

0799

1 BEFORE THE WASHINGTON UTILITIES AND
2 TRANSPORTATION COMMISSION

3 WASHINGTON UTILITIES AND)
4 TRANSPORTATION COMMISSION,)
5 Complainant,)DOCKET NO. UG-040640
6 vs.)DOCKET NO. UE-040641
7 PUGET SOUND ENERGY, INC.,)
8 Respondent.)Volume VI
9)Pages 799-1014
10)
11 In the Matter of the Petition)
12 of PUGET SOUND ENERGY, INC.,)
13 For an Order Regarding the)
14 Accounting Treatment for)DOCKET NO.
15 Certain Costs of the Company's)UE-031471
16 Power Cost Only Rate Filing,)
17)
18 In the Matter of the Petition)
19 of PUGET SOUND ENERGY, INC.,)
20 For an Accounting Order)
21 Authorizing Deferral and)DOCKET NO.
22 Recovery of Investment and)UE-032043
23 Costs Related to the White)
24 River Hydroelectric Project.)
25)

16
17 A hearing in the above matter was held on
18 December 16, 2004, at 9:30 a.m., at 1300 South
19 Evergreen Park Drive Southwest, Room 206, Olympia,
20 Washington, before ADMINISTRATIVE LAW JUDGE DENNIS
21 MOSS and CHAIRWOMAN MARILYN SHOWALTER and
22 COMMISSIONER RICHARD HEMSTAD, and COMMISSIONER
23 PATRICK OSHIE.
24
25 Deborah L. Cook, RPR, CSR
Court Reporter

0800

1 The parties were present as follows:

2 THE COMMISSION, by ROBERT D. CEDARBAUM,
3 Assistant Attorney General, 1400 South Evergreen
4 Park Drive Southwest, Post Office Box 40128,
5 Olympia, Washington 98504-0128, Telephone
6 (360) 664-1188, Fax (360) 586-5522, E-mail,
7 bcedarba@wutc.wa.gov.

8 THE PUBLIC, by SIMON J. FFITCH, Assistant
9 Attorney General, 900 Fourth Avenue, Suite 2000,
10 Seattle, Washington, 98164-1012, Telephone (206)
11 389-2055, Facsimile (206) 389-2058, E-mail
12 simonf@atg.wa.gov.

13 PUGET SOUND ENERGY, by KIRSTIN S. DODGE,
14 Attorney at Law, Perkins Coie, LLP, 10885 Northeast
15 Fourth Street, Suite 700, Bellevue, Washington
16 98004, Telephone (425) 635-1407, Fax (425) 635-2407,
17 E-Mail kdodge@perkinscoie.com; and by JASON KUZMA,
18 Attorney at Law, Perkins Coie, LLP, 10885 Northeast
19 Fourth Street, Suite 700, Bellevue, Washington
20 98004, Telephone (425) 635-1407, Fax (425) 635-2407,
21 E-Mail, jkuzma@perkinscoie.com.

22 INDUSTRIAL CUSTOMERS OF NORTHWEST UTILITIES by
23 S. BRADLEY VAN CLEVE, Attorney at Law, Davison Van
24 Cleve, 1000 Southwest Broadway, Suite 2460,
25 Portland, Oregon, 97205, Telephone, (503) 241-7242,
26 Fax (503) 241-8160, E-mail mail@dvclaw.com

27 NORTHWEST INDUSTRIAL GAS USERS, by EDWARD
28 A. FINKLEA, Attorney at Law, Cable Huston
29 Benedict Haagesen & Lloyd, LLP, 1001 Southwest
30 Fifth Avenue, Suite 2000, Portland, Oregon
31 97204, Telephone (503) 224-3092, Fax
32 (503) 224-3176, E-Mail efinklea@chbh.com.

33

34

35

36

37

0801

1 -----

2 INDEX OF EXAMINATION

3 -----

4	WITNESS:	PAGE
5	MICHAEL PARVINEN	
6	Direct Examination by Mr. Cedarbaum	805
7	Cross Examination by Ms. Dodge	806
8	Examination by Chairwoman Showalter	813
9	Examination by Commissioner Oshie	817
10	Examination by Judge Moss	818
11	Recross Examination by Ms. Dodge	818
12	Redirect Examination by Mr. Cedarbaum	819
13	Recross Examination by Ms. Dodge	821
14		
15	JAMES RUSSELL	
16	Direct Examination by Mr. Cedarbaum	822
17	Cross Examination by Mr. Van Cleve	824
18	Cross Examination by Ms. Dodge	831
19	Examination by Chairwoman Showalter	851
20	Examination by Commissioner Hemstad	856
21	Examination by Commissioner Oshie	858
22	Recross Examination by Ms. Dodge	860
23	Redirect Examination by Mr. Cedarbaum	862
24		
25		

0802

1 -----

2 INDEX OF EXAMINATION

3 -----

4	WITNESS:	PAGE
5	JULIA RYAN	
6	Direct Examination by Ms. Dodge	865
7	Cross Examination by Mr. Van Cleve	867
8	Cross Examination by Mr. Cedarbaum	889
9	Examination by Chairwoman Showalter	900
10	Examinatin by Commissioner Hemstad	931
11	Examination by Commissioner Oshie	935
12	(Separate, Confidential Record)	945-951
13	Examination by Judge Moss	948
14	Redirect Examination by Ms. Dodge	952
15		
16	DONALD SCHOENBECK	
17	Direct Examination by Mr. Van Cleve	959
18	Cross Examination by Ms. Dodge	961
19	Examination by Chairwoman Showalter	965
20	Examination by Commissioner Hemstad	978
21	Further Examination by Chairwoman Showalter	981
22	Examination by Commissioner Oshie	991
23	Further Examination by Chairwoman Showalter	993
24	Examination by Judge Moss	999
25	Recross Examination by Mr. Cedarbaum	1001

0803

1 -----

2 INDEX OF EXHIBITS

3 -----

4	EXHIBIT	RECEIVED
5	PUGET SOUND	
6	71 to 96, 107	867
7	97 to 103 C	888
8	108 MARKED	958
9	104 to 106	900
10	STAFF	
11	441 TO 444	806
12	421 TO 427	824
13	428 TO 435	862
14	PUBLIC COUNSEL	
15	227	1013
16	ICNU	
17	371 HC TO 387	960
18	390 TO 391	965
19	BENCH	
20	4 TO 9, 11 TO 13	1003
21	BENCH REQUESTS	
22	No. X	885
23	No. 8	983
24	No. 9	1002
25		

1
2
3
4
5
6
7
8
9
10
11
12
13
14
15
16
17
18
19
20
21
22
23
24
25

PROCEEDINGS

JUDGE MOSS: Mr. Finklea, you are joining us for the first time. If you would just enter your appearance for the record.

MR. FINKLEA: Yes, thank you. I am Edward Finklea of Cable Houston, and I represent the Northwest Industrial Gas Users. My associate, Chad Stokes, made an appearance on Monday. And thank you for having me at the hearing today.

JUDGE MOSS: Thank you for joining us today.

Mr. Parvinen, if you will stand and raise your right hand.

MICHAEL P. PARVINEN,
produced as a witness in behalf of the Staff, having been first duly sworn, was examined and testified as follows:

JUDGE MOSS: Please be seated and thank you.

0805

1 DIRECT EXAMINATION

2

3 BY MR. CEDARBAUM:

4 Q If you could state your name, and spell
5 the last name please?

6 A Michael P. Parvinen, P-a-r-v-i-n-e-n.

7 Q And you are part of a Staff presentation
8 in this proceeding; is that correct?

9 A Yes.

10 Q If I could direct your attention to what
11 has been marked for identification as Exhibit
12 441. Does that exhibit constitute your direct
13 testimony in this proceeding?

14 A Yes, it does.

15 Q And associated with your direct testimony
16 are exhibits for identification numbers 442
17 through 444; is that correct?

18 A Yes.

19 Q And was your direct testimony in all of
20 those accompanying exhibits, were they prepared
21 by you or under your supervision and direction?

22 A Yes.

23 Q Are they true and correct to the best of
24 your knowledge and belief?

25 A Yes.

0806

1 MR. CEDARBAUM: Thank you. I would offer
2 441 through 444.

3 JUDGE MOSS: Hearing no objection, those
4 will be admitted. Thank you.

5 (EXHIBIT 441 to 444 RECEIVED.)

6 JUDGE MOSS: And the designee for PSE is
7 for 20 minutes. Ms. Dodge, proceed.

8

9 CROSS EXAMINATION

10

11 BY MS. DODGE:

12 Q Mr. Parvinen, would you turn to your
13 testimony 441 at page 11?

14 A (Complies.)

15 Q I would like to ask you about your
16 adjustment 2.06, bad debts.

17 A All right.

18 Q Are you familiar with the history of
19 treatment of bad debt expenses in the company's
20 recent rate cases?

21 A Generally.

22 Q Is it correct that prior to the settlement
23 of the 2001 rate case bad debt expense was
24 normalized by looking at the five-year history of
25 actual bad debts, throwing out the low and high

0807

1 year, and averaging the three remaining years?

2 A I am not sure if that treatment, throwing
3 out the high and low, has been done in the past.
4 I know it has been normalized. I think over the
5 history it also has been adjusted to actual. The
6 theory is to just try to set a bad debts level
7 that is representative of what it will be in the
8 rate year.

9 Q And as part of the settlement of the 2001
10 rate case, is it correct that bad debt expense
11 for that case used the actual test year amount?

12 A I believe that's correct, yes.

13 Q And consistent with the settlement of the
14 2001 case, the Company's original filing in this
15 case used the actual bad debts for the test year,
16 the year ending September 30 2003; is that right?

17 A That's correct.

18 Q But rather than using the Company's bad
19 debt expense from the test year, or returning to
20 the historical approach of averaging the test
21 year with other years, you have chosen a
22 different approach in this case to recommend?

23 A Yes. Our recommendation was to use a
24 three-year average.

25 Q And that is the years ended September 2000

0808

1 through 2002?

2 A Yes.

3 Q Your approach excludes the test year all
4 together, doesn't it, because as you state you
5 view it as being abnormally high?

6 A Yes.

7 Q However, your method does not include any
8 year during which bad debt expenses were lower
9 than other years, does it?

10 A If one of the three years that I used was
11 abnormally low, I guess it would be included. I
12 didn't notice that any of those three years were
13 abnormally low.

14 Let me point out that in the Company's
15 rebuttal case they had proposed using a method,
16 as you had described, using a five-year average,
17 throwing out the high year and the low year, or
18 using a three-year average based on the last five
19 years removing the highest year and the lowest
20 year, and averaging the three.

21 Staff has no problem with that method.

22 We would agree with that, and I think going
23 forward most likely that would produce a good
24 result. And for consistency purposes, that would
25 be a method that we would propose going forward

0809

1 unless by chance it produced a result that wasn't
2 consistent. So I guess on brief we would support
3 the Company's rebuttal method.

