
14 Colstrip is the only significant generating asset
15 that the Company has on its books. And as I
16 testified, I am very concerned about this scenario
17 where the Company liquidates its generation and takes
18 the profits for the benefit of shareholders during
19 the rate plan and then, later on, if we get to an
20 environment where we have open access, the stranded
21 cost issues are related exclusively to the Company's
22 PURPA resources.

23 So my testimony is that if there is
24 stranded cost, we need to look at it on the whole
25 picture, the entire resource portfolio of the

00273

1 Company.

2 Q. Switching to a different topic, there's
3 been discussion throughout today and with you, also,
4 about what a power stretch saving was and what it is
5 and what it isn't. Were you asked some data requests
6 by the Company to provide documentation for your
7 position that Colstrip is not a power stretch saving?

8 A. Yes, in preparation of my testimony, I did
9 a thorough review of the merger record to try to find
10 something that was related to Colstrip and something
11 that was related to where one could say that Colstrip
12 was part of the Company's power stretch savings, and
13 my review of the record and everything that I could
14 find, as I testified earlier, was that power stretch
15 savings were primarily related to the big ticket
16 items, which were the PURPA resources of the company,
17 as well as some more minor, in terms of magnitude of
18 dollars stretch savings, and that's the Montana Power
19 litigation that Mr. Gaines referred to, and some
20 other minor things related to generation.

21 But the big thing, the thing that drove the
22 numbers, were those PURPA resources in the -- that
23 the Company entered into in the late '80s and early
24 '90s.

25 Q. Referring you to Exhibit 52 for

00274

1 identification.

2 A. I do not have a copy.

3 Q. Referring you to Exhibit 52 for
4 identification, do you recognize this document as
5 your response to the Company's Data Request Number 8?

6 A. Yes.

7 Q. And can you just briefly describe what this
8 document is?

9 A. The Company asked me to describe the
10 documents that support my contention that the
11 analysis of merger benefits and increased costs
12 recognized by the stipulation did not contemplate the
13 sale of Colstrip. And I, in an effort to be
14 responsive in a quick turnaround time, I provided
15 this response.

16 Q. Looking at the second page of the exhibit,
17 the last paragraph, there's reference to Record
18 Requisition Number 45 from the merger proceeding. Do
19 you see that?

20 A. Yes.

21 Q. And is that record requisition response
22 what's been marked for identification as Exhibit 43?

23 A. Fifty-three.

24 Q. Excuse me, 53?

25 A. Yes, it is.

00275

1 Q. And am I correct that in Exhibit 53 --
2 where on Exhibit 53 is Colstrip included?

3 A. It begins -- first off, if you see, up in
4 the upper left-hand corner, this represents Study
5 Number 9504, which is my Exhibit KLE-3, which is the
6 stipulation, the power costs. So that's the
7 connection. And you will see right at the very front
8 of the exhibit, you see Colstrip's and the various
9 accounts for One and Two and Three and Four.

10 And then, if you look on the second page,
11 you'll see the wheeling charges from Colstrip. And
12 then, on the next page, you'll see the fuel costs for
13 Colstrip. And let's see. You'll see on the next
14 page the O&M for Colstrip. And the next page,
15 there's references to Colstrip. And on the final
16 page, there's references to Colstrip.

17 Q. Okay.

18 A. Although several of those numbers are zero.
19 But basically, this document supports the idea that
20 in the Company's power cost forecast for the
21 stipulation, Colstrip was included and was expected
22 to be part of their cost of operation and were part
23 of the element of, quote, power cost pressures.

24 Q. And again, Exhibit 53 is the power cost
25 forecast that was included in Exhibit D to the

00276

1 stipulation?

2 A. That's correct.

3 Q. Looking at Exhibit 54 for identification,
4 can you identify this as your supplemental response
5 to Exhibit 52?

6 A. Yes. After we got the initial response
7 out, I had the opportunity to go back and pull out
8 the documents that specifically related to the
9 testimony and provide copies to the Company regarding
10 the same question.

