BEFORE THE
WASHINGTON UTILITIES AND TRANSPORTATION COMMISSION

BELLINGHAM COLD STORAGE COMPANY and GEORGIA-PACIFIC WEST, INC.,	No. UE-001014 No. UE-000735
Complainants,	
v.	PUGET SOUND ENERGY, INC.'S PHASE I MOTION FOR SUMMARY DETERMINATION
PUGET SOUND ENERGY, INC.,	
Respondent.	[Oral Argument Requested]

CONTENTS

1. Pursuant to WAC 480-09-426 and the Prehearing Conference Order in these dockets, Puget Sound Energy, Inc. ("PSE"), hereby submits its Motion for Summary Determination regarding issues related to Phase I of this proceeding.[1]

2. This motion brings into issue the following rules or statutes: RCW 80.04.110, 80.04.120, 80.28.020, 80.28.100, 80.28.110, WAC 480-09-426 and 480-40-335.

INTRODUCTION

3. The Special Contracts that the Complainants challenge speak for themselves. The Special Contracts have "the same effect as filed tariffs and are subject to enforcement, supervision, regulation, and control as such." WAC 480-80-335(3). The Special Contracts explicitly subject the Complainants to the risk of market volatility, and are also crystal clear with respect to how the price charged to BCS and GP is to be measured and determined: it is by reference solely to the Index set forth in the Special Contracts. Nor do the Special Contracts allow the Complainants to rewrite the Special Contracts under the guise of Optional Price Stability provisions that are clearly to be negotiated. Thus, the plain language of the Special Contracts requires dismissal of the Complainants' power pricing claims. Risk avoidance mechanisms that were available to the Complainants were not exercised. As a matter of law, the Complainants cannot unilaterally escape the consequences of their bargain or the terms of the existing tariff, and their power pricing claims should be dismissed.

4. Even if the Commission were to look beyond the plain terms of the Special Contracts, the Special Contracts were permitted to go into effect within a regulatory context that protects the public interest and prohibits the remedies the Complainants are seeking

[1] The July 24, 2000, Prehearing Conference Order divided issues raised in these dockets into two phases. In Phase I, the Commission will consider and resolve power pricing issues. In Phase II, the Commission will consider and resolve transmission issues. The Order set a deadline of July 31, 2000, for the filing of dispositive motions for Phase I.

through these proceedings. When BCS and GP entered into the Special Contracts, they sought and obtained an alternative to rates set by reference to PSE's embedded costs. The Complainants obtained market-based pricing only through threats of bypassing PSE's system altogether. The fact that the market is no longer desirable to them does not justify a unilateral decision allowing them to opt back into the protections of cost-based pricing. Changing the existing Special Contracts, and permitting BCS and GP access to power at cost-based rates effectively would require PSE's core customers to subsidize poor decision making by BCS and GP.

5. "In setting rates, the Commission is obligated to balance investor and consumer interests." POWER v. WUTC, 104 Wn.2d 798, 819, 711 P.2d 319 (1985). Complainants would have the Commission upset this allocation of risks and benefits, to the detriment of PSE's shareholders and other customers. Neither PSE nor its other customers should be asked to subsidize the Complainants. This is not what was intended nor what is provided by the Special Contracts. Complainants' proposed remedies would impair PSE's contract rights, and would effect an unconstitutional taking.

6. In the Merger Order, PSE's rates were frozen from 1997 through 2001. The rate plan approved in the Commission's Merger Order factors in the risks and potential rewards of a five-year rate freeze. However, PSE thereby obtained the corresponding commitment that PSE's shareholders would retain the benefits of increased efficiencies, decreased costs, and other management decisions during the rate stability period. Selectively altering this balance takes away benefits from PSE secured by the Merger Order. Any change in the pricing principle for these Special Contracts during the rate freeze without PSE's consent would be inconsistent with the Merger Order. To change that component of the Merger Order is inherently unfair to PSE. PSE relied on the Merger Order and agreed to bear

(and has borne) the risk of downward market index fluctuations under these Special Contracts and the other risks inherent in the rate stability plan under the terms approved in the Merger Order. Such a change would operate under the current circumstances to unconstitutionally take PSE's property and impair PSE's rights under the Merger Order and its Special Contracts with GP and BCS.

7. For the foregoing reasons, PSE is entitled to summary determination as a matter of law. However, should the Commission determine that PSE is not entitled to summary determination on all Phase I issues, the Commission should narrow the scope of these proceedings.

8. In their prayer for relief, the Complainants assert a desire for pricing that is "set equal to a payment which represents the estimated cost to PSE of operating its least efficient power plant, the Whitehorn simple-cycle combustion turbine (estimated at 40.15 mills/KWh)." Complaint at 9. The costs to PSE of purchasing power or generating power through its own resources are not relevant to the price for power under the Special Contracts. The Commission should dismiss this request for relief as a matter of law, and rule that matters related to PSE's costs (or estimated costs) of generating or purchasing power or any request for cost-based pricing are outside the scope of these proceedings.

9. PSE's resource costs, including but not limited to the costs for operating its Whitehorn combustion turbine generation, are not the equivalent of any Dow Jones Mid-Columbia index or any other market index. Moreover, the benefits from these resources are already committed to PSE's core customers and to PSE. Providing the Complainants with access to pricing based on PSE's resources or power purchases or a new pricing mechanism based on PSE's resource costs would be inconsistent with the Special Contracts, inconsistent with the Commission's orders permitting the Special Contracts to go into effect, inconsistent

with the Merger Order and the Commission's Schedule 48 orders, inconsistent with PSE's resource planning, and prejudicial to the interests of PSE and its core customers. Thus, the Commission should dismiss any claim for pricing based on the costs to PSE of purchasing power or generating power through its own resources, and narrow the scope of these proceedings to exclude any consideration of PSE's generation or power purchases.