4 Q Thank you. Let's move then to page 12 of
5 your testimony, adjustment 2.07, the
6 miscellaneous operating expenses. And in
7 particular, the incentive payment issue.

8 A Okay.

9 Q I would also like you to have in front of
10 you, if you would, Exhibit 337. We will hand
11 them up. And -- 337. And this was a workpaper
12 that was discussed with respect to Mr. Hunt's
13 testimony.

14 A Yes.

15 Q And in addition, Exhibit 333, which was
16 Mr. Hunt's testimony. And if you would turn to
17 page 3 of that Exhibit 333.

18 A (Complies.) Okay.

19 Q Now, Exhibit 337 is mostly just for your
20 reference. But as I understand it, this is the
21 workpaper that shows how the Company developed
22 the amount for the test year for the incentive
23 plan expense; is that right?

24 A That's correct.

25 Q The Company's development of its test year

0810

1 amount in a sense normalized the incentive plan
2 expense, didn't it, in that it allocated three
3 months from its 2002 expense and nine months from
4 its 2003 expense in order to come up with a test
5 year incentive plan expense; is that right?

6 A I wouldn't characterize it as normalizing.
7 But the method that you identified is correct,
8 yes.

9 Q Rather than using the Company's incentive
10 payment expense from the test year, you have
11 chosen to propose the incentive payment
12 expense -- an incentive payment expense that fell
13 entirely out of the test year; isn't that right?

14 A No. I chose the level that -- I used the
15 2004 payment so the payment was outside the test
16 year, but the payment was for nine months of test
17 year performance.

18 Q The expense itself that you are
19 recommending was paid in 2004 is that correct?

20 A That's correct. And it was for
21 performance done in 2003.

22 Q At page 12 of your testimony, line 8?

23 A Yes.

24 Q You state that the test year amount was
25 abnormally high compared to more recent years.

0811

1 That's not correct, is it?

2 A No, that is correct. If you look at the
3 Company's Exhibit 333 on page 3, the chart on
4 page 3, if you looked at the last three years
5 2003, 2002, and 2001, and just those three years,
6 then the 2002, which was actually the payment
7 during the test year, does look abnormally high.

8 Especially when you take that into account
9 looking at what the plan is on a going forward
10 basis. And that was the basis for that statement
11 in my testimony.

12 Q Looking at Exhibit 333, the last line of
13 page 2 and the first line of page 3, that states
14 that the test period amount that the Company has
15 proposed is \$3,440,174; is that correct?

16 A That's correct.

17 Q And that is consistent with Exhibit 337,
18 the workpaper which shows on the right-hand side
19 of the sheet under the total column after
20 allocation of three months of 2002, and nine
21 months of 2003, a total of \$3,440,174; is that
22 right?

23 A That's correct.

24 Q So the test period amount the Company is
25 seeking is the 3.4 million number, not the 6.6

0812

1 million number; isn't that right?

2 A That's right.

3 Q And it's your testimony that the \$3.4
4 million number is abnormally high compared to the
5 2 million -- 6.6 million and 2.7 million expenses
6 from 2001 through 2003?

7 A No. Just that the test period, the test
8 period amount that was booked in the test period,
9 which in this case is the 6.6 million figure was
10 abnormally high. And that's why I didn't include
11 it in the calculations of the proforma level.

12 I only used a full year of 2003, which
13 would be the 2 million 96 figure. So that's the
14 difference between the Company and the Staff on
15 this particular component of the incentive
16 mechanism, is the Company's 3.4 million versus
17 the Staff's figure of 2.0 million.

18 Q Looking again at page 3 of Exhibit 333,
19 it's correct, isn't it, that the \$2 million
20 figure that you are advocating is lower than any
21 incentive plan expense the Company has had in the
22 last five years; isn't that correct?

23 A That's correct. And that -- and the
24 reason I did use that one as opposed to trying to
25 use an average or something was based on what

0813

1 will be paid out in incentives for the year 2004,
2 paid in 2005, the rate year, which will be zero
3 because the proforma plan is tied to -- even
4 though it's got components within it tied to
5 things like customer service, the main component
6 is earnings, earnings per share.

7 And if the earnings per share does not
8 reach \$1.50, then there will be no incentive
9 payments at all. So Staff was being conservative
10 by using the \$2 million figure, because as I
11 mentioned, the Company will not achieve the
12 \$1.50; so, therefore, no payments will be made
13 for the 2004 year.

14 MS. DODGE: That's all I have for this
15 witness.

16 JUDGE MOSS: Thank you. Are there
17 questions for Mr. Parvinen from the bench?

18

19 EXAMINATION

20

21 BY CHAIRWOMAN SHOWALTER:

22 Q I am just trying to follow this argument
23 on Exhibit 333 on the chart as to what is
24 abnormally high or low. Just looking at the
25 surface chart it looks to me as if the year 2002

0814

1 is lower than two of the other years. Is the
2 issue that it's higher than average? Is that
3 what you mean by abnormally high or it's out of
4 whack?

5 A If you just looked at 2003, 2002, and
6 2001, then it looks out of whack. If you compare
7 it to the five, it looks right. If you add 2004
8 to that list, it would be zero.

9 Q 2004 is zero?

10 A Yes.

11 Q So that if we added in 2004, the average
12 would be brought down?

13 A Yes.

14 Q Right now the five-year average is 5,000
15 or so -- \$5 million or so?

16 A Right.

17 Q What hits me is that these jump all over
18 the place. That is, there's quite a bit of
19 variation in it. So how should we -- why should
20 it be one year or the other? In other words, if
21 you look at 2002, that looks higher than average.
22 If you look at 2001, it's perhaps the same amount
23 below average. I'm not sure?

24 A Yeah.

25 Q When you say one is abnormally low in the

0815

1 same manner as one is abnormally high.

2 A Yeah. The numbers change year by year
3 based on the plans. The plans, the incentive
4 plans get modified every year. They have been
5 very complex to having something like 600
6 different types or measurement components
7 whittled on down to very few items.

8 For example, in 2004 has much less
9 components, 20 something comes to mind. However,
10 none of the components matter if the Company
11 doesn't achieve a certain level of earnings.

12 Q Right. Is what we're trying to do here
13 build into the revenue requirement a certain
14 amount that would be used for bonuses should the
15 conditions apply?

16 A Staff is recommending the level in this
17 case of \$2,096,000 in two rates.

18 Q Why would it not -- why wouldn't an
19 average of some sort be appropriate?

20 A Excuse me. I have to back up. \$2 million
21 is the level that we're at here. Then Staff
22 recommended disallowing a portion of that that is
23 then tied to earnings. This would be the total
24 level of incentives that the Company would be
25 paying.

0816

1 Q In other words, part of your disallowance
2 is conceptual?

3 A Yes.

4 Q Set that aside now.

5 A All right.

6 Q In the universe at which you accept
7 conceptually there should be incentives paid, are
8 you basing it on an average? And if not, why
9 not?

10 A I'm not basing it on an average. I am
11 basing it on the most recent year as being
12 representative of a going forward level.

13 Q And then that gets me back to my question,
14 it looks to me as if no year is very
15 representative if this chart is indicative.
16 Would you agree?

17 A Well, yes, that would be true.

18 CHAIRWOMAN SHOWALTER: Okay. Thank you.

19 JUDGE MOSS: Anything further from the
20 bench?

21 COMMISSIONER OSHIE: I want to follow up,
22 because I may have missed your last answer.

23

24

25

0817

1 EXAMINATION

2

3 BY COMMISSIONER OSHIE:

4 Q But why do you believe that the most
5 recent period is the most representative going
6 forward with regard to the incentive pay?

7 A Well, as I mentioned, that's probably a
8 conservative number given that the 2004 year
9 would be zero. That will be paid in 2005. Well,
10 nothing will be paid in 2005.

11 But to encourage the Company to continue
12 to use the incentive program in an appropriate
13 manner, Staff did use the most recent year that
14 we knew at the time as a level going forward.

15 Q And if I can -- well, at least succinctly
16 state what I believe your reason for not using
17 averaging is because the incentive pay mechanisms
18 employed by the Company have changed over time.
19 In other words, the same incentive pay structures
20 that the Company was using, let's say five years
21 ago, are not in place today?

22 A That's true.

23 JUDGE MOSS: I want to clarify one point.

24

25

0818

1 EXAMINATION

2

3 BY JUDGE MOSS:

4 Q You used the word conservative a couple of
5 times. Do you mean higher or lower? That term
6 is used either way. Do you -- when you say you
7 are being conservative, do you mean you are
8 overestimating or underestimating?

9 A Well, I guess I wouldn't call it
10 estimating, but I am using a level that is higher
11 than what I could have otherwise justified. A
12 known and measurable number going forward is
13 zero, so we could have justified that number.

14 CHAIRWOMAN SHOWALTER: So if anything,
15 you are being generous to the Company, is what
16 you meant by conservative?

17 THE WITNESS: Yes.

18 JUDGE MOSS: Any follow up from the
19 bench's question?

20 MS. DODGE: I have some.

21

22 RECROSS EXAMINATION

23

24 BY MS. DODGE:

25 Q Mr. Parvinen, you are basing your

0819

1 recommendation on what you say is the known and
2 measurable fact that there will be no pay out in
3 2005 because of 2004 earnings; is that right?

4 A I could have used that for justification
5 for adjusting to zero, yes.

6 Q And you state that's because you believe
7 the Company will not meet the earnings per share
8 threshold in the plan?

9 A That's correct.

10 Q Are you aware that the earnings per share
11 threshold for purposes of the incentive plan
12 payment is before any disallowance for Tenaska is
13 taken into account?

14 A I don't recall seeing that stated in the
15 incentive plan at all, no.

16 JUDGE MOSS: Is that all you have?

17 MS. DODGE: Yes.

18 JUDGE MOSS: Any redirect?

19 MR. CEDARBAUM: Briefly.

20

21 REDIRECT EXAMINATION

22

23 BY MR. CEDARBAUM:

24 Q When we're talking about the incentive
25 plan, Mr. Parvinen, that's what is included in

0820

1 Exhibit 335. It's a company exhibit labeled 2004
2 Goals and Incentive Plan?

3 A Yes, that's correct.

4 MR. CEDARBAUM: Thank you for providing
5 him that.

6 Q BY MR. CEDARBAUM: And turning to page 3
7 of the exhibit.

8 A (Complies.)

9 Q If you direct your attention to the bottom
10 of the page, it's the second full paragraph from
11 the bottom that begins, "It is important." Do
12 you see that?

13 A Yes, I do.

14 Q Let's give everybody a chance to read
15 that.

16 A (Reading document.)

17 Q Okay. When you refer to the \$1.50
18 earnings per share incentive goal, this was the
19 basis for that statement?

20 A Yes.

21 Q And, again, you saw nothing in this
22 incentive plan with respect to Tenaska's
23 disallowance?

24 A That's right.

25 MR. CEDARBAUM: Thank you. Those are all

0821

1 my questions.