11 MR. CEDARBAUM: I would offer Exhibits 52,
12 53 and 54.

13 JUDGE SCHAER: Any objections?

14 MS. HARRIS: No objection.

15 JUDGE SCHAER: Those documents are
16 admitted. And let's talk for a moment about 53 and
17 confidentiality, please. Did you want that to be
18 treated as confidential information, Ms. Harris?

19 MS. HARRIS: By first glance, if it was
20 confidential, I would like it to remain confidential.

21 JUDGE SCHAER: So we'll change that to
22 C-53, and I'm going to ask you to work with Mr.
23 Cedarbaum to see that copies of that are properly
24 labeled and put in envelopes and handled in the
25 Records Center so that we don't accidentally let out

00277

1 any of the confidential materials. Go ahead, please,
2 Mr. Cedarbaum.

3 MR. CEDARBAUM: Thank you.

4 Q. Mr. Elgin, Exhibit 49 that you discussed
5 with Ms. Harris this afternoon is the transcript in
6 the merger proceeding when you testified, along with
7 Mr. Davis, Mr. Lazar, and Mr. Manifold, in support of
8 the stipulation?

9 A. Yes.

10 Q. Can you just generally describe the
11 elements of the stipulation. There's some discussion
12 in here about BPA exchange issues. Can you just
13 briefly describe what the rate plan was designed to
14 consider?

15 A. Yes. The rate plan went one step further
16 than the rate plans that were presented by the
17 Company, Staff, and Public Counsel in the merger,
18 although Public Counsel did present a rate plan that
19 included the impacts of residential exchange
20 benefits.

21 And when we went into the discussions, what
22 we tried to do was look at two sources of cost
23 pressures that were facing Puget. And we knew at
24 that time that Bonneville was making overtures to do
25 what it could to reduce the benefits that were

00278

1 flowing to IOUs as part of the exchange. And we
2 anticipated, at least in the merger, that there could
3 very well be a loss of residential exchange benefits
4 at the end of the rate plan period of 2001.

5 And so what we didn't want to do is have
6 ratepayers stuck with a dramatic increase, depending
7 on whatever Bonneville might do with the exchange.
8 And so the rate plan basically looked at what was
9 going to happen to residential rates and rates as a
10 result of losing benefits, and so providing some
11 increases in cost to eventually roll that in and roll
12 the loss of benefits in to rates and then looking at
13 another set of costs, and that had to do with power
14 cost increases, direct savings and synergy savings
15 from the merger, best practices, and power stretch
16 savings.

17 And so the whole idea behind the rate plan
18 was to provide an orderly transition to Puget's
19 rates, and particularly the residential rates, so
20 that when the expected loss of exchange benefits were
21 to occur at the end of the rate plan period, we would
22 have rolled in significant amounts of increases to
23 offset that. Then, on the other side is that the
24 Company had a five-year window to manage its cost, to
25 capture power stretch savings, capture best

00279

1 practices, and implement the merger so that it could
2 offset and manage all the cost pressures within a
3 five-year period. And then, at the end of the
4 five-year period, PSE would be on strong financial
5 footing. And that was the genesis of the rate plan
6 and how those two packages fit together, to recognize
7 those diverse impacts.

8 Now, the complicating thing and the
9 competing issue became out of Bonneville's need to
10 have recognized cost support for flowing benefits
11 from the residential exchange. So then the other
12 thing we had to do was say, okay, what was the
13 underlying analysis with respect to Puget's electric
14 costs so that Bonneville would have the cost support
15 that it would need to continue to calculate average
16 system costs under its 1984 record of decision for
17 determining PSE's average system cost.

18 So in a way, it was looking at those two
19 areas where PSE rates were facing upward pressure,
20 one from the cost side and the benefit side, letting
21 PSE manage that in the merger, and the other thing
22 was the loss of the exchange in providing some
23 gradual increases so that at the end of the rate plan
24 period, we could have fixed the exchange problem and
25 what we anticipated in terms of loss of exchange

00280

1 benefits and that Puget would be again on solid
2 financial footing.

