Q. Please state your name and business address.

A. My name is Roland C. Martin; my business address is 1300 South Evergreen Park Drive SW, Olympia, Washington 98504.

Q. By whom are you employed and in what capacity?

A. I am employed by the Washington Utilities and Transportation Commission (WUTC) as a Regulatory Consultant in the Electric Section.

Q. Have you prepared an exhibit which describes your educational background and professional experience?

A. Yes, I have. Exhibit No. 403 (RCM-1) is that exhibit.

Q. What is the purpose of your testimony in these consolidated proceedings?

A. I address the accounting and ratemaking proposals by PacifiCorp, Avista and Puget Sound Energy relating to the gain from the sale of their interests in the Centralia facilities. My testimony is composed of individual sections devoted to each utility because of variations in their respective proposals.

I - PacifiCorp

Q. What aspects of PacifiCorp's application are you addressing?

A. I address PacifiCorp's calculation of the gain from the sale of its share in the Centralia Plant, the proposed sharing of the gain between shareholders and customers, and the proposed ratemaking treatment related to the portion of the gain allocated to customers.

Q. Please describe your understanding of the gain as calculated and presented by the Company.

A. Mr. Miller presents in Exhibit No. 208 the calculation of an estimated net book gain of $82,662,795 from the sale of PacifiCorp's 47.5% share of the Centralia facilities. This is an estimate because a number of elements and assumptions in the calculation may change, such as the amounts of plant balances and expenses associated with the sale. PacifiCorp should be directed to refile the details of the transaction after closing based on known facts for further Commission review and consideration.

Q. Does Staff have specific exceptions regarding the Company's gain calculation presented in Exhibit 208?

A. Yes. First, the Company included in the gain calculation accruals for plant and mine environmental liabilities in the amounts of $2,000,000 and $3,000,000, respectively. These amounts represent expenses PacifiCorp may incur in the future as a result of previous ownership of the plant and mine. These costs are unknown and speculative, and should be excluded from the gain calculation. Exclusion of these amounts is consistent with the Commission's decision in Docket No. UE-990267 involving the sale of PSE's share of the Colstrip facilities. The Company may file for a petition seeking the appropriate regulatory treatment to be accorded the environmental remediation costs when they become known.

Second, PacifiCorp has not included in the gain analysis the excess deferred federal income taxes related to Centralia which is estimated to be $5.9 million. If PacifiCorp is able to obtain a favorable ruling from the Internal Revenue Service permitting pass-through of excess deferred taxes as part of the net gain, the gain will be higher by the same amount. Staff recommends that Commission direct the Company to seek such a ruling from the IRS, consistent with the directive given PSE in Docket No. UE-990267.

Q. Please describe briefly PacifiCorp's proposal with respect to disposition of the net gain of approximately $83 million.

A. PacifiCorp proposes to assign approximately 36% of the net gain to shareholders and 64% to customers. The 64% is the percentage relationship between depreciation reserve to gross plant, while the 36% is the relationship of net plant to gross plant. The 64% allocation to customers equates to approximately $53 million, which the Company proposes be used to offset booked generation-related regulatory assets. This treatment effectively reduces rate base.

Q. What is Staff's recommendation with respect to the net gain from the sale of PacifiCorp's share of Centralia?

A. Staff recommends rejection of the Company's proposed assignment of a portion of the gain to shareholders. Instead, the Commission should pass through the entire net gain to ratepayers, for the reasons explained in Mr. Elgin's testimony. The precise method to flow-through the entire gain to ratepayers would be determined in PacifiCorp's pending general rate proceeding, Docket No. UE-991832.

Q. In addition to Mr. Elgin's testimony, what other guidelines support the Staff proposal for full flow-through of the gain to ratepayers?

A. The parties to the Stipulation and Order of Dismissal dated May 26, 1992, in Washington Court of Appeals No. 29404-1 embraced the Commission's adoption of an adjustment in Docket U-89-2688-T involving Puget Sound Power & Light Company (Puget), that gave the property sales gain/loss to the customer, based on an allocation reflecting the time the property was included in ratebase. Specifically, paragraph 6 of that Stipulation provided in part: "The amount to be allocated to the customer in future rate cases will be based on the amount of time the property was included in ratebase in relationship to the total time the property was held by the Company." Consistent with this principle, ratepayers deserve the full benefit of the gain because ratepayers have supported the Centralia facilities in rates through the date of sale.