2 JUDGE MOSS: That will complete --

3 MS. DODGE: Your Honor, I do have a follow
4 up to that question.

5 JUDGE MOSS: Well, if it's just one
6 we will allow it.

7 MS. DODGE: Well, maybe two.

8

9 RECROSS EXAMINATION

10

11 BY MS. DODGE:

12 Q Mr. Parvinen, do you have any knowledge of
13 when this Goals and Incentive Plan for 2004 was
14 printed?

15 A No, I do not.

16 Q And are you aware of the date that the
17 Commission issued its orders associated with the
18 Tenaska disallowance?

19 A I honestly don't know that date either.

20 MS. DODGE: That's all.

21 JUDGE MOSS: All right. Mr. Parvinen, we
22 appreciate you giving your testimony today, and
23 with that, I believe you can step down.

24 Are we going to have Mr. Russell?

25 JUDGE MOSS: Please raise your right hand.

0822

1 JAMES M. RUSSELL,
2 produced as a witness in behalf of the Staff, having
3 been first duly sworn, was examined and testified as
4 follows:

5

6 JUDGE MOSS: Thank you. Please be seated.

7

8 DIRECT EXAMINATION

9

10 BY MR. CEDARBAUM:

11 Q If you could state your full name and
12 spell your last name?

13 A My name is James M. Russell,
14 R-u-s-s-e-l-l.

15 Q And you are also a participant, a member
16 of the Staff team presenting testimony in this
17 proceeding?

18 A Yes.

19 Q If you could direct your attention to what
20 has been marked for identification as Exhibit
21 421. Does this exhibit constitute your direct
22 testimony in this proceeding?

23 A Yes, it does.

24 Q And directing your attention to what has
25 been marked as identification as Exhibits 422

0823

1 through 427, are these exhibits that accompany
2 your direct testimony?

3 A For some reason I have 422 through 426.
4 Maybe I miss numbered mine.

5 Q JMR-2 through JMR-7?

6 A Yes. I didn't mark 7.

7 Q And with respect to both your detect
8 testimony and the accompanying exhibits, were
9 these exhibits prepared by you or under your
10 supervision or direction?

11 A Yes, they were.

12 Q And are they true and correct to the best
13 of your knowledge and belief?

14 A Except for the revisions that Mr. Yohannes
15 (sic) will be making, and the payroll item that
16 Mr. Parvinen will be making. Those flow through
17 my exhibits into the revenue requirement
18 calculation, so I would envision revising five or
19 six exhibit pages, and three or four testimony
20 pages for those revisions.

21 Q And those could be provided when
22 Dr. Mariam provides his errata pages that he
23 discussed yesterday?

24 A Correct.

25 Q And with that clarification, your exhibits

0824

1 are true and correct to the best of your
2 knowledge?

3 A Yes. Yes, they are.

4 MR. CEDARBAUM: Thank you, Your Honor. I
5 would move for the admission of Exhibits 421
6 through 427.

7 JUDGE MOSS: Hearing no objection, those
8 will be admitted.

9 (EXHIBIT 421 TO 427 RECEIVED.)

10 MR. CEDARBAUM: Mr. Russell is available
11 for cross-examination.

12 JUDGE MOSS: Before we begin that, I would
13 point out that I do have a typographical error on
14 the exhibit list and PSE's first cross exhibit is
15 428, not 728 as indicated. Other than that, I
16 think they are numbered correctly.

17 We have 10 minutes designated for ICNU,
18 and 30 for PSE. We have been having ICNU go
19 first, so we will follow that, Mr. Van Cleve.

20 MR. VAN CLEVE: Thank you, Your Honor.

21

22 CROSS EXAMINATION

23

24 BY MR. VAN CLEVE:

25 Q Good morning, Mr. Russell.

0825

1 A Good morning.

2 Q Can you refer to page 20 of your
3 testimony?

4 A I am there.

5 Q And at line 1 you state that the Company
6 is booking its 2004 rate case costs as a
7 regulatory asset; is that right?

8 A Yes.

9 Q And down at the bottom of the page
10 starting at line 17, you give your recommendation
11 for the treatment of the 2004 rate case costs in
12 this case; is that right?

13 A Yes.

14 Q And you are proposing that the costs be
15 normalized?

16 A Well, for 2004 rate case costs, I am
17 proposing that the amount the Company incurs
18 through August of 2004 be deferred and amortized,
19 and then the remaining expenditures after that
20 date be normalized.

21 Q Now, the proposal to amortize part of the
22 costs and normalize part of the costs raised the
23 same double counting issue that you raised with
24 respect to the PCORC expense?

25 A No.

0826

1 Q And did the Company file a request for
2 deferred accounting for the 2004 rate case costs?

3 A Not for the general --

4 Q And has the Commission issued an order
5 approving that deferral?

6 A I could not find in any of the
7 Commission's prior orders where they specifically
8 authorized the deferral of general rate case
9 costs.

10 Mr. Story testified yesterday that it goes
11 back to the early '80s. I did look at some
12 orders in the '80s, but all I could find in those
13 orders is the word "amortize," which I agree, it
14 does imply that there is some asset that you are
15 spreading over time.

16 Q If you could direct your attention to what
17 is marked as Exhibit 436, which is the two pages
18 from the 20th Supplemental Order in docket UE
19 920433.

20 A I am sorry. I don't have 436.

21 MR. VAN CLEVE: May I approach the
22 witness?

23 JUDGE MOSS: Sure. Provide him a copy
24 that was distributed yesterday. So if someone
25 doesn't have it, let Mr. Van Cleve know.

0827

1 THE WITNESS: Thank you.

2 Q BY MR. VAN CLEVE: Mr. Russell, if you
3 could take a look on the back side of this page,
4 which is page 20 from this order, and the fourth
5 and fifth paragraphs, if you could read those to
6 yourself so you can see what they say. You don't
7 have to read them out loud.

8 A (Reading document.) Okay.

9 Q Do you see where it says that "Advance
10 Commission approval is necessary before deferring
11 costs"?

12 A Yes.

13 Q And then it says in the next paragraph,
14 "Without such approval the Company has no
15 authority to defer"?

16 A Yes.

17 Q And my question is, do you think that it
18 was appropriate for the Company to book the 2004
19 rate case costs as a regulatory asset without
20 advance approval of the Commission?

21 A Yes, I do.

22 Q And why is that?

23 A Well, the uniform system of accounts
24 requires that the Company have -- actually, it's
25 in my testimony, the description of account 928,

0828

1 that says the Company is required to get prior
2 Commission approval before it can defer rate case
3 costs.

4 Q I'm not sure I understood your answer
5 then. So why was it appropriate to book those
6 costs as a regulatory asset if there wasn't
7 Commission approval?

8 A In my reading of the Commission orders --
9 and actually I did not read this order. I was
10 not aware of this. When I read this I'm not sure
11 whether they are actually talking about which
12 rate case costs. But after reading this, I do
13 have some concern about the issue.

14 Q If the Commission reached the conclusion
15 that it wasn't appropriate to treat these costs
16 as a regulatory asset, would that change your
17 recommendation that a portion of these costs be
18 amortized?

19 A Yes. If I knew, in fact, the Commission
20 had explicitly ordered that. I'm not sure the
21 adjustment would be a lot different, because my
22 proposal would be to normalize rate case costs;
23 in other words, simply averaging rate case costs
24 over a period of years.

25 So whether the Company's method of

0829

1 deferring and amortizing results in a different
2 number than if you were to simply normalize, I'm
3 not sure that the number is so different or the
4 bottom line effect would be different.

5 Q Can you say why, as a policy matter, you
6 think normalization is a superior method to
7 dealing with these costs compared to the deferral
8 and amortization approach?

9 A Well, the rate case costs aren't a huge
10 portion of the Company's expenditures. Things
11 that I believe should be deferred and amortized
12 are larger dollar items, like the PGA process.
13 There is some deferrals associated with recovery
14 of DSM programs.

15 But normal expenditures, whether they are
16 every three years or every year, should be
17 expensed in accordance with the uniform system of
18 accounts. I mean, if we defer everything there
19 is absolutely no risk to the Company.

20 Q Has Staff reviewed the 2004 rate case
21 costs to determine whether they are reasonable?

22 A They are an estimate going forward, so
23 it's hard to determine reasonableness with an
24 estimate going forward.

25 Q Well, what I am asking about specifically

0830

1 are the costs that have been deferred that you
2 are proposing be amortized through August of
3 2004. Have Staff reviewed the reasonableness of
4 those costs?

5 A Not really. I am concerned about some of
6 the levels of expenditures, but if you look at
7 past raise cases they have also been in that
8 range, million-dollar-plus range. I do have some
9 concern about the level of those costs, but did
10 not do an in-depth analysis comparing legal fees
11 with other utilities, or consulting fees with
12 other utilities.

13 Q And one of your Exhibits, JMR 5 which is
14 Exhibit 425, that's a Staff memorandum related to
15 the deferred accounting petitions for the PCORC
16 costs, right?

17 A Right.

18 Q And page 3 of that exhibit in paragraph
19 No. 2 indicates that Staff had concerns also with
20 the level of the legal expenses in the PCORC
21 case; is that right?

22 A Yes.

23 MR. VAN CLEVE: That's all the questions I
24 have, Your Honor.

25 JUDGE MOSS: Thank you. Ms. Dodge.

0831

1 CROSS EXAMINATION

2

3 BY MS. DODGE:

4 Q Mr. Russell, we will stay on topic on rate
5 case costs. Looking at Exhibit 436 the 20th
6 Supplemental Order that Mr. Van Cleve handed
7 you --

8 A Okay.

9 Q Do you have it?

10 A Yes.

11 Q Are you aware that this was the order on
12 the second phase of UE 921262? Not the rate case
13 phase; rather the prudence phase of that docket?

14 A I get that sense from reading this.

15 Q So the costs discussed here were not
16 general rate case costs, were they?

17 A I don't know.

18 Q And it's true, isn't it, that with respect
19 to the power cost only rate case, a new type of
20 proceeding that first took place last year, the
21 Company filed an accounting petition for
22 authorization to defer its costs for that case?

23 A That's correct.

24 Q In your testimony at page 21, it's 421.

25 A I'm there.

0832

1 Q Lines 2 to 3, you state "There may be a
2 legitimate misinterpretation by PSE of prior
3 Commission decisions on how to account for rate
4 case costs."

5 A Yes.

6 Q You don't mean to suggest, do you, that
7 the Company is treating its rate case cost
8 expenses differently in this case than it and the
9 Commission have for over 20 years?

10 A It's hard for me to go back, reading the
11 orders, and determine how those rate case costs
12 were treated on the Company's books, given the
13 Commission's orders.

14 There, again, I don't see the word "defer"
15 anywhere in Commission orders. I do see the word
16 "amortize," which as I stated does imply
17 amortization of an asset over time. But I can't
18 determine from those orders where any specific
19 authority was given.

20 Q And, generally, to amortize the cost it
21 would first have had to have been deferred,
22 wouldn't it?

23 A Technically, yes.

24 Q Wouldn't it be more correct to say that
25 you would like to see the Commission change its

0833

1 historic treatment of rate case expenses?