3 Q. Okay.

4 A. That's finished.

5 Q. Referring you to Exhibit C-55 for
6 identification, page one. Can you identify what this
7 document is? It might be at the very end.

8 A. Very end. Yes, I have that.

9 Q. Can you hold it up, so I make sure?

10 A. Yeah.

11 Q. Okay.

12 A. I got it. It's the last two pages of the
13 packet of materials, yes. This document is the final
14 spreadsheet that provided the parties with what were
15 the programmed increases in terms of stability to
16 then offset the potential loss of exchange benefits
17 over the rate plan period. So you see at the top
18 what we have is, '97 through 2001, the expected
19 residential load. Go down to -- then the next column
20 is merely the load multiplied by the benefit that was
21 the Schedule 94 exchange benefit that was in effect
22 at the time, and then go down, skip a line and go to
23 the one and a half percent years, '97 through 2001.
24 These are the program increases that PSE would get
25 under the rate plan. And then you can see the

00281

1 objective was to try to provide PSE with enough rate
2 increases so that, over a period of time, the loss of
3 exchange benefits would be offset by the programmed
4 increases.

5 CHAIRWOMAN SHOWALTER: What do you mean by
6 programmed increases? I see the line, but what do
7 you mean?

8 THE WITNESS: The rate plan, the rate plan,
9 the one percent and the one and a half percent
10 increases that happen each year.

11 Now, these other columns were estimates of
12 what we anticipated the REA to be. It begins, says
13 estimated REA starts with \$50.7 million and declines
14 over time. You can see that we anticipated that the
15 residential exchange benefit would, for all intents
16 and purposes, go away. The next line is the piece
17 that PSE expected from its PRAM Four true-up, and
18 then next piece was a piece related to tax treatment
19 of an IRS ruling, favorable ruling from the IRS for
20 conservation.

21 And I guess the end result is that you see
22 the very -- in the total column, the very last line,
23 the rate plan basically was intended to put PSE at
24 risk over this period, considering all these factors
25 of about 17 and a half million dollars. And so as I

00282

1 testified before, this was the piece that was dealing
2 with the rate pressure for Puget on their exchange,
3 and how the rate increases were designed to help roll
4 that into rates.

5 Q. And page one was circulated among Staff,
6 Public Counsel and, at that time, Washington Natural
7 and Puget Sound Power and Light?

8 A. That's correct.

9 Q. Referring you, Mr. Elgin, to page two of
10 the Exhibit, C-55, can you describe what that is?

11 A. Yeah, C-55 is just a reconciliation from
12 what the rate -- what we expected, because in the
13 rate plan, we were guessing as to what might happen
14 and what might be the benefits, and then C-55 was
15 prepared by Staff to show --

16 CHAIRWOMAN SHOWALTER: You mean page two?

17 THE WITNESS: Page two of C-55 was prepared
18 to show what was actually happening as a result of
19 the rate plan and the impact in residential exchange
20 benefits.

21 Q. Prepared when? This is a current document?

22 A. This is a current document. This was just
23 prepared in the last week. And you can see that,
24 comparing the figures, we were pretty close on what
25 the estimated impact was, the amount that was given

00283

1 to customers, but you can see that the exchange
2 benefits were more than was expected and that the
3 rate increase from customers, as they're programmed,
4 where we anticipated Puget to be at about risk of 17
5 and a half million dollars, what's actually going to
6 happen is at the end of the rate plan period, the
7 total cumulative is Puget's about 800,000 to the
8 good.

9 So this exhibit demonstrates to me that the
10 rate plan accomplished that element of the objective
11 and that was to provide programmed increases to
12 eventually roll into permanent rates the loss of
13 exchange benefits.

14 Q. And just finally, is it your understanding
15 that the numbers, both pages -- let me ask you. Are
16 the numbers on both pages of Exhibit C-55 publicly
17 available?