FACTS

A. The Special Contracts

10. In May of 1996, PSE entered into special contracts with Bellingham Cold Storage Company ("BCS") and Georgia-Pacific West, Inc. ("GP") (sometimes referred to collectively hereinafter as the "Complainants").[2] The Special Contracts were entered into pursuant to WAC 480-40-335 and were allowed to go into effect by the Commission on June 7, 1996. See In re the Special Contract Filed by Puget Sound Power & Light Co., Docket Nos. UE-960612 and UE-960613, Order Imposing Conditions on Special Contract Allowed To Go Into Effect (June 7, 1996) ("Special Contract Orders").

11. The Special Contracts provide that GP and BCS agree to purchase power exclusively from PSE in accordance with an attached Schedule RTP and the Power Sales Agreement. See Special Contracts, p. 1, Power Sales Agreement.

12. Schedule RTP provides that GP and BCS shall pay an hourly energy price equal to the "Index" energy price, with certain adjustments that are not relevant to this proceeding. See Special Contracts, p. 5, Schedule RTP at I (Definitions: "Non-Firm Energy"). As the Commission has recognized, the Index sets the price at which the Complainants purchase power from PSE "based upon hourly regional wholesale prices

[2] The Special Contracts, which include the Amendments to Power Sales Agreement dated as of April 28, 2000, and discussed below, are found at Exhibit A to PSE's Answer to Formal Complaint.

established through a daily index of non-firm energy, priced at peak and off-peak hours." See Special Contract Orders at 2. Beginning 180 days following the effective date of the Special Contracts, the "Index" meant "the Mid-Columbia Non-Firm Electricity Index prices, reported by Dow Jones to Dow Jones Telerate Subscribers for on-peak hours and off-peak hours for each day of the relevant billing month." Schedule RTP at I (Definitions: "Non-Firm Energy").

13. Schedule RTP further provides that "[t]he customer bears all the risk for price movements in the market price . . . in absence of the election of related optional services," i.e., Optional Price Stability services. Id. Neither GP nor BCS has accepted offers by PSE to provide Optional Price Stability services under the Special Contracts. See Affidavit of William A. Gaines dated July 27, 2000, submitted in Answer to Complainants' Emergency Motion ("Gaines Emergency Aff.") at ¶¶ 4-8.

14. As of April 28, 2000, PSE entered into an "Amendment to Power Sales Agreement" with each of GP and BCS ("Amendments"). The Amendments provided for a modification of the definition of the Index set forth in the Special Contracts, effective November 1, 1999, in order to clarify an ambiguity in the Index, but did not otherwise change the Special Contracts. The Amendments were entered into pursuant to an "Accord and Satisfaction And Agreement Regarding Index" signed by PSE, GP and BCS on October 27, 1999.[3]

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[3] The Amendments and Accord and Satisfaction are also found at Exhibit A to PSE's Answer to Formal Complaint.

The Amendments and Accord and Satisfaction together reflected voluntary settlement of a dispute between the only parties affected by the rate under the Special Contract. That settlement involved agreement that PSE would pay (and PSE has paid) $800,000 for the period prior to November 1, 1999, and agreement that the dispute over payments made after that date under the Special Contracts would be resolved by calculating the rate as specified in the Amendments. Although this settlement is not at issue in this motion, PSE reserves its rights with respect to this issue, and notes that such settlement is not retroactive ratemaking. See In re Application of Consumers Power Co.

15. The Special Contracts, as amended, were filed with the Commission on June 28, 2000. On July 12, 2000, the Commission permitted the Amendments to become effective as of July 13, 2000 (rather than November 1, 1999).[4] See In re the Special Contract Filed by Puget Sound Energy, Docket No. UE-960612 and Docket No. UE-960613, Second Supplemental Order Granting Amendment to Special Contract on Less Than Statutory Notice (July 12, 2000) ("Amendment Orders"). Thus, since July 13, 2000, the "Index" for the Special Contracts has been the Index set forth in the Amendment, the Dow Jones Mid-Columbia Electricity Index reporting "Firm On-Peak," "Firm Off-Peak" and "Sunday NERC Holidays 24 Hour Firm" energy prices (in dollars per megawatt hour):

> For purposes of this agreement, "Index" means the Dow Jones Mid-Columbia Electricity Index reporting "Firm On-Peak," "Firm Off-Peak" and "Sunday & NERC Holidays 24 Hour Firm" energy prices (in dollars per megawatt-hour). For purposes of this agreement, "on-peak," "off-peak," "Firm On-Peak," "Firm Off-Peak" and "Sunday & NERC Holidays 24 Hour Firm" have the respective meanings ascribed to such terms by Dow Jones in connection with the Dow Jones Mid-Columbia Electricity Index.

Amendments at ¶ 1(a).

16. As of April 28, 2000, as part of the Amendments, BCS and GP agreed to "support approval of the filing of this Amendment and the Accord and Satisfaction and shall

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Requesting the Commission to Review and Approve a Settlement, Case No. U-10037, 1992 Mich. PSC LEXIS 94 at *14 (Mich. PSC 1992) (adoption of settlement was not unlawful because parties "voluntarily entered into the settlement . . . and gave up potential claims of illegal retroactive ratemaking"); Complaint of Ametel Consulting Co. v. Southwestern Bell Tel. Co., Docket No. 5580, 1984 Tex. PUC LEXIS 75 at *8-13 (Tex. PUC 1984) (approving arm's length agreement with sophisticated customer to resolve billing dispute).

