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June 15, 2010

David W. Danner, Executive Director and Secretary
Washington Utilities and Transportation Commission
1300 S. Evergreen Park Dr. SW
P. O. Box 47250
Olympia, Washington 98504-7250

RE: *In the Matter of the Amended Petition of Puget Sound Energy, Inc. For an Order
Authorizing the Use of the Proceeds from the Sale of Renewable Energy Credits and
Carbon Financial Instruments*
Docket UE-070725

Dear Mr. Danner:

Enclosed for filing in the above-referenced docket are the original and 10 copies of
Commission Staff's Response to Puget Sound Energy's Petition for Reconsideration, and
Certificate of Service.

Sincerely,

DONALD T. TROTTER
Assistant Attorney General

DTT:klg
Enclosures
cc: Parties

BEFORE THE WASHINGTON UTILITIES AND TRANSPORTATION COMMISSION

Amended Petition of

PUGET SOUND ENERGY, INC.

For an Order Authorizing the Use of the
Proceeds from the Sale of Renewable
Energy Credits and Emission Reduction
Allowances for Renewable Resource
Research, Development, and Demonstration
Projects and the Associated Accounting
Treatment

DOCKET UE-070725

COMMISSION STAFF'S
RESPONSE TO PUGET SOUND
ENERGY'S PETITION FOR
RECONSIDERATION

1 Puget Sound Energy's (PSE) Petition for Reconsideration (Petition)¹ requests the Commission reconsider Order 03² to: (1) relieve PSE from accruing interest on balances in the new Regulatory Liability account;³ and (2) add \$3,165,000 to PSE's share of Renewable Energy Credit (REC) proceeds related to the California Receivable.⁴

2 For the reasons stated below, the Commission should grant PSE's Petition for the purpose of clarifying Order 03 to require PSE to accrue interest on REC balances prior to the time the Commission includes them in rate base for rate making purposes. Once the Commission includes REC amounts in rate base, PSE should cease accruing interest on those amounts. The Commission should deny the Petition on the California Receivable issue.

¹ Puget Sound Energy Inc.'s Petition for Reconsideration (May 28, 2010).

² Final Order Granting in Part, and Denying, in Part, Amended Petition: Determining Appropriate Accounting and Use of Net Proceeds from the Sales of Renewable Energy Credits and Carbon Financial Instruments (May 20, 2010) (Order 03).

³ Petition at second page, ¶ 3, to third page, ¶ 6.

⁴ Petition at third page, ¶ 7, to fifth page, ¶ 11.

I. FACTS

3 **Regulatory Liability Method.** In Order 03, the Commission accepted the
Regulatory Liability method proposed by Staff as the Commission's method for returning
REC proceeds to ratepayers.⁵ As the Commission observed, the Regulatory Liability
method calls for PSE to book REC proceeds in a regulatory liability account, "which will be
used to reduce PSE's rates"⁶ As Staff explained, this rate reduction is accomplished by
using the unamortized balance of the Regulatory Liability account as a rate base reduction.⁷

4 In approving that method, the Commission required PSE to accrue interest on the
balances in the Regulatory Liability account.⁸ When Staff described its proposed
Regulatory Liability method, Staff did not expressly refer to interest accrual.⁹

5 **California Receivable.** In Order 03, the Commission gave PSE a share of REC
proceeds related to the California Receivable issue. Though the Commission found the
evidence to be "decidedly mixed," the Commission determined PSE achieved a "premium"
over market when it sold RECs to SCE.¹⁰ Specifically, the Commission found it was
"reasonable to infer a premium of \$5.60 [per REC] in the settlement price paid by SCE
[Southern California Edison]."¹¹

6 The Commission determined the total amount of premium to be \$11.2 million, which
the Commission reduced by \$4.6 million in outside litigation costs PSE already had

⁵ Order 03 at 28, ¶ 68 and at 30, ¶ 80 (Finding of Fact No. 11). At pages 29, ¶ 78 (Finding of Fact No. 9) and at page 31, ¶ 88 (Conclusion of Law No. 7), the Commission called upon PSE and other parties to support the appropriate interest rate the Commission should apply to the REC balances in the account.

⁶ Order 03 at 27, ¶ 66.

⁷ Parvinen, Exhibit No. MPP-1T at 8:17-18.

⁸ Order 03 at 28, ¶ 68.

⁹ Staff witness Parvinen described the Regulatory Liability method in his Exhibit MPP-1T at 8:15-23.

¹⁰ Order 03 at 18, ¶ 44.

¹¹ Order 03 at 18, ¶ 48.

recovered from ratepayers,¹² and then by 50% to reflect an equitable sharing, resulting in a \$3.3 million share of REC proceeds for PSE.¹³

II. ARGUMENT

A. The Interest Accrual Issue

7 PSE takes exception to the Commission's requirement in Order 03, Paragraph 68, that PSE accrue interest on balances in the Regulatory Liability account. Citing the Commission's recent order in a PSE rate case, PSE argues "to accrue [interest] on rate base that is also earning a rate of return is not allowed because it would result in double recovery."¹⁴

8 In order to understand PSE's argument, it is necessary to review the Commission's recent PSE rate case order upon which PSE relies. In that case, the issue involved PSE's Mint Farm generating facility. The applicable statute¹⁵ permitted PSE to accrue and defer the cost of capital, among other things, before the Commission included the plant in rate base. Accordingly, PSE deferred Mint Farm capital costs using the Commission-authorized rate of return. In addition to such capital cost accrual, however, PSE also asked the Commission for permission to collect from ratepayers carrying costs on the Mint Farm plant balances, pending the plant's inclusion in rate base.¹⁶

¹² This \$4.6 million amount of litigation costs may change as PSE accounts for its in-house legal costs related to the California Receivable. Order 03 at 10-11, ¶¶ 30-34, and at 30, ¶ 79 (Finding of Fact No. 10). Thus, the \$4.6 million very likely is an understated figure, which means the Commission's calculation of PSE's share of REC proceeds very likely is overstated.