Q. Are there prior Commission decisions that support the Staff proposal?

A. Yes. In Docket No. 87-1533-AT involving the sale of The Washington Water Power Company's (WWP) combustion turbine generator, the Commission authorized the sale based upon the premise that 100 percent of the after-tax gain was returned to the ratepayers. WWP, which is Avista's predecessor, was ordered to defer the gain on the sale into a deferred credit account until final disposition of the gain was determined in its next general rate case.

Q. Included in the Company's proposal is the use of the customer portion of the gain to write-off generation-related assets. Please comment on this aspect of the proposal by the Company.

A. Staff does not necessarily disagree with the idea that the portion of the gain accruing to ratepayers (100% under Staff's recommendation) may be used to offset certain regulatory assets that are determined to be recoverable in rates. The application of the gain as an offset to regulatory assets is one of the many potential methods of disposition of the gain that will accomplish flow-through of benefits to customers. To ensure that all of the broader aspects of ratemaking are considered, however, the determination of the appropriate benefit pass-through methodology, as well as the recoverability of regulatory assets to be potentially offset by the gain, are best addressed in the general rate proceeding.

II- Avista Corp.

Q. What aspects of Avista's application are you addressing?

A I address Avista's proposal to retain all of the book gain from the sale of its share of the Centralia facilities. I also address Avista's alternative proposal to offset certain costs with the gain allocated to customers under a gain-sharing approach similar to PacifiCorp's.

Q. Please describe your understanding of the gain as calculated and presented by the Company.

A. Mr. McKenzie presents in Exhibit No. 312 the calculation of an estimated net book gain of $29,605,503 from the sale of Avista's 15% share of the Centralia facilities. Similar to PacifiCorp, this is an estimate because a number of elements and factors in the calculation may change, such as the closing date of the sale, and the true up of estimates to actuals once actual information is available, as explained in his testimony. Avista should also be directed to refile the details of the transaction after closing based on known facts for further Commission review and consideration.

Q. Please describe briefly Avista's proposal with respect to the net gain of $29,600,000.

A. Avista proposes to assign all of the gain to shareholders. However, if the Commission were to allocate a portion of the gain to customers based on the method proposed by PacifiCorp, Avista proposes to offset the gain allocated to customers against the costs of storm damage resulting from Ice Storm 1996. Any remaining gain would be applied against the transition obligation under accounting standards for post-retirement benefits other than pensions.

Q. What is Staff's recommendation with respect to the net gain from the sale of Avista's share of Centralia?

A. Staff recommends rejection of the Company's proposed assignment of the entire gain to shareholders. Staff further recommends rejection of the proposal to allocate the gain between customers and shareholders. Staff proposes to pass through the entire net gain to ratepayers, for the reasons explained in Mr. Elgin's testimony. Consistent with the

Staff recommendation for PacifiCorp, the method to flow-through the gain to ratepayers would be determined in Avista's pending general rate proceeding, Docket No. UE-991606.

Q. In addition to Mr. Elgin's testimony, what other guidelines support the Staff proposal for full flow-through of the gain to ratepayers?

A. In my testimony concerning PacifiCorp, I discussed the principle embodied in the Stipulation and Order of Dismissal dated May 26, 1992, in Washington Court of Appeals No. 29404-1 and Docket No. 87-1533-AT involving the sale of The Washington Water Power Company's (WWP) combustion turbine generator. These same principles support Staff's recommendation concerning Avista's proposal to flow the entire gain to shareholders.

Q. Anticipating that the Commission rejects Avista's proposal for full assignment of the gain to shareholders, Avista claims that shareholders, at a minimum, should retain a portion of the gain that is proportional to the un-depreciated amount of the Centralia investment. Please comment on this proposal by the company.

A. As I stated earlier for PacifiCorp, Staff opposes the depreciation-based methodology because it does not give the entire gain to the ratepayers. However, Staff does not necessarily disagree that the portion of the gain accruing to ratepayers (100% under Staff's recommendation) may be used to offset certain regulatory assets that are determined to be recoverable in rates. This is one of the many potential methods of disposition of the gain that will flow the benefits to customers. However, all aspects of ratemaking should be considered simultaneously. Therefore, the appropriate benefit pass-through methodology, as well as the recoverability of regulatory assets to be potentially offset by the gain, are best addressed in Avista's pending general rate proceeding.