2 A I don't know from reading those orders
3 what the Commission's intent was. That's the
4 problem here. I think there is some confusion
5 about the word "amortize" and "normalize."

6 I see it all the time in my work. People
7 say "amortize" when they really mean "normalize"
8 or "average." Even in Mr. Story's testimony he
9 actually gives a definition of "normalize" and
10 "amortize," I think, in recognition that there
11 has been some confusion.

12 Q In looking at the prior cases that you
13 looked at, and thinking about this issue, would
14 it be correct to say that typically the question
15 in these cases has been whether to amortize the
16 actual costs of a rate case for recovery over one
17 year, or two years, or three years, and sometimes
18 whether any specific costs from the case should
19 be disallowed?

20 A Yes, I have seen discussions about how
21 long the period should be over which you recover
22 rate case expenses. But in some of the exhibits
23 the -- actually the word "average" has been used,
24 rather than amortize, or divided by three years,
25 or divided by two years.

0834

1 Q Could you turn to Exhibit 430, please.

2 A (Complies.)

3 Q And this is the Commission's Eleventh
4 Supplemental Order from the Company's 1992
5 general rate case. And in looking at page 3 of
6 that exhibit, the adjustment 2.26 rate case
7 expense?

8 A Yes.

9 Q It's correct, isn't it, that in this case
10 the Company proposed to recover rate case costs
11 over two years, while the Commission Staff
12 proposed recovery over three years?

13 A The Company proposed two years, and Staff
14 proposed three, yes.

15 Q Now, looking at Exhibit 431.

16 A (Complies.)

17 Q Do you have that?

18 A I do.

19 Q The testimony of Staff witness Thomas
20 Schooley in the 1992 rate case, looking at page
21 2, line 15, this is the section where he begins
22 his discussion of adjustment 2.26 rate case
23 costs; is that right?

24 A Yes.

25 Q And then at pages three to four, here

0835

1 Mr. Schooley is presenting Staff's proposal for a
2 three-year amortization period rather than two
3 years. I will give you a chance to look at that.

4 A (Reading document.) Yes.

5 Q And then looking at page 4, lines 1
6 through 5 --

7 A (Complies.)

8 Q Mr. Schooley states that in the prior
9 general rate case in 1989, those rate case costs
10 had been amortized over 24 months.

11 A Correct.

12 Q Going to Exhibit 432.

13 A (Complies.)

14 Q This is the Commission's Third
15 Supplemental Order from the Company's 1989
16 general rate case.

17 A Okay.

18 Q If you look at page 2 of that exhibit,
19 line 2.20, rate case costs appears to fall under
20 the section at the top of that column labeled
21 Uncontested Adjustments; is that right?

22 A Yes.

23 Q And then at page 3 of the exhibit, the top
24 of the page, that describes how that top portion
25 of the table on the prior page set forth the

0836

1 uncontested adjustments?

2 A Yes.

3 Q And then Exhibit 433, this is the
4 Commission Staff's brief in that same 1989
5 general rate case, isn't it?

6 A Yes.

7 Q Looking at the bottom of page 2, and I
8 mean exhibit page 2, of course, it states that
9 the Company updated its costs associated with its
10 rate case filing?

11 A Okay.

12 Q And it cites Exhibits T 886 at page 20, as
13 well as page 2.12 of Exhibit 887 from that
14 docket.

15 A Page --

16 Q I am looking at the citations in the Staff
17 brief at the bottom of page 2.

18 A Exhibit No. T 88 on page 20? Excuse me, T
19 886 page 20.

20 Q T 886 and T 887, page 2.12.

21 A I don't see that reference.

22 Q On page 2?

23 A Right.

24 Q The bottom of the page?

25 A I am sorry, last line, yes.

0837

1 Q Last line.

2 A Okay.

3 Q Looking at Exhibit 434.

4 A (Complies.) I have it.

5 Q Does this appear to be Exhibit T 886 And

6 if you flip a couple of pages, T 887 from the

7 1989 rate case?

8 A Yes, I see T 886.

9 Q And then at page 4.

10 A Yes.

11 Q 887?

12 A 887, yes -- or Exhibit 887.

13 Q And this is the rebuttal testimony of

14 Mr. Story in that case?

15 A Yes.

16 Q At exhibit page 3 in the section on rate

17 case expense --

18 A Yes.

19 Q At line 16 through 18 --

20 A Okay.

21 Q Mr. Story states, "The Company also

22 updated its costs associated with this case based

23 on expenses to date and the estimated amounts to

24 complete the proceeding." Do you see that?

25 A Yes.

0838

1 Q And then at page 5 of the exhibit we
2 have --

3 A Is that the last page?

4 Q That is right. -- we have the reference
5 page 2.12 with the rate case expense adjustment.

6 A Right.

7 Q And this shows that he has averaged that
8 expense over two years?

9 A Well, it says average. It doesn't say
10 amortize.

11 Q And after that it says, "rate case
12 amortization"?

13 A Yes. Line 8 says that.

14 Q And then finally Exhibit 435.

15 A I have that.

16 Q This is Mr. Story's direct testimony in
17 that 1989 rate case?

18 A Yes.

19 Q And at page 3 of this exhibit, the bottom
20 of the page --

21 A Yes.

22 Q Beginning at line 19, he discusses rate
23 case expense?

24 A Yes.

25 Q And he states, "This proforma adjustment

0839

1 calculates the expected costs for this case and
2 amortizes them over two years." Do you see that?

3 A Yes, I do.

4 Q Now, if the Commission were to change to a
5 policy of treating general rate case expenses as
6 any other expense, it's true, isn't it, that
7 nearly all the expenses associated with the
8 general rate case would typically be incurred
9 after the end of the test year for that case?

10 A Correct.

11 Q And if the Company is not filing a general
12 rate case every year, it would be possible for
13 the entire expense associated with the general
14 rate case to fall in between test years, wouldn't
15 it?

16 A It would. But if you normalize, you would
17 look at history. You would look at a five- or
18 10-year period, and go back and capture rate case
19 costs in prior years. And by saying yes to that
20 answer, I don't want to imply that rate case
21 costs would never be recovered.

22 Q And how would you propose to normalize
23 rate case expenses for inclusion in rates?

24 A Over a three-, five-, or 10-year period.

25 Q Meaning -- and by that, do you mean you

0840

1 would look backwards in history at prior case
2 costs?

3 A Yes.

4 Q And how would you account for increases in
5 fees in that normalization process?

6 A Well, through the normalization process
7 that always happens. I mean, increased fees are,
8 you know, depends on the magnitude of the
9 increase. I would be willing to look at new
10 levels of costs, but I think generally the
11 Commission should adopt a normalization process.
12 And through the analysis, we can account for that
13 somehow, if there are, in fact, increased costs
14 that result in material changes to those
15 expenses.

16 So I'm not prohibiting that from happening
17 by advocating a normalization process.

18 Q And how would you account for cases that
19 settle within two months, versus those that are
20 fully litigated?

21 A That would flow through the averages in
22 future rate cases, or you could consider that in
23 your calculation of normalized rate case costs.
24 It could be handled several ways.

25 Q Moving to another topic, Mr. Russell.

0841

1 A Okay.

2 Q Are you the lead auditor for that case?

3 A On the electric side, yes. Mr. Parvinen
4 was on the gas side.

5 Q In your role as auditor, are you aware
6 that Puget Sound Energy has utility investments
7 that do not earn a return?

8 A Generally, yes.

9 Q One example of those might be
10 environmental costs that are associated with the
11 gas side of the business?

12 A I am not exactly sure how those are being
13 handled. I think, looking at the working capital
14 calculations that Mr. Parvinen did for both the
15 gas and electric side, you could look at assets
16 that are considered regulated and earning a
17 return, regulated not earning a return, or
18 totally nonregulated assets.

19 Q And are you aware that there is some
20 construction work in progress that is not allowed
21 to earn AFUDC in rate base?

22 A There may be a timing associated with
23 that. If a plant is under construction, it would
24 be AFUDC. In other words, the Company would be
25 reflecting in its income statement a return

0842

1 component of that, and that return component plus
2 a debt component would be added to the
3 construction work in progress.

4 So during the construction phase, there's
5 really no lag. But after the plant goes in
6 service, and the time of the next rate case
7 before the rates become effective, there may be
8 some amount of what you might refer to as lag.

9 Q And there may be some other examples also,
10 aren't there? For example, with respect to Baker
11 Hydro Project licensing costs, there could be
12 delays between construction --

13 A That could fall under a situation that I
14 just explained, yes.

15 Q When construction ends and when those
16 costs are actually added into rate base?

17 A Correct.

18 Q And are you aware generally that PSE has
19 utility investments that earn less than the
20 authorized rate of return?

21 A The total authorized --

22 Q The return that's allowed on those is
23 actually less than the overall authorized rate of
24 return for the Company?

25 A Are you asking me if the actual amount

0843

1 that the Company earns is less than the
2 authorized?

3 Q I am saying for just those particular
4 investments, that type of investment.

5 A I'm sorry. Are you asking if some of
6 those assets are returning a return less than the
7 Commission has authorized, but the Commission or
8 through the regulatory treatment those regulatory
9 assets are earning less than they are authorized?
10 I am not quite sure.

11 Q Right. Through the regulatory treatment
12 they are earning less than is generally
13 authorized for the Company.

14 A Do you have an example?

15 Q For example, the PGA and PCA deferrals
16 those are in the FERC interest rate.

17 A They do, by rule.

18 Q And that rate is currently about 4.2
19 percent, isn't it?

20 A I don't know what that rate currently is.

21 Q Do you have an idea of the magnitude of
22 that rate generally compared to the authorized
23 rate of return for the Company?

24 A I would assume it is lower, yes.

25 Q Mr. Russell, I would like to turn for a

0844

1 moment to catastrophic damage. Let me get
2 reoriented. Look at your Exhibit 421, page 25.

3 A (Complies.) I am there.

4 Q And we will also be referencing Exhibit
5 428.

6 A Okay.

7 Q As well as Exhibit 142. We will provide
8 that.

9 MS. DODGE: It's the McLain cross-exam
10 exhibit. This was the attachment to the Data
11 Request that was provided as Exhibit 428.

12 CHAIRWOMAN SHOWALTER: What was the number
13 again?

14 MS. DODGE: 142.

15 Q BY MS. DODGE: Okay. Now, generally Staff
16 agrees with the Company that it would be
17 appropriate to change the current trigger that
18 invokes the deferred accounting mechanism for
19 catastrophic storm damage; is that a fair
20 statement?

21 A Yes, it is.

22 Q And, however, your testimony proposes to
23 limit the IEEE definition of major event by
24 limiting costs that would be authorized for
25 deferral to storm events; is that right?

0845

1 A Yes. I just restricted deferral to
2 weather-related or storm-related events on the
3 electric side only.

4 Q And then you would also add an annual
5 fixed dollar amount that triggers -- it's a
6 threshold that would trigger whether storm
7 damage costs thereafter may be deferred?