[4] The effective date was changed due to Staff's concern that an earlier effective date would constitute retroactive ratemaking, and apparently due to Staff's belief that charges between June 1, 1998, and July 12, 2000, should be re-evaluated in light of the Commission's decision in the Fifth Supplemental Order in Docket No. UE-981410 (Air Liquide, et al. v. Puget Sound Energy). See Commission Staff Open Meeting Memorandum, Docket Nos. UE-960612 and UE-960613, Agenda Date July 12, 2000. As noted in footnote 3 above, the negotiated settlement should stand.

express no view inconsistent with the proposition that such approval is in the public interest." Amendment at ¶ 2.

B. Complainants Have Benefited in the Past From the Index Price, and Have Opted Not to Hedge Against the Risks of Price Increase

17. During the term of the Special Contracts, the Complainants have reaped substantial benefits from the deal they struck with PSE. PSE estimates that the Special Contracts resulted in a savings in power costs for the Complainants of approximately $8 million, from the inception of the Special Contracts through the end of April 2000. See Gaines Emergency Aff. at ¶ 24.

18. GP and BCS have had the opportunity to hedge against the risks of an increase in the market price for electricity, both through PSE and through other sources. However, they have elected not to do so. See Gaines Emergency Aff. at ¶¶ 4-8.

19. Since 1997, PSE has made proposals to Complainants that would have protected them from market volatility, including the following offers:

> In 1997, the year after the Special Contracts were signed, PSE offered BCS and GP a fixed price swap that would have provided BCS and GP with a fixed price for five years at a price below 20 mills/kWh. This would have provided GP and BCS with protection against all market price volatility from 1997 through 2001 at a price that would have been substantially below current market prices. BCS and GP turned down PSE's 1997 proposal for price stability.
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> In late 1999, PSE offered BCS and GP a fixed price of 28 mills/kWh flat for five years. Again, this would have provided BCS and GP with protection against all future market volatility for five years at a price that would have been well below current market prices. BCS and GP turned down PSE's 1999 proposal for price stability.
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> Earlier this year, with markets beginning to tighten and with predictions of increased price volatility, PSE offered BCS and GP a Summer price cap of 70 mills/kWh, which would have reduced price volatility to a level that has turned out to be below Summer market prices. BCS and GP rejected the price stability proposal.

See Gaines Emergency Aff. at ¶ 4. Moreover, on June 29, 2000, the same day the Complaint in this proceeding was filed, a GP representative stated to PSE and others, including the Mayor of Bellingham, that *it has been GP's corporate policy not to hedge.* See id.[5]

20. The Special Contracts contain an "Optional Price Stability" provision. Section III of the Schedule RTP states that the price for this service is to be "Negotiated." Schedule RTP at III (Prices - "Optional Price Stability").

C. The Complainants Are Non-Core Customers, Who Have Elected to Pay Market-Based Prices for Power and Forego Access to PSE's Power Resources

21. The Special Contracts were entered into by GP and BCS in lieu of a bypass alternative offered by Public Utility District No. 1 of Whatcom County ("PUD"). The bypass alternative was considered by the Commission in determining that the Special Contracts complied with WAC 480-80-335(5). The Complainants sought and obtained the Special Contracts, with market-based pricing, as they believed that buying power at market-based prices would cost less than buying power at PSE's embedded-cost based rates. See Special Contract Orders at 1-2.

22. The Special Contract Orders allowing the Special Contracts to go into effect state: "After the expiration of the five year power sales agreement, the customer shall have no expectation of access to power resources that it otherwise may be entitled to under RCW 80.28.110." Special Contract Orders at 4. In permitting the Special Contracts to go into effect, the Commission affirmed that the Complainants, through the Special Contracts, became non-core customers. GP and BCS have no right to prices based on PSE's existing resource base. The Complainants' future power resources were to be those available to PSE

[5] During oral argument on Complainants' Emergency Motion for Implementation of Optional Price Stability Provision of Special Contracts And, If Necessary, For A Retail-Access Pilot Program ("Emergency Motion"), counsel for GP admitted that GP chose to self insure against the risk of market volatility.

on the market, at the prices set forth in the Special Contracts. See id.

23. The Commission also explicitly recognized that the Complainants would bear the risk of future increases in price: "The energy charge is based upon hourly regional wholesale prices established through a daily index of non-firm energy, priced at peak and off-peak hours. The *customers assume the risk of fluctuations* in regional non-firm energy prices, *but may purchase optimal price stability at negotiated rates*." Special Contract Orders at 2 (emphasis added).

24. Customers that purchase power pursuant to the Special Contracts are similar to Schedule 48 customers, in that both are "non-core" customers. See WUTC v. Puget Sound Power & Light Co., Docket No. UE-960696, Commission Order Approving Schedule 48 With Conditions (Oct. 31, 1996) ("Schedule 48 Order") at 2, 6. The Commission has held that costs may not be shifted to other customer classes based on changes in market prices. Id. at 5, 6-7. See also Special Contract Orders at 3. Within the past year, the Commission has reaffirmed its earlier decisions prohibiting cost shifting to other customer classes:

> The Commission approved Schedule 48 on October 31, 1996. Washington Utilities and Transportation Commission v. Puget Sound Power & Light Company, Docket No. UE-960696, Commission Order Approving Schedule 48 With Conditions. As the caption to that Order reflects, the Commission imposed conditions. Among those conditions is the following:
>
> > (1) **No Cost Shifting** – The revenue difference between Schedule 48 rates and the effective tariff rates that otherwise would be applicable to current Schedules 31, 46, 49, or special contract customers (i.e., lost revenues), shall not be shifted to other customer classes and shall be borne by shareholders until a future Commission determination regarding allocation of costs and cost savings, and then on a prospective basis only.
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> Id. at 5. We emphasize that this condition, along with the others established by the Commission's Order approving Schedule 48, remains effective. We reiterate, too, the Commission's understanding that this condition is a "guarantee that other classes will not pay more

as a result of Schedule 48." Id. at 7.