18 A. Well, the numbers on the second page are,
19 because you can calculate them just by getting loads.
20 I don't know where the public might get the estimated
21 residential loads, but the public could make some
22 guess about this, about what those loads are. The
23 residential exchange, actual amount from BPA is
24 known. That's a publicly-available document, the
25 second line. And then the third line is, again, if

00284

1 you have -- whatever number you use for the first
2 column, you apply that to the increase, and you can
3 get the third column. And so, in a sense, it's
4 pretty much calculable from publicly-available
5 information.

6 MR. CEDARBAUM: Thank you. I would offer
7 Exhibit C-55.

8 MS. HARRIS: Your Honor, I'll object, as we
9 did earlier, that the first page, as stated by Mr.
10 Cedarbaum, was distributed during settlement
11 negotiations to the stipulation. To the extent this
12 document was contemplated by the parties during
13 negotiations, I believe it's privileged.

14 MR. CEDARBAUM: Can I respond, Your Honor?

15 JUDGE SCHAER: I want to deal with this in
16 two pieces. First of all, does everyone agree that
17 this should be confidential if it does go in? I told
18 you we'd take that up when it's offered.

19 MS. HARRIS: I believe both pages should be
20 confidential, to the extent that you cannot get the
21 residential load by publicly-available information.

22 JUDGE SCHAER: Would you go ahead and
23 respond to the settlement discussion?

24 MR. CEDARBAUM: I would agree with the
25 objection prior to this case, but in this case, I

00285

1 believe the Company has waived any objection to
2 privilege on Exhibit C-55 in a number of instances.
3 Most of the witnesses in this case have testified
4 with respect to the rate plan, what that rate plan
5 intended to do, what it intended not to do. Mr.
6 Elgin has done so today without any objection by the
7 Company, his deposition was offered into evidence and
8 had discussions of that without any objection by the
9 Company.

10 So at least with respect to Staff
11 testimony, a lot of evidence has gone in on this
12 point without objection by the Company. But most
13 importantly, Mr. Gaines' rebuttal testimony
14 discusses, in a number of places, what he believes
15 the principles of the rate plan to be. Specifically,
16 I would point you to page two of his rebuttal
17 testimony, line nine. He discusses what he thinks is
18 the fundamental principle. Page eight, line six, he
19 also talks about what he believes the principles of
20 the rate plan were. He also discusses specifically
21 the BPA exchange, what he believed to be a \$108
22 million figure as to benefits that, basically, the
23 Company would have to recoup itself.

24 So the issue of what the rate plan was
25 designed to do, the principles underlying it, have

00286

1 been discussed on this record extensively. I think
2 once that was done, we should be allowed to go into
3 what the rate plan really was intended to do from
4 settlement discussions, and if the document was
5 prepared and circulated amongst the parties which
6 shows exactly that, that's fair game.

7 JUDGE SCHAER: Mr. Manifold.

8 MR. MANIFOLD: Yes, very briefly. It seems
9 -- I would argue for admission of the document. And
10 it seems to me the reason that settlement discussions
11 are confidential is so that people can honestly and
12 fairly enter into settlement discussions without
13 concern that anything they say in those will then be
14 used against them in that case should settlement not
15 be successful. If that's the principle, a settlement
16 was successful, and this isn't that case.

17 So those reasons for keeping settlement
18 discussions off the record I think apply to that case
19 or something so directly related to it that it's
20 still within the ambit of still exposing each other
21 to things that you wouldn't have said but for a
22 confidentiality. It seems to me this document at
23 this time in this case, in addition to the reasons
24 Mr. Cedarbaum has cited, doesn't fall within that
25 principle of why you want to keep settlement

00287

1 negotiations confidential.

2 JUDGE SCHAER: Ms. Harris.

3 MS. HARRIS: First, Your Honor, I take
4 exception to Mr. Cedarbaum's representation. Mr.
5 Gaines' testimony goes to the principles of the rate
6 plan. Mr. Gaines was not involved in the merger, he
7 stated that on the stand. He was not involved in any
8 sort of settlement negotiations in the merger
9 proceeding. His testimony only addresses the rate
10 plan as it appears in the merger order.