¹³ Order 03 at 19, ¶¶ 46-47, at 29, ¶ 75 (Finding of Fact No. 6), and at 30, ¶ 85 (Conclusion of Law No. 4).

¹⁴ Petition at second page, ¶ 5, citing *Utilities & Transp. Comm'n v. Puget Sound Energy, Inc.*, Docket Nos. UE-090704 & UG-080705, Order 11, Rejecting Tariff Sheets; Authorizing and Requiring Compliance Filing (April 2, 2010) (Order 11) at ¶¶ 242 & 247.

¹⁵ RCW 80.80.060(6).

¹⁶ *Utilities & Transp. Comm'n v. Puget Sound Energy, Inc.*, Dockets UE-090704 & UG-080705, Order 11 at 82, ¶ 237 to 84, ¶ 246.

9 The Commission rejected PSE's request for carrying cost recovery. In its analysis, the Commission noted Staff's opposing argument that if the Commission allowed recovery of carrying costs, in addition to the capital costs PSE deferred, "the Company's total return on investment will exceed the allowed net of tax return."¹⁷ In rejecting PSE's request for carrying costs, the Commission did not use the term "double recovery," as PSE implies. It is more accurate to say the Commission denied the carrying costs because it would result in excessive recovery by PSE: "... there is no reason to allow PSE to recover yet additional revenue [i.e., over and above the capital costs PSE already deferred] in the form of carrying costs."¹⁸

10 To date, PSE has not accrued any interest, carrying costs, or return on REC balances. Thus, a different question arises: whether PSE should accrue interest on REC balances **before** the Commission includes them in rate base for rate making purposes?¹⁹ The answer is Yes, because unlike the situation in the recent PSE rate case involving Mint Farm, the Commission's requirement that PSE accrue interest on REC balances would neither be excessive nor a "double recovery," to use PSE's term. PSE advances no reason why it should not accrue interest on REC balances prior to rate base treatment, and Staff perceives no reason.

11 Consequently, the Commission should clarify its order to indicate that PSE should accrue interest on REC balances prior to the time the Commission includes them in rate base

¹⁷ Id. at 83, ¶ 242.

¹⁸ Id. at 85, ¶ 248. PSE does not raise any argument related to the impact of REC-related accrued interest on the calculation of working capital for rate making purposes. Such accrued interest likely would affect the calculation of PSE's working capital, but that does not appear to be sufficient reason for the Commission to reject interest accrual on REC proceeds,

¹⁹ There appears to be no dispute that PSE should not accrue interest on REC amounts once the Commission includes those amounts in rate base for rate making purposes.

for rate making purposes. However, once the Commission includes REC amounts in rate base, PSE should cease accruing interest on those amounts.

B. The Commission Should Not Increase PSE's Share of REC Proceeds Due to the California Receivable

12 PSE has provided the Commission insufficient reasons to expand PSE's already more than generous²⁰ share of REC proceeds. In short, PSE is simply wrong to claim the Commission committed an "oversight" by calculating a premium over market only for PSE's sale of RECs to SCE,²¹ when the facts show the Commission was being insightful.

13 For example, the Commission clearly referred to the price PG&E paid PSE for RECs as a market price.²² Obviously, if PG&E paid market price for RECs, there can be no premium over market price related to that sale. Indeed, because the "settlement of the California litigation was not contingent upon a completed agreement for the sale of RECs to [PG&E],"²³ PG&E would have been imprudent to pay more than market price for PSE's RECs.

14 In sum, because PG&E paid PSE no premium over market, the Commission should deny PSE's Petition on the California Receivable issue.

III. CONCLUSION

15 For the reasons stated above, the Commission should grant PSE's Petition for the purpose of clarifying Order 03 to require PSE to accrue interest on REC balances prior to the time the Commission includes them in rate base for rate making purposes. However, once the Commission includes REC amounts in rate base, PSE should cease accruing

²⁰ See discussion in footnote 22, *infra*.

²¹ Petition at fourth page, ¶ 10.

²² Order 03 at 19, footnote 53. Given the Commission's observation in footnote 53 that the SCE sale "established a new 'market price'", it is no understatement to say the Commission was exceedingly generous giving PSE any premium-related reward regarding the sale of RECs to SCE. If the Commission reconsiders that decision, it should take away the \$3.3 million it gave PSE related to that sale.

²³ DeBoer, Exhibit No. TAD-1T at 7:3-11.

interest on those amounts. The Commission should deny the Petition on the California Receivable issue.

Dated this 15th day of June 2010.

Respectfully submitted,

ROBERT M. MCKENNA
Attorney General

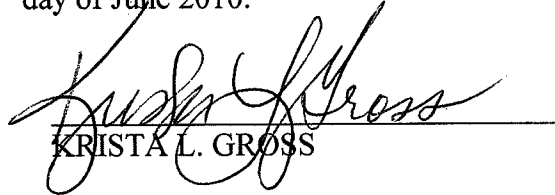
A handwritten signature in black ink, appearing to read 'D. Trotter', is written over a horizontal line.

DONALD T. TROTTER
Assistant Attorney General
Counsel for Washington Utilities and
Transportation Commission

Docket UE-070725
CERTIFICATE OF SERVICE

I hereby certify that I have this day served the attached document upon the persons and entities listed on the Service List below by depositing a copy of said document in the United States mail, addressed as shown on said Service List, with first class postage prepaid.

DATED at Olympia, Washington this 15th day of June 2010.



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C=Confidential

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