WUTC v. Puget Sound Energy, Docket No. UE-981238, Seventh Supplemental Order, Order Approving and Adopting Stipulation and Settlement Agreement (Nov. 30, 1999) at 4-5 (Seventh Supp. Order); Amendment Orders at 1-2.

25. Also, the Commission has reemphasized that customers receiving market-based prices bear the risk of fluctuations in the market:

> Our approval of the Stipulation and Settlement Agreement here depends in part on our acceptance of the $0.46 per kVa-month optional firming rate as being a rate that reasonably reflects market prices and the parties' apparent belief that the $0.46 per kVa-month rate is expected to continue to reflect market prices during the effective period of the settlement. *Swings in actual market prices in future periods* vis-à-vis the $0.46 per kVa-month rate for optional firming, however, may result in lost revenue to PSE, *or may result in customers paying more than might be the case in a fully open, competitive market*. *The respective parties have assumed these risks of market fluctuation* under the terms of the Commission's Order approving Schedule 48 and under this Order approving the Stipulation and Settlement Agreement. *We expect both PSE and the Schedule 48 customers to conduct themselves accordingly on a going-forward basis*.

Seventh Supp. Order at 5 (emphasis added).

III. ARGUMENT

A. Standard on Motion for Summary Determination

26. Pursuant to WAC 480-09-426(2), a party requesting summary determination must show that "the pleadings filed in the proceeding, together with any properly admissible evidentiary support, show that there is no genuine issue as to any material fact and the moving party is entitled to summary determination in its favor." The Commission considers motions for summary determination under "the standards applicable to a motion made under CR 56 of the civil rules for superior court." Id. The civil rules provide:

> The judgment sought shall be rendered forthwith if the pleadings,

> depositions, answers to interrogatories, and admissions on file, together with the affidavits, if any, show that there is no genuine issue as to any material fact and that the moving party is entitled to a judgment as a matter of law.

CR 56(c).

27. The moving party bears the burden of demonstrating an absence of any material fact and entitlement to judgment as a matter of law. Magula v. Benton Franklin Title Co., 131 Wn.2d 171, 182, 930 P.2d 307 (1997). A material fact is one of such nature that it affects the outcome of the litigation. Greater Harbor 2000 v. Seattle, 132 Wn.2d 267, 279, 937 P.2d 1082 (1997).

B. PSE Is Entitled to Summary Determination in Its Favor on All Phase I Issues

1. The Index Accepted by the Commission Is the Lawful Rate, and the Special Contracts Unambiguously Allocate the Risk of Increases in Market Price to the Complainants

a. Standards for considering the Complainants' challenge to the Special Contracts

28. The Special Contracts have "the same effect as filed tariffs and are subject to enforcement, supervision, regulation, and control as such." WAC 480-80-335(3). When a rate is filed, published and permitted to become effective, it is the only lawful rate until challenged in the manner provided by statute, and it is presumed to be reasonable. See Puget Sound Navigation Co. v. Department of Public Works, 157 Wash. 557, 561-62, 289 P. 1006 (1930), aff'd, 160 Wash. 703 (1931); State ex rel. Standard Oil Co. of California v. Department of Public Works, 185 Wash. 235, 238-239, 53 P.2d 318 (1936). See also General Tel. Co. v. City of Bothell, 105 Wn.2d 579, 585, 716 P.2d 879 (1986); Air Liquide America Corp. et al. v. Puget Sound Energy, Inc., Docket No. UE-981410, Fifth Supplemental Order Granting Complaint, Ordering Refunds and Other Relief, 1999 Wash. UTC LEXIS 591 at *10-11 (Aug. 3, 1999) ("Air Liquide").

29. Where a complaint challenges the reasonableness of an effective rate, such rate may only be changed if the Commission, after notice and hearing, finds that the existing rate is unjust or unreasonable. See RCW 80.04.110(1); RCW 80.04.120; RCW 80.28.020. Only after the Commission makes such a finding can it then "determine the just, reasonable, or sufficient" rates or charges "to be thereafter observed and in force." RCW 80.28.020.[6]

30. The complainants in a challenge brought pursuant to RCW 80.04.110 bear the burden of proving that the challenged rate is unreasonable. See, e.g., State ex rel. Model Water & Light Co. v. Department of Pub. Serv., 199 Wash. 24, 35, 90 P.2d 243 (1939); In re Complaint of AT&T Communications of the Northwest, Inc. v. U S WEST Communications, Inc., Docket No. UT-991292, Tenth Supplemental Order, Order Granting Motion to Dismiss (May 19, 2000) at 5.

31. In the present case, BCS and GP focus nearly exclusively on the changes they believe should be made to the pricing provisions of the Special Contracts, and seek imposition of their proposed remedies on an expedited basis. In so doing, *they utterly ignore their burden to make a threshold showing that they are entitled to any relief at all.*

32. The Commission determines the meaning of a tariff "from its plain terms, or, where it is not plain and unambiguous, by applying rules of construction." Air Liquide, 1999 Wash. UTC LEXIS 591 at *10; National Union Ins. Co. v. Puget Sound Power & Light Co., 94 Wn. App. 163, 171, 972 P.2d 481 (1999), review denied, 138 Wn. 2d 1010 (1999). In the case of special contracts that the Commission allows to become effective, the Commission also implicitly considers principles of contract law to inform its analysis and decision,

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[6] During oral argument on Complainants' Emergency Motion, counsel for GP argued that, pursuant to RCW 80.28.040, the Complainants do not have to establish that the rate in effect is unjust and unreasonable. Complainants' argument is inconsistent with the well-established principle that a complainant bears the burden when a rate is challenged, and appears to confuse the standards for challenges to rates with matters germane to the adequacy of service.

because special contracts are the product of negotiation. See Air Liquide, 1999 Wash. UTC LEXIS 591 at *12-13.