8 A I would, yes.

9 Q And with respect to storm events, you are
10 proposing a \$5 million threshold in storm costs
11 from the March to December 2005 period?

12 A Yes.

13 Q And thereafter you are proposing \$7
14 million as a threshold in each of the years 2006
15 and 2007?

16 A Correct.

17 Q And looking at Exhibit 428?

18 A I have that.

19 Q Now, under the current catastrophic storm
20 definition that the Company has proposed to
21 change, the Company incurred an average of \$4.8
22 million each year in storm damage that was not
23 deferred; is that right?

24 A Correct.

25 Q And looking at Exhibit 142, your

0846

1 spreadsheet --

2 A Okay.

3 Q Now, this shows, doesn't it, the upper
4 level for each year 2003, 2002, 2001, and going
5 down to 1999. Is it correct that the lines on
6 the third -- well, the fourth column over show
7 the total for that year. So, for example, for
8 2003 there was a total of 14.8 million for storm
9 costs?

10 A Yes. Yes.

11 Q And in 2002 there were just over 4
12 million?

13 A Yes.

14 Q And 2001 there are 4.5 million?

15 A Yes.

16 Q And 2002 5.1 million?

17 A Yes.

18 Q And in 1999 9.3 million?

19 A Yes.

20 Q So in the last five years, according to
21 your spreadsheet, the Company has never had less
22 than \$4 million in storm expenses, has it?

23 A Well, not in those years. 1998 down
24 below, there was \$270,000 in 1998 if you look at
25 it on a September-end basis. In other words,

0847

1 that just captures another year, nine months.

2 Q And given the five-year average --

3 A I am sorry. A year of -- it's a full
4 year. \$269,000.

5 Q And looking in the last five years, the
6 average O&M storm damage of 5.8 million, if your
7 threshold had been in place, the Company would
8 have had to absorb on average at least 3 million
9 in additional costs that were not deferred more
10 than under the current mechanism; is that
11 correct?

12 A How do you do that math?

13 Q Just looking at your \$7 million threshold
14 and the 4.8 million average over the last five
15 years.

16 A Okay.

17 Q Is that right?

18 A 2.2 million, the difference --

19 Q And --

20 A 4.8 million is 7 -- 7 minus 4.8. I am
21 sorry.

22 CHAIRWOMAN SHOWALTER: Can both the
23 questioner and the witness identify the terms as
24 opposed to just saying numbers?

25 Q BY MS. DODGE: Here, Mr. Russell, are you

0848

1 clear that we're looking at your proposed \$7
2 million threshold before the Company can defer
3 any storm related costs for amortization?

4 A Yes.

5 Q Versus the Company's actual experience
6 over the last five years, which has been it has
7 only had to incur, on average, 4.8 million before
8 it has been permitted to defer costs for
9 amortization; is that right?

10 A I believe so. I just want to clarify that
11 that includes both catastrophic and O&M. Is that
12 your understanding in the question? It appears
13 to me, looking at the last column, that the
14 actual average is 7. Looking at the second to
15 the last question, the total average is 7.5
16 million.

17 Q Well, that, of course, includes costs that
18 were deferred?

19 A Correct.

20 Q I'm speaking of costs that the Company
21 absorbed prior to deferral.

22 A Well, I wouldn't say absorbed, because you
23 had a level set in your rates. But it's the
24 average of the O&M. I think that's what that 4.7
25 represents.

0849

1 Q And by that, you mean the nondeferred
2 costs?

3 A Correct.

4 Q So, again, the costs that were not
5 deferred over the five years were on average 4.8
6 million?

7 A Correct.

8 Q And under your proposal, the Company would
9 have to incur nondeferred costs of 7 million
10 before it would be allowed to defer any?

11 A That's correct. But there is a sharing
12 associated with this proposal. The Company's
13 actual storm expenses fluctuate from \$270,000 in
14 1998 up to, looks like, 16 million. I am looking
15 at the lower part of the page here, 16.5 million
16 in 2003. So they are highly variable.

17 So in other words, what I am saying is if
18 we set 4.8 million in rates today, the Company
19 may end up only spending 2 million, therefore
20 save some level of costs. In other words, the
21 costs would be lower than what we embedded in
22 rates.

23 On the flip side, the Company may incur 7
24 million or more than the 7 million, and eat some
25 level. So it's a balancing act that I'm trying

0850

1 to do here. Setting the threshold higher than
2 the average, because in certain years the Company
3 is going to actually incur less than the average.
4 So it's kind of like the PCA in the bands. It's
5 a lot simpler in the PCA, but that's why I set it
6 at 7 million, not 4.8 or 5 million.

7 My proposal, as I state in the response,
8 actually is better to the Company, in my mind,
9 because it establishes the Company's earnings
10 over the current deferral mechanism. Because in
11 one -- under the current mechanism, if you look
12 at Exhibit 142, the Company actually incurred --
13 I think one year was in the -- O&M, the highest
14 year in O&M was 9.3 million for 1999.

15 So the Company actually incurred 9.3
16 million, but did not defer anything under the
17 current proposal. Under my proposal the Company
18 would have deferred anything over 7.

19 MS. DODGE: Thank you.

20 JUDGE MOSS: That completes your
21 questions? Are there any questions from the
22 bench for Mr. Russell?

23

24

25

0851

1 EXAMINATION

2

3 BY CHAIRWOMAN SHOWALTER:

4 Q Mr. Russell, are you the witness from the
5 Staff that has the most overarching view of the
6 case on the electric side?

7 A I bring everything together. The power
8 costs flow into, and all the other
9 recommendations of Staff, kind of flow into the
10 bottom line revenue requirement calculations.

11 Q Okay. I am interested in asking you some
12 fairly high-level questions about the overall
13 case. And that is, if we, the Commission, accept
14 your recommendation, and particularly I'm
15 thinking about the overall revenue requirement
16 and the return on equity calculations, but also
17 everything else, is it your opinion that it is
18 not likely that the Company would be downgraded?

19 A I would -- and I don't want -- I would
20 hesitate to even try and answer that question. I
21 think Mr. Wilson would be the appropriate
22 witness.

23 Q So you don't have an opinion as to whether
24 that is probable or not?

25 A I don't.

0852

1 Q If the Company were downgraded, let's say
2 one notch at the corporate level, and one notch
3 at the senior secured debt level, if that
4 occurred, would that be of concern to you? That
5 is, are you worried about that -- if that
6 happens, does that worry you?

7 A Well, again, I hesitate to answer those
8 kinds of questions. But I think the cost of
9 capital witnesses are probably more appropriate
10 witnesses to answer that question.

11 I am not a finance expert. I have an
12 accounting background, but obviously in other
13 witness's testimony there are calculations about
14 the impact of downgrades in their testimony. So
15 I can't -- I would hesitate to try and answer
16 anything along those lines. I am sorry.

17 Q So there is no one on the Staff, as
18 opposed to the expert witnesses, who has an
19 opinion on the two questions I asked; is that
20 correct?

21 A I think, again, Mr. Wilson. He's not on
22 Staff, but he's our higher expert. He would -- I
23 think he would be the best person to ask those
24 questions.

25 But, again, I look at the testimony and I

0853

1 see all the arguments about the costs and the
2 benefits, and the impacts, and I just don't
3 see -- I have some concerns about the Company's
4 calculations, especially with regard to the graph
5 shown on Mr. Gaines's exhibits netting those
6 three benefits, especially with regard to the
7 numbers that flow forward from Ms. Ryan's
8 testimony.

9 That's a net present value number, and is
10 not comparable at all to the other two numbers,
11 the impact associated with debt and financial
12 flexibility. I have some concern about that
13 calculation and that graph.

14 So I agree with Mr. Wilson and the other
15 cost of money witnesses. There may be some
16 impacts on debt costs going forward, but I have
17 not made a calculation to assess the cost benefit
18 analysis of the impact.

19 Q Does that also go for -- do you have any
20 opinion on the Company's ability to engage in
21 trading with other partners? That is, separate
22 from the issue of borrowing and quite -- well,
23 separate from the issue of acquiring additional
24 new resources, and going instead to some of the
25 other dimensions that the Company is raising, for

0854

1 example, hedging, and trading with trading
2 partners, do you have any opinion on those
3 aspects of the Company's activities?

4 A I am not an expert in that field. You
5 know, we look at hedging and the PGA process that
6 I have been involved with. I generally
7 understand some of the credit implications, but
8 how you actually measure those impacts and
9 convert it into revenue requirement, it's almost
10 impossible in my mind.

11 And really, that's what my testimony was
12 all about was calculating the revenue
13 requirement. So I cannot assess the impacts of
14 the credit requirements associated with hedging.
15 I don't know how you would quantify that into a
16 revenue requirement calculation.

17 I mean, utilities do hedging, Avista and
18 all the other utilities we regulate do hedging.
19 This is really the first time I have seen this
20 argument in support of a revenue requirement
21 calculation. Now, there may have been some other
22 cases, but I have not been involved with those.
23 And I have never heard this argument in a PGA in
24 what I've looked at, a utility saying that they
25 don't have enough revenue requirement to be able

0855

1 to do the hedging they want to do.

2 Q Well, do you have a sense of the Company's
3 credit rating over a long period of time, let's
4 say, for the last 15 years?

5 A No, I don't.

6 CHAIRWOMAN SHOWALTER: Thank you. I have
7 no further questions.

8 MR. CEDARBAUM: Commissioners, if I may
9 interject, Dr. Wilson was our finance expert and
10 he was on the stand earlier this week. I mean, I
11 would have hoped, actually, that these types of
12 questions could have been directed to him.

13 He's no longer in the state. He's gone
14 back to Virginia, but I could contact him if you
15 like, and make him available, but I would assume
16 by telephone, for these types of questions. But,
17 again, he was our witness on those areas.

18 CHAIRWOMAN SHOWALTER: And I will think
19 about that. I was trying to determine whether
20 there's anyone on the Staff's case who has what I
21 would think of the overarching sense of the case.
22 And frequently there's a policy analyst who does
23 have expertise, even though there are further
24 experts. And if that's not the makeup of these
25 witnesses, that's --

0856

1 MR. CEDARBAUM: And I think because of the
2 cost of capital, that umbrella issue was so
3 dominant in this case, that Dr. Wilson, I guess,
4 in that respect, you could look at as if not the
5 overriding policy expert, but certainly the one
6 to answer those questions for Staff as our
7 expert.

8 So, again, we can try to make him
9 available, if that's your preference. But I
10 would have to make those arrangements.

11 CHAIRWOMAN SHOWALTER: Thank you.

12

13 EXAMINATION

14

15 BY COMMISSIONER HEMSTAD:

16 Q With regard to the earlier inquiries
17 concerning deferral and amortization or expensing
18 of rate case costs, how should we interpret the
19 statements from Steve Reynolds for the Company
20 that on a going forward basis it would be the
21 Company's expectation to, in front of us
22 routinely -- I don't recall his words precisely,
23 but I think he said almost yearly, because of the
24 expectation of capital expenditures that the
25 Company would be incurring. In other words,

0857

1 reasonably expect to have more routine rate case
2 filings than has been the case historically.