11 Earlier in questioning, Mr. Manifold was
12 cautioned not to delve into settlement discussions
13 between the parties, and the Company has been very
14 careful to only take those actions to address the
15 merger during publicly-available testimony, hearing
16 transcripts, motions and this sort. We have never
17 delved into the settlement negotiations between the
18 parties.

19 JUDGE SCHAER: What about this document do
20 you think reflects negotiations, Ms. Harris?

21 MS. HARRIS: It was used between the
22 parties. I don't know who exactly produced this
23 document or how it was used during the settlement
24 negotiations or what it was used --

25 JUDGE SCHAER: Would you like to voir dire

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1 the witness on that?

2 MS. HARRIS: Excuse me?

3 JUDGE SCHAER: Would you like to voir dire
4 the witness on that? It was my understanding that
5 this was the outcome of negotiations, rather than a
6 position during them. And so would you like to find
7 out whether this was a position or how this document
8 arose by questioning Mr. Elgin?

9 VOIR DIRE EXAMINATION

10 BY MS. HARRIS:

11 Q. Is this a document that you created?

12 A. No.

13 Q. Do you know who created this document?

14 A. Yes, the Company.

15 MS. HARRIS: The Company has not waived its
16 privilege as far as this document.

17 MR. CEDARBAUM: Your Honor, I guess --

18 JUDGE SCHAER: I'm ready to rule, Mr.
19 Cedarbaum. I have heard testimony that was not
20 objected to about just about every line of this
21 exhibit, which is one reason I think our record will
22 be more complete if it goes in. I've also not heard
23 that this was a position taken by one party, but
24 rather, it appeared to me this was an outcome that's
25 reflected in the rate plan. And so on that basis,

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1 I'm going to allow this exhibit to be admitted. Is
2 there anything further you have for Mr. Elgin?

3 MR. CEDARBAUM: No.

4 JUDGE SCHAER: Okay. Anything from any
5 other party for Mr. Elgin?

6 MS. HARRIS: I have a few questions, Your
7 Honor.

8 R E C R O S S - E X A M I N A T I O N

9 BY MS. HARRIS:

10 Q. Mr. Elgin, could you please refer back to
11 your Exhibit Number KLE-3?

12 JUDGE SCHAER: That would be Exhibit 40.

13 THE WITNESS: Yes, I have that.

14 Q. There's been quite a bit of discussion
15 about table two and what's included in the fuel cost
16 and what is not included in the fuel cost.

17 A. That's correct.

18 Q. Could you please look down to footnote C?

19 A. Yes.

20 Q. And is it true to say that footnote C
21 applies to Columns D, E, F and G?

22 A. Footnote C, yes, it applies to D, E, F and
23 G, that's correct.

24 Q. And is it fair to say that footnote C
25 provides sort of a rule of thumb of how the

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1 escalations of Columns D, E, F and G are going to be
2 calculated?

3 A. That's correct.

4 Q. And what is the rule of thumb for the fuel
5 costs?

6 A. It says they're based -- it says, Costs for
7 this period are based on the following escalation
8 factors. Fuel costs escalated at three percent.

9 Q. What about purchase and interchange?

10 A. It's escalated at four percent.

11 Q. Does that state that it took into anything
12 -- does it state that any other variables besides
13 this general percentage increase was taken into
14 consideration in putting together table two?

15 A. No.

16 Q. Let's look at purchase and interchange.
17 It's escalating at four percent?

18 A. That's correct.

19 Q. Is the Tenaska restructuring indicated
20 anywhere in this purchase in the interchange row?

21 A. No.

22 Q. Is the Montana Power contract reflected
23 anywhere in this purchase and interchange row?

24 A. No.

25 Q. Are those two agreements or restructurings

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1 together contemplated in this row?