33. At least one public service commission has declined to accept a unilateral filing that sought to change one aspect of some special contracts, noting that "[t]he parties to the contracts negotiated their provisions and freely agreed to their terms" and the commission had previously found "the contracts as a whole to be reasonable…." See In the Matter of the Application of Ohio Edison Company for Authority to Change Certain of Its Filed Schedule Fixing Rates and Charges for Electric Service, 89-1001-EL-AIR, 1990 Ohio PUC LEXIS 1125 at *54-55 (Oct. 11, 1990).

b. The Special Contracts, on their face, subject the Complainants to the risk of increased power prices, and should be enforced

34. In the present proceedings, the Special Contracts explicitly subject the Complainants to the risk of market volatility:

> The *customer bears all the risk for price movements in the market price* and will receive non-firm energy service in absence of the election of related optional services.

Special Contract, p. 5, Schedule RTP I (Definitions: "Non Firm Energy") (emphasis added). There is no ambiguity in the Special Contracts as to this issue.

35. The Special Contracts, as amended, are also crystal clear with respect to how the price charged to BCS and GP is to be measured and determined: it is by reference solely to the Index set forth in the Special Contracts. See id.[7]

36. The Special Contracts do contemplate that BCS and GP may obtain protections from market volatility. See id. The Optional Price Stability provision of

[7] Although the parties had a dispute in the past regarding interpretation of the Index, that dispute was resolved by the negotiated Amendments to the Special Contracts, which the Commission has permitted to become effective. BCS and GP do not complain of any remaining ambiguity, but rather argue for wholesale abrogation of pricing provided for in the Special Contracts.

Schedule RTP provides:

> Price of these Optional Price Stability services will be customized to customer's needs. These services could include guarantee on an average commodity price, price caps on non-firm prices, or collars on the non-firm price.

Special Contracts, p. 6. However, Section III of the Schedule expressly states that the price for this service is "Negotiated." Neither GP nor BCS has accepted offered Optional Price Stability services under the Special Contracts, and they have failed to take advantage of multiple opportunities to hedge against potential price increases. See Gaines Emergency Aff. at ¶¶ 4-8.

37. Thus, the plain language of the Special Contracts requires dismissal of the Complainants' power pricing claims. The plain language of the Special Contracts also requires dismissal of any claim that Complainants are entitled to impose their own price under the Optional Price Stability provisions of the Special Contracts, and precludes any claim that Complainants are entitled to convert the Special Contracts to buy/sell agreements, and thereby obtain retail wheeling.[8]

38. Even if the Commission were to look beyond the plain language of the Special Contracts, the Commission's Special Contract Orders amply demonstrate the Commission's intent when it permitted the Special Contracts to go into effect. The Commission affirmed that the Index sets the price at which PSE is to sell power to the Complainants. It also affirmed that unless GP and BCS purchased protection from market volatility through rates negotiated with PSE, "[t]he customers assume the risk of fluctuations in regional non-firm

[8] As noted in footnote 1, transmissions issues are supposed to be addressed in Phase II of this proceeding, and not at this time. The scope of the Optional Price Stability provision was raised, however, in Complainants' Emergency Motion. The narrow issue presented in this motion is whether Optional Price Stability under the Special Contracts is anything other than a mechanism to negotiate price stability mechanisms, such as a "guarantee on an average commodity price, price caps or non-firm prices, or collars on the non-firm price." Special Contracts, p. 6.

energy prices." See Special Contract Orders at 2.

39. In addition to the rules applicable to interpretation of the Special Contracts, described above, fundamental principles of contract law support enforcement of the Special Contracts through dismissal of the Complainants' power pricing claims. A party may not escape its obligations under a contract simply because market conditions change in a way that makes its terms less attractive than when the contract was negotiated. See Blanck et al. v. Pioneer Mining Co., et al., 93 Wash. 26, 32, 159 P. 1077 (1916) ("Equity has never presumed to rewrite contracts for parties *sui juris* merely because of disappointed expectations" such as "rise or fall in values, profit or loss in the undertaking, mistakes of judgment, unforeseen events, which yet were fairly possible contingencies."); Felt v. McCarthy, 130 Wn.2d 203, 210, 922 P.2d 90 (1996) (a decline in the value of a contract is insufficient to warrant rescission of the contract under the frustration doctrine).

40. In the present case, the Special Contracts clearly allocate the risk of increases in price to BCS and GP. As a matter of law, the Complainants cannot unilaterally escape the consequences of their bargain. See Scott v. Petett, 63 Wn. App. 50, 60, 816 P.2d 1229 (1991) ("[T]he doctrine of frustration does not apply if the contract between the parties disclosed an allocation of that risk to one party or the other.").