III- PSE

Q. What aspects of PSE's application are you addressing?

A. I address PSE's request to amortize the gain from the sale of Centralia for ratemaking purposes over the five-year period commencing on January 1, 2000. Staff recommends rejection of the Company's amortization proposal. Instead, PSE should defer the entire gain, with a return equal to 7.16% compounded annually, until its next general case to ensure that the gain from the disposition of the facilities accrues to ratepayers.

Staff witness Alan Buckley presents testimony and exhibits demonstrating that there are short-term power cost benefits of the sale. Similar to Staff's proposal in Docket No. UE-990267 regarding the sale of Colstrip facilities, Staff recommends that the benefits identified by Mr. Buckley be deferred for ratepayers without true-up, with a return accruing on the balance compounded annually.

Q. Please describe your understanding of the gain as calculated and presented by the Company.

A. Mr. Karzmar presents in Exhibit No. 109 the calculation of an estimated book gain of $13,520,313 from the sale of PSE's share of the Centralia facilities. This is an estimate because a number of elements in the calculation may change, including the amounts of plant balances and expenses, as explained in his testimony. The $13.5 million is an estimate based on a closing date of December 31, 1999. PSE should also be directed to refile the details of the transaction based on known facts for further Commission review and consideration.

Q. Please describe briefly PSE's proposal with respect to the net gain of $13,520,313.

A. PSE proposes to amortize this gain over a five-year period commencing January 1, 2000, to Account 421.1, Gain on Disposition of Property. The taxes associated with the gain would be amortized to Account 410.2, Provision for deferred income taxes, other income and deductions. These are both below-the-line accounts. The proposal ensures that approximately 40% of the net gain is amortized during the Merger rate plan period for the benefit of shareholders.

Q. Is Staff's recommendation with respect to the net gain from the sale of PSE's share of Centralia consistent with the Merger rate plan that was approved by the Commission in Docket UE-960195?

A. Yes. The Merger Stipulation and Order specifically provided that associated gains or losses from property transactions during the rate plan period that are a direct result of the Merger, shall be included in PSE's current earnings (rather than deferred).

The properties presented in the Merger proceeding which were contemplated to be disposed of to achieve Merger synergies did not include production and transmission facilities in general, or the Centralia facilities in particular. It included distribution facilities and general plant such as headquarter assets, service centers and warehouses. The sale of the Centralia facilities, therefore, is not a direct result of the merger. Furthermore, at page 18 of the Commission's 3rd Supplemental Order in Docket UE-990267 involving the sale of PSE's share of Colstrip facilities, the Commission made it explicit that "its order approving the merger did not grant PSE permission to sell used and useful generation assets as a power cost savings".

Q. Does Staff propose a deferral mechanism with respect to the power supply benefits, similar to the mechanism proposed in Docket No. UE-990267 involving the sale of PSE's share in the Colstrip facilities?

A. Yes. The amounts of power cost benefits measured by Mr. Buckley would be deferred in a regulatory liability account and would not be subject to true-up. The lack of a true-up is different than the Commission's directive for Colstrip, for the reasons explained by Mr. Buckley in his testimony. The balance will accrue an annual return equal to the 7.16% determined to be an appropriate rate for PSE in the Colstrip sale, compounded annually. Similar to the deferral of the gain, the deferred benefits will be passed through to the ratepayers using an appropriate method determined in the next rate proceeding.

Q Do you have additional comment and recommendation with respect to the proposals of PacifiCorp, Avista, and PSE?

Q. Yes. If for some reason the Commission finds that there is a basis for gain sharing based on a method such as depreciation-based methodology or Merger rate plan period amortization, the Commission should limit the amount of benefit that is subject to such sharing. The gain subject to sharing should exclude an amount equal to the utilities' respective share of the accrued reclamation balance at closing date. That reclamation amount should be assigned in full to ratepayers. The estimated reclamation balances prior to tax considerations, projected to December 31, 1999, for PacifiCorp, Avista, and PSE which are subject to true-up, are $25.3 million, $10.3 million, and $4.1 million, respectively. These amounts in the reclamation trust funds are fuel costs included in Centralia operating costs and, thus, a component embedded in rates paid by the customers. Because the reclamation liability is transferred to the buyer, the benefit of reversal of the reclamation liability should not be subject to sharing. It should accrue to ratepayers who shouldered the reclamation cost accruals.

Q. Does that conclude your direct testimony concerning the applications of PacifiCorp, Avista, and PSE?

A. Yes.