3 Does that affect the issue of whether such
4 costs should be expensed as against deferred in
5 some way?

6 A Not really. And I say that because under
7 expense and normalize, obviously you can consider
8 not strictly a calculation of looking back and
9 averaging prior rate cases over a certain amount
10 of years, you can consider, okay, what do we also
11 expect the Company to incur on a going forward
12 basis. So that calculation could be done through
13 the expense and normalization process. It could
14 be handled.

15 One of the main arguments I have with
16 deferral and amortization is basically the blank
17 check that you would be giving the Company for
18 incurring rate case costs. It's open-ended.
19 They simply spend whatever they want on rate case
20 costs and it has no impact to them. Whereas if
21 you adopt expense and normalize, I think it gives
22 more incentive to the Company to try and control
23 costs than deferral treatment does.

24 I think that would -- that's the real
25 reason that you should consider going to an

0858

1 expense and normalization process for rate case
2 costs.

3 Q The thrust of my question was really if
4 the expectation is that the Company would be here
5 more routinely, does that strengthen the point
6 that it should either be normalized or expensed
7 rather than deferred?

8 A Well, I just don't see one being stronger
9 than the other under those situations. You could
10 handle that situation under both methods.

11 COMMISSIONER HEMSTAD: Thank you. That's
12 all I have.

13

14 EXAMINATION

15

16 BY COMMISSIONER OSHIE:

17 Q I want to clarify one thing, Mr. Russell.
18 When you talk about deferral, deferral of rate
19 case expenses, would those costs be considered
20 under your concept of deferring a regulatory
21 asset in which the Company would earn the rate of
22 return until the balance has been amortized to
23 zero?

24 A Well, if the Commission does adopt
25 deferral and amortization, I would argue that

0859

1 they shouldn't earn a return on those deferred
2 costs. They are costs that they are incurring on
3 a fairly short time period.

4 I mean, if it was a huge amount that they
5 incur every 10 years, you can consider a return
6 on those deferrals. But since this is a
7 year-to-year, every two-year expenditure, if you
8 do allow amortization, I would argue that they
9 should not earn a return on those deferrals. I'm
10 not sure I answered your question.

11 Q No, I think you did, because when you were
12 talking about a deferral accounting mechanism, I
13 associated that with deferring it into the
14 regulatory asset account on which there is a rate
15 of return earned on that.

16 And so what you have done, at least
17 enlighten me, is that you have not separated that
18 out. So you are using the term deferral without
19 associating it with a rate of return on the
20 amounts deferred?

21 A Yes. Because if you look at the
22 description of accounts, or the accounts in my
23 testimony, you should defer the cost to 186 if
24 you are given specific authority. Normally the
25 balances in those accounts don't earn a return.

0860

1 So it implies they don't earn a return in my
2 mind.

3 COMMISSIONER OSHIE: Thank you, very much.
4 That helped clarify the issue with me.

5 JUDGE MOSS: That appears to complete the
6 questions from the bench. Any follow up,
7 Ms. Dodge?

8 MS. DODGE: Yes. Just a moment, please.

9 JUDGE MOSS: Do you have just a couple?

10 MS. DODGE: Just a couple.

11

12 RE-CROSS EXAMINATION

13

14 BY MS. DODGE:

15 Q On that same issue, I understand the part
16 about between when the cost is deferred to when
17 it's approved into rates that you are saying
18 don't earn a return on that. Now, as to that
19 amount, once it is approved to be amortized,
20 whether it would be one year or two years or
21 three years, are you saying that ought not earn a
22 return?

23 A Correct. As I stated, it's a cost that
24 you incur every year or two, so it's a fairly
25 short-term amount. And you amortize that over a

0861

1 fairly short period in especially in light of
2 increased amount of rate cases being filed. So
3 it's simply one method of spreading costs over a
4 period of time, in my mind.

5 Q With respect to Ms. Ryan's testimony, you
6 stated you had some concerns that she was using a
7 net present value number. It's your
8 understanding, then, that her testimony was not
9 presenting an annualized number?

10 A When I read her testimony, I understood
11 that she had calculated some numbers based on
12 10-year hedging scenarios, and net present value
13 got back to today, effectively.

14 Q And your concerns are based on the
15 assumption that she was embedding 10 years worth
16 of benefits in those numbers, is that --

17 A Yes.

18 Q That's correct?

19 A Yes.

20 MS. DODGE: I just have one other
21 housekeeping matter. I was informed that I
22 neglected to offer Exhibit 428 through 435.

23 JUDGE MOSS: Okay. And ICNU had
24 identified and referred to 436. I don't think
25 you offered it, either.

0862

1 MR. VAN CLEVE: Your Honor, I just
2 identified it as an exhibit for convenience. I
3 don't think we need it in the record, because
4 it's a Commission order.

5 JUDGE MOSS: So 428 through 435 have been
6 offered. Any objection? Hearing none, they will
7 be admitted.

8 (EXHIBITS 428 to 435 RECEIVED.)

9 JUDGE MOSS: Any redirect?

10 MR. CEDARBAUM: Yes, Your Honor, just a
11 couple of areas.

12

13 REDIRECT EXAMINATION

14

15 BY MR. CEDARBAUM:

16 Q Mr. Russell, in the rate case cost areas
17 during your cross-examination you indicated in
18 your review of the prior Commission orders and
19 other materials you felt that there had been --
20 I don't know about confusion, but a lack of
21 clarity with respect to the term normalize,
22 amortize, average, those sorts of things. Do
23 you recall that?

24 A Yes. Yes.

25 Q A number of the exhibits that were offered

0863

1 in cross-examination through you by the Company
2 consist of various orders and sections of
3 testimony, and things like that.

4 I don't think you need to look at them, or
5 know the numbers for this question. But do you
6 feel that that lack of clarity, and the use of
7 those terms is present in those materials
8 as well?

9 A Yes. Because the term amortize and
10 average and expense are all used, in my mind,
11 interchangeably. And I think that's where the
12 confusion or lack of clarity in my mind lies.

13 Q Switching topics, now, you were asked some
14 questions regarding CWIP, construction work in
15 progress. And you testified that during
16 construction the Company is allowed to accrue
17 AFDUC; is that correct?

18 A Yes.

19 Q And is it correct that once construction
20 is over and the facilities, or whatever it is, is
21 placed into service, the Company transfers that
22 item into plant and service?

23 A Yes.

24 Q And once that is done, does the Company
25 begin to depreciate those facilities?

0864

1 A Yes.

2 Q Is depreciation part of the return?

3 A Yes, it is.

4 Q Through depreciation, what is the effect
5 on the Company's cash flow in addition to return
6 aspect?

7 A It's not -- depreciation is not a cash
8 outlay.

9 Q Is there any improvement in the Company's
10 cash flow from depreciating property?

11 A I am just trying to think through. It's
12 been a long time since I looked at a cash flow
13 statement.

14 Q If you --

15 A I hesitate to go beyond the statement that
16 it's not a cash outlay.

17 MR. CEDARBAUM: Thank you. Those are all
18 of my questions.

19 JUDGE MOSS: I believe that completes our
20 examination of you, Mr. Russell. We appreciate
21 your testimony, and you can step down.

22 We will take our morning recess a little
23 late. It sort of slipped my mind. Why don't we
24 come back at 20 after the hour.

25 (Brief recess.)

0865

1 JUDGE MOSS: Let's come back to order,
2 please. Ms. Ryan, I presume.

3 THE WITNESS: Yes.

4

5 JULIA RYAN,
6 produced as a witness in behalf of The Company,
7 having been first duly sworn, was examined and
8 testified as follows:

9

10 JUDGE MOSS: Thank you. Please be seated.

11

12 DIRECT EXAMINATION

13

14 BY MS. DODGE:

15 Q Ms. Ryan, do you have before you your
16 direct testimony and rebuttal testimony in this
17 matter, as well as the exhibits to your testimony
18 which have been identified as Exhibits 71 through
19 107?

20 A Yes, I do.

21 Q Do you have any additions or corrections
22 to make to any of that testimony or exhibits at
23 this time?

24 A Yes. I have one correction to make. It
25 is in Exhibit 71, and it is on page 19 of 29.

0866

1 And on line 5 --

2 Q Just a moment.

3 A On line 5 in the middle of the line it
4 says 36 million, and it should be 30 million.

5 Three, zero.

6 Q With that correction, are the answers to
7 the questions in Exhibits 71 through 107 true and
8 accurate to the best of your knowledge?

9 A Yes, they are.

10 MS. DODGE: Your Honor, we offer Exhibits
11 71 through 107 into evidence, and offer Ms. Ryan
12 for cross-examination.

13 JUDGE MOSS: There apparently is no
14 objection or I would have heard it, so I will
15 admit those. And your witness is available for
16 cross?

17 MR. CEDARBAUM: I am sorry, Your Honor,
18 does that include the cross-examination exhibits,
19 because there was a break between --

20 JUDGE MOSS: There is an out-of-sequence
21 number.

22 MS. DODGE: I'm sorry. And we just
23 referenced Ms. Ryan's exhibits, so that would be
24 through 96.

25 JUDGE MOSS: Through 96 and 107. We had

0867

1 an out-of-sequence number, because of something
2 that came in late, I suppose, or I don't know.
3 But in any event, we have had offered, to be
4 perfectly clear, Exhibits 71 through 96 and 107.
5 And those are admitted as marked.

6 (EXHIBITS 71 to 96, 107 RECEIVED.)

7 JUDGE MOSS: And then we have cross that
8 we will talk about, I am sure, during the course
9 of the examination.

10 And I have for this witness 60 minutes
11 indicated by you, Mr. Van Cleve, and shorter
12 times for Public Counsel and Staff. So I would
13 prefer to have you go first, and you may cover
14 some of their areas.

15 MR. VAN CLEVE: Thank you Your Honor. It
16 shouldn't take that long.

17 JUDGE MOSS: And we will break at 12, so
18 we may disrupt you, if you are not done.

19

20 CROSS EXAMINATION

21

22 BY MR. VAN CLEVE:

23 Q Good morning, Ms. Ryan.

24 A Good morning.

25 Q Can you refer to page 22 of your rebuttal

0868

1 testimony, Exhibit 82?

2 A (Complies.) All right. I am on page 22.

3 Q At line 17 you say that "The Company has
4 no reason to believe that gas prices for the rate
5 year will move back to the levels in the
6 Company's original filing." Is that your
7 position here today, also?

8 A Yes, it is.

9 Q And do you believe that gas prices are
10 trending up, or trending down, or even for the
11 rate year at this point in time?

12 A They have been trending up since we filed
13 our rebuttal testimony, which had gas prices
14 ending September 13. The market is continuing to
15 trend up.