41. The Special Contracts, on their face, do not require that the Index perfectly reflect "the market" for electricity, or that there be a "perfect market," or that the market be without risk. Rather, the Special Contracts set the price PSE is to charge BCS and GP by reference to a plainly defined Index, and explicitly allocate the risk of increased prices to BCS and GP. Risk avoidance mechanisms that were available to the Complainants were not exercised. The Complainants cannot escape the plain terms of the Special Contracts that the Commission permitted to go into effect, or the obligations they undertook in agreeing to the

Special Contracts, including the recent amendments thereto, merely because they are now facing the downside of risks they freely accepted. The Commission should enforce the Special Contracts, as a matter of law, and dismiss all power pricing issues raised in the Complaint.[9]

2. As a Matter of Regulatory Policy, the Commission Should Dismiss the Power Pricing Claims Raised in the Complaint

42. The Special Contracts, standing alone, require dismissal of Complainants' power pricing claims. However, there are other grounds that warrant summary dismissal of the Complainants' claims. This case involves more than an effort on the Complainants' part to break their contract and undo an existing tariff. These Special Contracts were permitted to go into effect within a regulatory context that protects the public interest, and prohibits the remedies the Complainants are seeking through this proceeding.

a. BCS and GP are no longer core customers, and cannot expect PSE's core customers to subsidize imprudent business decisions made by BCS and GP

43. When BCS and GP entered into the Special Contracts, they sought and obtained an alternative to rates set by reference to PSE's embedded costs. The Complainants obtained market-based pricing only through threats of bypassing PSE's system altogether. See Special Contract Orders at 1-2. The Commission only permitted the Special Contracts to go into effect subject to provisions, discussed above, protecting PSE's remaining core customers from economic consequences that might result from the decision of PSE, BCS and GP to enter into the Special Contracts, as an alternative to complete bypass of PSE's system. See id. at 3-4. The risk of volatility in market prices was a risk absolutely and completely

[9] See also Response of Atlantic Richfield Co., Intervenor, to PSE's Request for Continuance and Extension of Time (July 26, 2000) at 3, 5 ("It seems the single critical issue at hand is whether the complainants have a contractual remedy under their special contracts." "ARCO firmly believes that both parties to any such contract should honor their respective obligations.").

assigned to the Complainants, not PSE's core customers.

44. In its 1995 Policy Statement regarding regulation of the electricity industry, the Commission emphasized the principle that PSE's core customers are not to subsidize customers that obtain market-based prices:

> Non-economic bypass and the inappropriate shifting of costs of the electric system between or among customers do not constitute fair and efficient competition, are contrary to the public interest, and should be avoided. Customers of continuing monopoly service should benefit, or at least not be harmed, from choices made by customers with access to competitive options.

In re Commission's Notice of Inquiry: Examining Regulation of Electric Utilities in the Face of Change in the Electric Industry, Docket No. UE-940932, Guiding Principles for Regulation in an Evolving Electricity Industry (Dec. 13, 1995) at 2.

45. GP and BCS elected to opt out of the burdens and benefits placed on and enjoyed by core customers, preferring market-based pricing. As a result, BCS and GP have no right to complain about market prices, and no right to PSE's existing resource base. The fact that the market is no longer desirable to them does not justify a unilateral decision allowing them to opt back into the protections of cost-based pricing. Changing the existing Special Contracts, and permitting BCS and GP access to power at cost-based rates effectively would require PSE's core customers to subsidize poor decision making by BCS and GP.

b. Changing the pricing provisions of the Special Contracts would impair substantial rights secured to PSE by those contracts

46. "In setting rates, the Commission is obligated to balance investor and consumer interests." U S WEST Communications v. WUTC, 134 Wn.2d 74, 121, 949 P.2d 1337 (1997) (citing POWER v. WUTC, 104 Wn.2d 798, 819, 711 P.2d 319 (1985). The Commission "must in each rate case endeavor to not only assure fair prices and service to

customers, but also to assure that regulated utilities earn enough to remain in business each of which functions is as important in the eyes of the law as the other." Id.

47. At the time the Commission permitted the Special Contracts to go into effect, PSE's annual revenues under the Special Contracts were unknown, "since customers are responsible for paying the actual market prices based upon the power cost index." PSE Response to WUTC Staff Data Request No. 5, UTC Docket Nos. UE-960612 and UE-960613. However, the revenue losses to PSE were then estimated at $3.6 to $4 million over the terms of the Special Contracts. See Staff Memo (James W. Miernyk) dated June 7, 1996, UTC Docket Nos. UE-960612 and UE-960613. Through April of this year, the revenue losses to PSE (and benefits to GP and BCS) have been more than double that estimate. See Gaines Emergency Aff. at ¶ 24.

48. Complainants would have the Commission upset this allocation of risks and benefits, to the detriment of PSE's shareholders and other customers. Neither PSE nor its other customers should be asked to subsidize the Complainants. This is not what was intended nor what is provided by the Special Contracts. Complainants' proposed remedies would impair PSE's contract rights, and, for the reasons noted below, would effect an unconstitutional taking.

c. The relief requested would also impair substantial rights secured to PSE by the Merger Order

49. On February 5, 1997, the Commission approved the Merger Plan for PSE (from the entities then known as Puget Sound Power & Light Company and Washington Natural Gas Company) under the terms set forth in Docket Nos. UE-951270 and UE-960195, Fourteenth Supplemental Order Accepting Stipulation; Approving Merger ("Merger Order"). In the Merger Order, PSE's rates were frozen from 1997 through 2001. The rate plan

approved in the Commission's Merger Order factors in the risks and potential rewards of a five-year rate freeze:

> Considering these cost pressures and the potential for savings associated with the merger, the Rate Plan reflects the implicit balance struck by the stipulating parties between five years of "rate certainty" for [core] customers, and five years of opportunity for the company to manage its resource cost pressures.

Merger Order at 21.

50. Thus, the risk of increased PSE costs was allocated to PSE rather than its customers during the five-year rate freeze. However, PSE thereby obtained the corresponding commitment that PSE's shareholders would retain the benefits of increased efficiencies, decreased costs, and other management decisions during the rate stability period. See id. at 13, 21-22 ("Within the five-year window, PSE's financial results will be a function of management's ability to achieve savings in order to provide shareholders with an opportunity to earn a reasonable rate on investment"), 26-27, Stipulation p. 4.