2 A. No.

3 Q. There's no magic to this row, is there?

4 A. Well, I don't know what you mean by magic.

5 Q. It's just escalating at four percent?

6 A. Right, and in so doing, what it's saying is
7 that these factors will continue to escalate through
8 this period at this rate. And it says A applies to
9 these factors that were in the exhibit that we
10 previously discussed and marked as Exhibit 53, which
11 was power cost forecast Number 9504, and that
12 includes Colstrip, it includes Tenaska, it includes
13 all of those that we just discussed. And this is how
14 those factors were modeled and applied to develop
15 these power cost deltas.

16 Q. Mr. Van Cleve asked you about Tenaska and
17 Montana Power, and I believe some other
18 restructurings. Do you remember those questions?

19 A. Yes, I recall those.

20 Q. I think you stated that the Company had
21 done very well in restructuring some of its power
22 costs?

23 A. No, I didn't say very well. I said the
24 Company had realized some benefits from those,
25 restructuring the Montana Power contract and also

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1 from the Tenaska contract.

2 Q. Are there any other restructurings that you
3 can identify?

4 A. No. As I mentioned, the other significant
5 one was the Company's mitigation efforts in the March
6 Point contracts.

7 Q. Did the Company ever make a proposal to
8 Staff to share any increases or savings that it
9 achieved?

10 A. Well, I don't know what you mean by share,
11 so I mean, if you would say we would reduce the
12 rates, no. In fact, that's why -- if that's what you
13 mean by share, that's why when the Tenaska
14 restructuring came in and we shaped that, we viewed
15 that restructuring as a power stretch saving, and we
16 said that was what was contemplated by the merger.
17 That was a power stretch goal, what the Company did
18 with that specific contract. We also knew that
19 Montana Power was part of those power stretch goals,
20 but the sale of Colstrip was not.

21 Q. During the merger, did the Company ever
22 propose to share its power cost savings?

23 A. No, and in fact, the whole premise of the
24 merger was for the Company to restructure those
25 contracts and get those power stretch savings so it

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1 could earn a fair rate of return, and we have lived
2 by that bargain, because we are not only allowing the
3 Company to keep those benefits, but we've also
4 created a regulatory asset that obligates ratepayers
5 for future costs as a part of that restructuring, so
6 we've been very up-front with that.

7 Power stretch savings are those contracts,
8 those troublesome PURPA contracts. Power stretch
9 savings, by no sense, can be, in my mind, attributed
10 to a sale of a major generation asset. To me, that's
11 a slam dunk.

12 Q. Is it your testimony that the Company never
13 offered a plan in its rebuttal testimony during the
14 merger proceeding to share power cost savings with
15 the customers?

16 A. It did in the sense that it proposed a rate
17 plan, just like Staff proposed a rate plan and Public
18 Counsel proposed a rate plan in the merger
19 proceeding, and that's what we ultimately agreed on.
20 We agreed on a rate plan, and we're sharing those
21 savings and the Company's actually realizing them.
22 I'm sorry, go ahead. I'm finished.

23 Q. Did Staff move to strike any proposal made
24 by the Company in rebuttal testimony to share power
25 cost savings with customers?

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1 A. I don't know what you're talking about
2 there. I can't answer that question.

3 Q. Did Staff move to strike the Company's PBR
4 proposal?

5 MR. CEDARBAUM: Your Honor, I'll object.
6 First of all, this is coming off an exhibit that has
7 been excluded, and so it seems to me that testimony
8 along the same lines should be excluded, as well,
9 based on relevance.

10 JUDGE SCHAER: Where in the redirect was
11 this addressed, Ms. Harris?

12 MS. HARRIS: I'm sorry. I'm addressing
13 questions from Mr. Van Cleve, where he went into the
14 power cost savings and the savings that the Company
15 has achieved.

16 JUDGE SCHAER: And was there anything in
17 his questions that addressed the rebuttal testimony
18 of the Company in the merger process?

19 MS. HARRIS: No, not specifically the
20 merger process, but --

21 JUDGE SCHAER: I think you're outside the
22 scope of the redirect. Any other questions, please
23 proceed.

24 Q. Mr. Elgin, have you done any analysis on
25 the real estate value or the value of the real estate

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1 in the Colstrip transaction?