16 It is our belief that the prices will
17 still remain in the vicinity of the prices which
18 we filed at the end of September. They could go
19 up some more, as they have done more recently.
20 We do not expect them to go back to the levels
21 that we submitted in the prefiled testimony.

22 Q I would like to direct your attention to
23 Exhibit 98 C.

24 A Okay. I have turned to that page.

25 Q And this is --

0869

1 COMMISSIONER HEMSTAD: I am sorry. Give
2 me the reference again.

3 MR. VAN CLEVE: 98 C.

4 COMMISSIONER HEMSTAD: Page?

5 MR. VAN CLEVE: Page No. 4.

6 Q BY MR. VAN CLEVE: Are you at page 4 of
7 Exhibit 98 C?

8 A Yes, I am.

9 Q Does this exhibit show gas supply
10 arrangements that the Company has entered into
11 since it filed its original case?

12 A Yes, it does.

13 Q And this is a Supplemental Response to an
14 ICNU Data Request 5.02, and the numbers at the
15 bottom referencing the contracts entered into
16 between 9/30 and 11/11. Do you see that?

17 A Yes, I do.

18 Q And if you go over to the column May 2005,
19 and you come down to those most recent contracts,
20 do you see in the MMBTU column that that is a
21 negative number?

22 A Yes, I do.

23 Q And so does that mean your most recent
24 transaction shown here for the month of May 2005
25 is a sale of gas?

0870

1 A Yes, it is a sale of gas. And at the same
2 time when we enter into a sale of a gas purchase,
3 it is because we are replacing it with something
4 else.

5 So I believe that we were buying power at
6 the same time, because of the change in the
7 market heat rates. So we were selling the gas,
8 and then turned around and purchased the power
9 for the power portfolio.

10 Q So you are saying that for that particular
11 sale, that there was an exact matching purchase?

12 A I don't know exactly, but it is our
13 practice not to sell hedges unless we can further
14 optimize by replacing with something else that is
15 more advantageous to the portfolio.

16 Q And next to the negative number, the
17 number in parenthesis, that's the number you
18 made the sale at?

19 A Yes, I believe that's correct.

20 Q I would like to refer you now to Exhibit
21 101. And this exhibit has two pages. The second
22 page is an updated version of the first page.
23 And this is your workpaper 006; is that correct?

24 A Yes, it is.

25 Q And does this show for your rebuttal case

0871

1 the calculations of power costs that are used to
2 create the revenue requirement?

3 A (Reading document.) Yes, it does. I was
4 hesitating because I wanted to check to see if it
5 is the full power cost. I can confirm that it is
6 at least a subset of the power costs.

7 Q So if we look at the very bottom line on
8 the page --

9 COMMISSIONER HEMSTAD: Counsel, I'm not
10 sure which page we're on.

11 MR. VAN CLEVE: I'm sorry. Page 2 of
12 Exhibit 101.

13 COMMISSIONER HEMSTAD: Is it marked page
14 2?

15 MR. VAN CLEVE: Yes, it is.

16 CHAIRWOMAN SHOWALTER: Exhibit 101?

17 MR. VAN CLEVE: Correct.

18 COMMISSIONER HEMSTAD: Perhaps we can go
19 off the record.

20 (Discussion off the record.)

21 JUDGE MOSS: Okay. I think we're all set,
22 Mr. Van Cleve.

23 MR. VAN CLEVE: Thank you, Your Honor.

24 Q BY MR. VAN CLEVE: We're on Exhibit 101,
25 page 2 of 2. And let me start off with a

0872

1 different question, Ms. Ryan. At the very bottom
2 left of the page, there's a C in parenthesis.
3 And then it says, "Rebuttal GRC Summary 50-year
4 Hydro 2005 to 2006 Aurora, Plus Not Aurora XLS."
5 What does that designation of this spreadsheet
6 mean?

7 A That's a label that our team put on the
8 spreadsheet to indicate what information is
9 contained here. It's a title for the
10 spreadsheet.

11 Q And does this indicate that it's a
12 combination of two things?

13 A It does. It would indicate that it
14 includes both costs that are in the Aurora model,
15 and costs that we model outside of Aurora.

16 Q Now, looking at the last line on the page,
17 does this show that for the test year that there
18 were \$670,339,000 in power costs, and then the
19 next column is the proposed power costs in this
20 case. And then if you go over to the third
21 column, that's the increase in power costs that
22 you are seeking? Is that the right way to read
23 that?

24 A Yes, but as a point of clarification.
25 This does not include the gas price change that

0873

1 we have filed. And Exhibit 93 provides
2 additional information that incorporates that gas
3 price change.

4 Q Okay. I would like to focus your
5 attention on the lines related to the Fredonia,
6 Frederickson, and Whitehorn plants. Do you see
7 those? They have 547 at the far left?

8 A Yes, I do.

9 Q And those are combustion turbine plants?

10 A That's correct.

11 Q Okay. I will refer to those as the CT's.
12 And if you look at the fixed and variable columns
13 for the test year, the proposed rate case amount
14 and the change, and I will go over to the change,
15 these are basically increased costs that you are
16 seeking to recover related to the CT's; is that
17 right?

18 A Yes, that's correct.

19 Q And there's two categories of costs. One
20 is labeled variable, and one is fixed. And what
21 I would like to get to is what is included in
22 those costs, where they come from?

23 A Okay. What is your question then?

24 Q Well, let's focus first on the fixed
25 costs. And if you could turn to Exhibit 102 C.

0874

1 A (Complies.)

2 Q This is your workpaper 080, correct?

3 A That's correct.

4 Q And does this exhibit show that the
5 Company is seeking to recover for 200 hours of
6 assumed oil burn at the CTs?

7 A That is correct. We have 200 hours
8 budgeted with an oil price cost estimate. And
9 this cost is a cost to meet load over and above
10 the expected load, which is modeled in Aurora.

11 And this budget item includes -- well, it
12 covers both oil purchases, but if it's more
13 economic and we end up dispatching the plants on
14 gas, or buying the power on the market, this
15 budget item is to cover all of those events.

16 Last year we ran approximately 250,000
17 megawatt hours over the average. And if we
18 looked at and we ended up purchasing most of that
19 power in the market, and the costs last year were
20 approximately \$10 million -- excuse me, I would
21 like to say that differently.

22 When we looked at the hours over the
23 expected load, megawatt hours over our expected
24 load, and applied an average winter price it
25 ended up being about \$10 million.

0875

1 Q If you go down to the bottom right-hand
2 corner of Exhibit 102 C, does that show that the
3 cost of this oil that you are presuming is burned
4 in the CT's is approximately \$12.75 million?

5 A That is a calculation based upon the
6 135,000 megawatt hours above, and estimates of
7 future market purchases, if they were entered
8 into, and existing oil inventories.

9 Q And referring back to page 2 of Exhibit
10 101, the variable column for the CT plants, those
11 numbers, is that the output from Aurora?

12 A I am sorry --

13 Q I am at Exhibit 101, page 2?

14 A Could you ask the question now that I am
15 on page 2 of the exhibit?

16 Q Sure. We're looking at the increased cost
17 amount for Fredonia, Fredrickson, and Whitehorn.
18 And I am looking at the variable numbers and the
19 fixed numbers. And do -- are the variable
20 numbers the output of Aurora?

21 A Yes, I believe so, subject to check.

22 Q So this is the cost of the expected
23 operation of these plants produced by Aurora; is
24 that correct?

25 A To meet expected load, correct.

0876

1 Q And these numbers to the right under
2 fixed, is that primarily related to this cost of
3 oil?

4 A I am not sure. I think that these are
5 different fixed costs, because as I said before,
6 what we do in Aurora is we model for an average
7 load. And so we put in both fixed and variable
8 costs anticipated with our units to meet that
9 load.

10 And so I think that the oil inventory,
11 which I explained, covers both power and gas and
12 oil, that we buy over and above what we use to
13 meet average load is not included in these
14 numbers. But we could check that.

15 Q Can you refer to Exhibit 103 C?

16 A (Complies.) Yes, I have it in front of
17 me.

18 Q Page 1 -- basically, let me just say that
19 Mr. Schoenbeck prepared this exhibit. And what
20 he did was he took electronic spreadsheets that
21 the Company provided and pulled pieces out, and
22 basically cut and pasted this together.

23 And he was trying to understand the
24 derivation of the variable and fixed costs for
25 the CTs that we were talking about in Exhibit

0877

1 101. And if you look on page 1, the Aurora cost,
2 and on page 2 is the Aurora generation and
3 megawatt hours, basically they added up to the
4 numbers under the variable column in Exhibit 101.
5 And have you verified whether these came from
6 your spreadsheets?

7 A I did look at this, and this did -- I
8 mean, the numbers appear to come from our
9 workpapers. And the only thing I would mention
10 is that the numbers in the section labeled Aurora
11 Costs, the top section, on page 1 and on page 2,
12 come from a run of Aurora using the filed gas
13 prices, not with the updated gas prices.

14 And I don't know if this is going to
15 impact where you are going. But with the new gas
16 prices, the forecasted generation was lower. So
17 these are workpapers using the earlier filed gas
18 price. So it has a different generation impact.

19 Q But even with the new gas price, Aurora
20 doesn't show any generation at these plants with
21 oil, does it?

22 A The oil cost is an added cost to the
23 Aurora costs. Because it's put into the budget
24 or the base line to cover those days, those
25 hours where we're running over what we need,

0878

1 what we projected for expected load.

2 So there's a placeholder for days when you
3 have load that exceeds average. And we calculate
4 those costs. There's some other costs, exchanges
5 and transmission costs, some peaking options that
6 are in the power cost base line to meet higher
7 than expected load, higher than average load.

8 Q So why couldn't you just increase the load
9 in Aurora, and have Aurora dispatch the most
10 efficient resource available to serve those
11 loads, and find the cost that way?

12 A I don't claim to be an expert on how
13 Aurora is run. We have people within the Company
14 who are very conversant with it. We have been
15 using it to meet average load, and that's the
16 convention that we have been pursuing in this
17 proceeding, and in other proceedings, as well as
18 for our lease cost planning.

19 I don't know if we can do as you are
20 suggesting. That's why we model it outside of
21 Aurora, and then bundle it all together in the
22 total power costs.

23 Q So this \$12.75 million cost that you put
24 into the case that's not part of Aurora, have you
25 also put into the case additional revenues that

0879

1 you will receive as a result of having loads that
2 are in excess of expected?

3 A I believe we do. I don't know exactly
4 where that information resides.

5 Q Could you provide that information,
6 because we were unable to discover that?

7 A Would you ask the question again? I want
8 to make sure I have answered it properly.

9 Q Yes. You have included \$12.75 million of
10 the cost of burning oil. And you did this
11 outside of Aurora for the purpose of serving
12 unexpectedly high loads, so loads in excess of
13 your forecast, or in excess of expected. Which
14 would generate additional revenues from
15 additional sales to your customers.

16 And have you put into the case those
17 additional revenues to offset this cost?

18 A I believe we have put an average. We also
19 have days when loads are much lower than normal,
20 and we have to sell our energy that we have
21 purchased to meet those loads typically at lower
22 prices. We have not put in an item there to
23 reimburse the Company.