51. In issuing the Merger Order, the Commission actively considered the issue of special contracts and market-based pricing for certain customers, and the fact that PSE bore the risk of revenue fluctuations due to market volatility. Both Commission Staff and Public Counsel presented testimony on this issue. See Staff Testimony (Ex. T-176, pp. 10-11, Ex. 177, lines 52-58; Public Council Testimony (Ex. T-219).

52. Selectively altering this balance takes away benefits from PSE secured by the Merger Order. GP and BCS had enough power and sophistication to demand the benefits and accept the customer risks of Special Contracts. The Merger Order assigns the seller's rate risks of the Special Contracts to PSE during the five-year rate freeze. Any change in the pricing principle for these Special Contracts during the rate freeze without PSE's consent would be a violation of the Merger Order.

53. Moreover, since early 1997, PSE has relied on the Commission's Merger Order and the Special Contracts approved by the Commission. PSE has configured and configures its power portfolio, including short-term purchases and sales of power, in anticipation of, on the one hand, its commitments to core customers and, on the other hand, in anticipation of future demand reflected in market-based or variable-price contracts. Under the Merger Order and Special Contracts, PSE has understood that its shareholders are at risk during the rate stability period if PSE's portfolio planning results in lost revenues, but PSE has also anticipated that its shareholders would benefit from increased revenues during the rate stability period obtained through wise or fortuitous portfolio planning. PSE has also relied on the Merger Order and the Special Contracts in making short-term purchases and sales of power and financial swap transactions to decrease the downside risk to PSE of power market volatility. See Affidavit of William A. Gaines In Support of Phase I Motion for Summary Determination, filed herewith ("Gaines Phase I Aff.") at ¶ 3.

54. If the Commission were to fail to enforce the pricing mechanism of the Special Contracts, that would violate the bargain struck with PSE in the merger. It essentially would deny to PSE the upside value of actions taken by PSE in reliance on the Merger Order, after assigning all of the downside risk to PSE of fluctuations with respect to PSE's costs and market prices.

55. In other contexts, the courts have consistently held that, as between shareholders and ratepayers, the "party that bore the risk of loss is the party entitled to the capital gains" and that "those who bear the financial burden of particular utility activity should also reap the benefits resulting therefrom." Illinois Public Telecoms. Ass'n v. FCC, 117 F.3d 555, 569 (D.C. Cir. 1997); accord Montana Power Co. v. FERC, 599 F.2d 295 (9th Cir. 1979). Under the Merger Order, PSE has borne and continues to bear the risks of the

Special Contracts. In exchange, PSE's shareholders are entitled to any benefits that the Special Contracts provide.

56. To change that component of the Merger Order is inherently unfair to PSE. PSE relied on the Merger Order and agreed to bear (and has borne) the risk of downward market index fluctuations under these Special Contracts and the other risks inherent in the rate stability plan under the terms approved in the Merger Order. A change that allows GP and BCS to keep the benefits they have secured to date under the Special Contracts, and then allows them to avoid the (perhaps temporary) burdens of those contracts, is inherently inequitable. See FPC v. Sierra Pacific Power Co., 350 U.S. 348 (1956) (the Federal Power Commission was not justified in accepting a tariff filing by Pacific Gas & Electric that abrogated a private contract between the generating utility and a distribution company where the generating utility had voluntarily agreed by contract to a rate affording less than a fair rate of return; having voluntarily entering into such a contract, the party is not entitled to be relieved of its improvident bargain).

57. Such action by the Commission would also constitute unlawful retroactive ratemaking by essentially forcing PSE to give up gains it might otherwise obtain (or, in this case, to stem the losses it will otherwise incur) during the rate stability period imposed in the Merger Order. See, e.g., Board of Pub. Util. Comm'rs v. New York Tel. Co., 271 U.S. 23, 31 (1926); Petition of Elizabethtown Water Co., 527 A.2d 354, 358 (N.J. 1987); Indiana Pub. Serv. Comm'n v. City of Indianapolis, 131 N.E.2d 308, 315 (Ind. 1956); Puget Sound Navigation Co. v. Department of Public Works, 157 Wash. 557, 561-62, 289 P. 1006 (1930), aff'd., 160 Wash. 703 (1931).

58. In no way, to date, have these Special Contracts provided a windfall to PSE. On the contrary, prior to the recent market shifts, PSE's revenues under the Special Contracts

were far short of the projections used in fashioning the Merger Order. To abrogate GP's and BCS's Special Contract obligations by granting them a new pricing mechanism, after they have reaped enormous benefits under those same contracts for the past four years, would be arbitrary, capricious and confiscatory. It would operate under the current circumstances to unconstitutionally take PSE's property and impair PSE's rights under the Merger Order and its Special Contracts with GP and BCS.

59. A taking occurs when government action forces some private persons alone to shoulder affirmative public burdens which, in all fairness and justice, should be borne by the public as a whole. Mission Springs, Inc. v. City of Spokane 134 Wn.2d 947, 964, 954 P.2d 250 (1998). Here, GP and BCS allege they are suffering losses, and that surrounding communities and other businesses are at risk of loss of jobs and production due to energy prices under the Special Contracts. They are essentially arguing that PSE should bear the burden of subsidizing their respective operations so as to protect their (GP's and BCS's) shareholders, employees and customers. However, if shareholders are to bear such burdens, those shareholders should logically be the owners of GP and BCS. If PSE is forced to bear them, a taking will have occurred.

60. In Duquesne Light Co. v. Barasch, 488 U.S. 299 (1989), the Supreme Court observed that a ratemaking agency must allow utilities the opportunity for recovery of capital and a return on investment, and cannot arbitrarily switch methodology in a way that precludes such recovery:

> [a] State's decision to arbitrarily switch back and forth between methodology in a way which required investors to bear the risk of bad investments at some times while denying them the benefit of good investments at others would raise serious constitutional questions.