2 A. No.

3 Q. Have you done any breakout analysis of the
4 value of the real property or the gain attributable
5 to the real property in the Colstrip transaction?

6 MR. CEDARBAUM: Your Honor, I'll object,
7 take your cue. I don't recall anybody asking these
8 types of questions on redirect.

9 MS. HARRIS: I'm sorry. Your Honor, you
10 asked the question.

11 JUDGE SCHAER: I did ask whether there was
12 real property at Colstrip.

13 MS. HARRIS: And he stated yes.

14 JUDGE SCHAER: And I believe you asked if
15 he did any breakout of that, and he said no, so I
16 don't know why you would ask it again.

17 MS. HARRIS: My further question was a
18 breakout on the gain, Your Honor, not necessarily the
19 real estate in the transaction.

20 JUDGE SCHAER: The gain on the real estate;
21 is that the question?

22 MS. HARRIS: Right.

23 JUDGE SCHAER: Go ahead.

24 Q. Have you made any analysis on the specific
25 gain for the real property in the Colstrip

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1 transaction?

2 A. By real property, you mean the land?

3 Q. Yes.

4 A. No.

5 MS. HARRIS: No further questions.

6 JUDGE SCHAER: All right. Is there
7 anything further for Mr. Elgin. Mr. Hemstad, did you
8 have something? Okay. Mr. Manifold.

9 MR. MANIFOLD: One very small thing.

10 R E C R O S S - E X A M I N A T I O N

11 BY MR. MANIFOLD:

12 Q. On the Redirect Exhibit C-55. Mr. Elgin.

13 A. Yes.

14 Q. On the first page, the last two lines, as I
15 understood your explanation, show anticipated income
16 to the Company in '97, the REA PRAM true-up and the
17 interest on conservation tax?

18 A. Yes.

19 Q. Okay. On page two, where you compared
20 actuals to anticipated, are those two anticipated
21 items included?

22 A. No, the only thing -- one of the items is
23 included. It's the piece that represents the
24 estimated PRAM true-up. In the contract, in the
25 settlement contract with BPA, PSE obtained more in

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1 the PRAM true-up. And basically, these numbers came
2 from a Commission Docket UE-970451, where they asked
3 to shape the exchange benefits, and so that comes
4 from their specific request to shape what it realized
5 under the contract.

6 I think -- I don't have that BPA document
7 right in front of me, but I think that number was
8 about 35 or 37 million, and in the next year was
9 about 10 million.

10 Q. But it's included on your second page?

11 A. Yeah.

12 Q. What about the 15 million on the interest
13 from conservation tax to make these parallel?
14 Wouldn't that need to be added on to page two?

15 A. Well, yes and no. The 15 million was in
16 another docket, and my understanding is that did flow
17 to ratepayers.

18 Q. The ratepayers?

19 A. Yes. So actually, to make it fair, that
20 would not be there.

21 MR. MANIFOLD: Okay, thank you.

22 JUDGE SCHAER: Is there anything further
23 for Mr. Elgin? Thank you for your testimony.

24 Before we break tonight, I'm told that
25 earlier bench request really wasn't answered in the

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1 way that I had hoped it would, so my bench request to
2 you, Mr. Roland Martin, is to please provide the
3 exact calculation of the estimated gain of
4 \$39,403,538 on page 14, line 15 of your testimony.
5 Can you do that by tomorrow?

6 MR. MARTIN: Yes.

7 JUDGE SCHAEER: Okay. So we will bring that
8 in and we'll make that an exhibit at tomorrow's
9 proceeding. Is there anything else that needs to
10 come before us before we break for the evening?

11 MR. CEDARBAUM: Will we be upstairs in the
12 hearing room tomorrow?

13 JUDGE SCHAEER: We will not. Unfortunately,
14 the collocation folks are up there tomorrow morning,
15 as well, so we will be back here. You may leave
16 anything in this room that you wish to leave here
17 tonight, and we will start at 9:00 tomorrow morning.
18 We're off the record.

19 (Proceedings adjourned at 6:00 p.m.)

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