488 U.S. at 315. See also South Central Bell Tel. Co. v. Louisiana Public Service Comm'n,

594 So.2d 357, 366 (La. 1992) ("the Commission switched back and forth between methodologies in a way that deprived investors of any benefit of appreciation in their property value").

3. Conclusion With Respect to Dismissal of Complainant's Power Pricing Claims

61. For the reasons set forth above, PSE is entitled to summary determination in its favor dismissing all of Complainants' claims related to power pricing, and a ruling that "Optional Price Stability" under the Special Contracts is a provision that only pertains to price stability, and the parties' ability to negotiate price stability thereunder, and does not pertain to other services, in particular, buy/sell transactions or any other form of retail wheeling arrangements.

C. Even if the Commission Determines That PSE Is Not Entitled to Summary Determination on All Phase I Issues, the Commission Should Narrow the Scope of These Proceedings by Ruling That the Complainants Are Not Entitled to Embedded Cost Resources, or to Power at Prices Based Upon Costs to PSE of Purchasing Power or Generating Power

62. In their prayer for relief, the Complainants assert a desire for a "pricing methodology" that will "price contract energy as it is priced in competitive markets." Complaint at 9. However, the Complainants then include a request that the Commission:

> order that energy commodity pricing…be set equal to a payment which represents the estimated cost to PSE of operating its least efficient power plant, the Whitehorn simple-cycle combustion turbine (estimated at 40.15 mills/KWh).

Id.

63. The costs to PSE of purchasing power or generating power through its own resources are not relevant to the price for power under the Special Contracts. The Commission should dismiss this request for relief as a matter of law, and rule that matters

related to PSE's costs (or estimated costs) of generating or purchasing power or any request for cost-based pricing are outside the scope of these proceedings.

64. The Special Contracts do not, in any way, refer to PSE's costs of purchasing or generating power. See Schedule RTP at I (Definitions: "Non Firm Energy").

65. Nothing in the Commission's Special Contract Orders, its Merger Order, or its orders regarding Schedule 48, supports any claim that PSE's generation or power purchase costs are relevant to determining the price the Complainants should pay during the term of the Special Contracts. Indeed, as described above, all of these orders assign the risk of increased *market based* prices to the Complainants. In its recent Air Liquide decision, the Commission explicitly rejected the proposition that power charges under Schedule 48 should match PSE's energy acquisition costs. See Air Liquide, 1999 Wash. UTC LEXIS at *55-56.

66. In addition, the Special Contract Orders explicitly prohibit any claim that the Complainants are entitled to any expectation of cost-based pricing. See Special Contract Orders at 4.

67. PSE is not obligated to include, has not included, and is not including power to be provided to BCS or GP under the Special Contracts in its long-term resource planning, and PSE has understood that these customers are no longer core customers. Thus, for example, PSE's 2000-2001 Gas and Electric Least Cost Plan ("LCP"), explicitly states: "Schedule 48 and Special Contract loads were not included in the analysis since PSE is not required to acquire long-term resources to meet these loads." See Gaines Phase I Aff. at ¶ 4.

68. With respect to the Complainants' reference to Whitehorn costs, PSE's resource costs, including but not limited to the costs for operating its Whitehorn combustion turbine generation, are not the equivalent of any Dow Jones Mid-Columbia index, or any other market index. Moreover, the benefits from these resources, including but not limited to

the Whitehorn combustion turbine generation, are already committed to PSE's core customers and shareholders. See Gaines Phase I Aff. at ¶ 5. It would be a fundamental betrayal of PSE's core customers and shareholders to permit non-core customers access to Whitehorn (or other PSE generation or power purchases) at cost-based rates at this time, simply because customers who elected to escape embedded-cost pricing and obtain power at market prices no longer like the recent high market prices.

69. Thus, providing the Complainants with access to pricing based on PSE's resources or power purchases or a new pricing mechanism based on PSE's resource costs would be inconsistent with the Special Contracts, inconsistent with the Commission's orders permitting the Special Contracts to go into effect, inconsistent with the Merger Order and the Commission's Schedule 48 orders, inconsistent with PSE's resource planning, and prejudicial to the interests of PSE's shareholders and core customers. GP and BCS simply are not entitled to any relief that is based upon the cost of power from PSE's generation or purchases, or that is based upon the availability of such power.

70. The Commission should therefore rule that issues related to the cost of power from PSE's generation and purchases, as well as the availability of such generation or purchases to deliver power to GP and BCS, are not relevant to this proceeding. The Commission should also narrow the scope of these proceedings to exclude any consideration of PSE's generation or power purchases.

IV. CONCLUSION

71. For the reasons set forth above, PSE respectfully requests that the Commission dismiss the Complaint, with prejudice, as to all Phase I, power pricing issues.

72. In the alternative, PSE respectfully requests that the Commission enter an order that:

A. Dismisses the Complainants' request for a price set by reference to PSE's cost of operating Whitehorn, or any other PSE generation or power purchase; and

B. Rules that matters related to cost-based pricing, PSE's costs of generating or purchasing power, or the availability of power purchases or generation from PSE, are outside the scope of these proceedings.

C. Rules that "Optional Price Stability" under the Special Contracts is a provision that only pertains to price stability, and the parties' ability to negotiate price stability thereunder, and does not pertain to other services, in particular, buy/sell transactions or any other form of retail wheeling arrangements.

DATED: July ___, 2000.

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By _____
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CERTIFICATE OF SERVICE
Docket Nos. UE-001014 and UE-000735

I hereby certify that I have this day served the foregoing document and the Affidavit of William A. Gaines in Support of Phase I Motion for Summary Determination, upon all parties of record in this proceeding, by facsimile and U.S. mail, postage prepaid, to:

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