24 So you have average loads that you plan
25 for, and you have days where you have loads

0880

1 higher and lower. And both of those events are
2 cost items to the Company. In an upward event,
3 it can also be a revenue generation, but in a
4 downward day when you don't have very high loads
5 and it's warmer than normal, it's a revenue loss.

6 I can't speak to how we're dealing with
7 those peaks and troughs. I know we have average
8 loads here.

9 Q Well, I guess I don't understand how you
10 can use average load to determine the revenues
11 that you received, but you use average load plus
12 \$12.75 million to determine your cost of
13 generation. It seems like a mismatch there.

14 A I am pretty sure there's no
15 inconsistencies, but I can't answer the question
16 specifically as you are asking it here. I think
17 the Company could answer the question. We can
18 find that answer.

19 Q Well, I guess I would request that you
20 provide that answer.

21 JUDGE MOSS: Are you putting it in the
22 form of a Records Requisition then?

23 MR. VAN CLEVE: Yes.

24 (RECORDS REQUISITION)

25 MS. DODGE: I was going to suggest that we

0881

1 may have the opportunity to provide that
2 information while Ms. Ryan is yet on the stand.

3 JUDGE MOSS: Then maybe we can come back
4 to this after lunch, Mr. Van Cleve, since we're
5 about to run into the lunch hour anyway. If you
6 have some more, I am assuming that you do --

7 MR. VAN CLEVE: Yes. I could turn to
8 another subject matter, I think I can dispose of
9 quickly.

10 JUDGE MOSS: Okay. And thank you,
11 Ms. Dodge.

12 Q BY MR. VAN CLEVE: If you can look at
13 Exhibit 99, please.

14 A (Complies.)

15 Q This was an ICNU Data Request 9.02, which
16 asks for actual generation information from
17 the -- what I refer to as the CTs for 1994
18 through 2004; is that correct?

19 A I believe so. This was a Data Request
20 that was prepared by Phillip Popoff under the
21 direction of Mr. Markell.

22 Q And I will tell you that there were
23 voluminous generator logs that have been omitted
24 here. And if you look at Exhibit 100, that is
25 the Company's Supplemental Response. And we have

0882

1 attached as an example what these generation logs
2 look like.

3 But if you turn to page 3, this shows no
4 generation for this unit for this particular
5 month. But you can see toward the bottom that
6 the megawatt hours of oil, and the megawatt hours
7 of gas are both specified. Do you see that?

8 A Yes, I see that the form here has space
9 for that information.

10 Q Now, I would like you to turn to page 4 of
11 Exhibit 103 C, which is the exhibit prepared by
12 Mr. Schoenbeck.

13 A (Complies).

14 Q And I am going to ask you to accept,
15 subject to check, that what this exhibit does is
16 total up the generator logs that were provided in
17 Exhibits 100 and 101.

18 A I have to say -- I apologize, but I can't
19 accept that subject to check, because this isn't
20 our work. This is, as you say, Mr. Schoenbeck's
21 work. And I don't know if this is correct, and
22 if I say subject to check, then I believe the
23 onus is on me and the Company to confirm that
24 these are correct when it's really
25 Mr. Schoenbeck's work. So, no.

0883

1 Q Okay. Well, I would like to make another
2 Records Requisition request that you provide a
3 total of those invoices to save the Commission
4 the time of going through hundreds and hundreds
5 of pages of generator logs to total up the
6 historic oil burn at these CTs.

7 MS. DODGE: Your Honor, I object to the
8 Records Requisition. This is essentially a
9 supplemental exhibit that ICNU is attempting to
10 insert into this proceeding through the
11 cross-examination device.

12 This topic was not addressed in
13 Mr. Schoenbeck's testimony. He didn't present
14 this exhibit in his testimony. The Company first
15 saw it last Wednesday as a cross-exam exhibit
16 from Ms. Ryan. These logs are a good six inches
17 thick of information. So if it had been
18 presented in Mr. Schoenbeck's testimony the
19 Company would have had a proper opportunity to
20 rebut it, examine it, and verify it.

21 And to have new matters brought up first
22 on cross-examination is, I don't believe, in the
23 spirit of the rules or -- and it's taking
24 advantage of some procedural devices that I don't
25 think ought to be used for this purpose.

0884

1 JUDGE MOSS: Any response?

2 MR. VAN CLEVE: Your Honor, one, this
3 issue was not discovered in time to be put into
4 Mr. Schoenbeck's testimony. And I think it's a
5 pretty simple request to total up logs that were
6 provided in response to a Data Request, and it is
7 very relevant to look at the historic levels of
8 oil generation in determining whether the
9 Company's proposal in this case, which is a
10 significant expense, is reasonable.

11 JUDGE MOSS: Well, we will consider that
12 over the lunch hour, and give you a ruling on
13 that when we come back. So we will take our noon
14 recess, and return at 1:30.

15 (Lunch recess taken.)

16 JUDGE MOSS: Let's be on the record.

17 Mr. Van Cleve, what was the exhibit number
18 we were looking at that was represented to be the
19 totals of those papers? I am looking for it, but
20 I am not finding it.

21 MR. VAN CLEVE: Your Honor, that is
22 Exhibit 103 C, page 4.

23 JUDGE MOSS: That's the problem. It was
24 the fourth page. The Commissioners -- we have
25 discussed the matter over the lunch break, and

0885

1 our ruling is that you should go forward with
2 your questions using this exhibit, with these
3 being treated with what they are purported to be,
4 and then the Company should verify these numbers
5 or let us know if they are incorrect.

6 And that will be, I suppose, in the form
7 of a bench request. Is it clear?

8 MS. DODGE: I believe so, Your Honor.
9 Yes.

10 (BENCH REQUEST NO. X.)

11 JUDGE MOSS: And with that, I think we can
12 continue. And perhaps -- do you think you have
13 another 20 minutes, or so?

14 MR. VAN CLEVE: I actually just have a
15 few more questions.

16 JUDGE MOSS: Good. We're making good
17 progress.

18 Q BY MR. VAN CLEVE: If you can refer to
19 that page, Ms. Ryan, page 4 of that Exhibit 103
20 C, page 4.

21 A I have the page. Thank you.

22 Q Assuming that this accurately represents
23 the actual oil generation at Fredrickson,
24 Fredonia, and Whitehorn, and I will ask you to
25 accept subject to check that the average of the

0886

1 years 2003 through 1994 for Fredrickson is 1,468
2 megawatt hours. Can you do that?

3 A The average for 1994 through 2003?

4 Q Right, for Fredrickson.

5 A Can you say it again so I can write it
6 down?

7 Q 1,468 megawatt hours.

8 A Okay.

9 Q And I would also like you to accept that
10 the number at the far left, 33,200, is the 200
11 hours of oil burn at Fredrickson for November
12 through February of the rate period.

13 A And does that -- is that consistent with
14 the spreadsheet workpapers that we provided?

15 Q If you can give me one minute, we will
16 confirm that --

17 A Yes, that looks correct.

18 Q I think that comes from your workpaper
19 060; is that right -- 080?

20 A It is correct.

21 Q Would you agree that the 3,000 -- 33,200
22 you are assuming in the rate year for oil burn
23 far exceeds the average per year of oil burn at
24 Fredrickson for the 2003 -- excuse me, 1994 to
25 2003 period?

0887

1 A Yes, I would accept that the projections
2 we have in the file for power costs are higher
3 than the average over the time frame.

4 And as I explained earlier, it is often
5 that we use gas instead of power -- instead of
6 oil. And on a going forward basis, this
7 particular winter we are concerned that the
8 reduction in pipeline capacity on the Northwest
9 pipeline, and the fact that oil would have to be
10 trucked into the facilities, that in absence of
11 having an oil proxy, we wouldn't have appropriate
12 cost to meet peaking days.

13 We don't hold firm transportation for the
14 CTs, combustion turbines, because they aren't
15 expected to fire more than in our example, eight
16 days a year. And it's far more cost effective to
17 have the oil inventory.

18 Q Would you also accept subject to check
19 with respect to the Fredonia plant that if you
20 average 1994 through 2003, that the average of
21 those numbers is 20,717?

22 A Yes.

23 Q And did you verify that the 68,800 is the
24 amount of oil consumption consumed in the rate
25 year for Fredonia?

0888

1 A Yes. That coincides with numbers that we
2 have for Fredonia 1 and 2, and a separate item
3 Fredonia 3 and 4 in our workpaper.

4 Q And could you go ahead and check the
5 Whitehorn number of 33,000?

6 A That is also the same number. You have
7 correctly taken the numbers from our workpapers,
8 and inserted them in this chart or table.

9 Q Would you also accept, subject to check,
10 that the average of 1994 to 2003 period for
11 Whitehorn is 14,054?

12 A Yes, I will accept that.

13 MR. VAN CLEVE: Your Honor, I would like
14 to move for the admission of Exhibits 97 C
15 through 103 C.

16 MS. DODGE: The Company objects to 103 C
17 for the reasons already described.

18 JUDGE MOSS: All right. And the
19 Commission, having considered the exhibit and its
20 use in the proceeding, I will overrule the
21 objection and the exhibits will be admitted.

22 (EXHIBIT 97 C to 103 C RECEIVED.)

23 JUDGE MOSS: And that will bring us to
24 questions from Mr. Cedarbaum, and we also have
25 questions from Public Counsel.

0889

1 MR. FFITCH: We have no questions. Thank
2 you.

3 JUDGE MOSS: Mr. Cedarbaum, go ahead.

4

5 CROSS EXAMINATION

6

7 BY MR. CEDARBAUM:

8 Q Ms. Ryan, if you could turn to Exhibit
9 83 C.

10 A (Complies.)

11 Q On what is labeled page 2 of 31, at the
12 bottom -- in fact, I think with the cover page
13 it's the third page of the exhibit.

14 MS. DODGE: I'm sorry. Which exhibit?

15 MR. CEDARBAUM: 83 C.

16 THE WITNESS: Page 2 of 83 C?

17 Q BY MR. CEDARBAUM: At the very last
18 paragraph, "The PSE customers do not want to be
19 surprised by rising energy costs." Do you see
20 that?

21 A I recognize the phrase, but can you tell
22 me again which paragraph it's in?

23 Q The very last paragraph on page 2.

24 A Okay.

25 Q Is it correct that on December 8 there was

0890

1 a meeting that you participated with Commission
2 Staff regarding these cost plan issues?

3 A No, I am sorry. I did not participate in
4 that meeting.

5 Q No? You haven't participated in that
6 meeting?

7 A No, I haven't participated in any of the
8 cost plan meetings this month.

9 Q With respect to the sentence that I read
10 to you, do you know whether, and if so, when, the
11 Company has established a frame work for
12 quantifying customers' reactions to rising energy
13 costs? And, again, just if you know, because you
14 may not, having not been at that meeting.

15 A We are engaged in working with customers
16 on a survey to ascertain their thoughts on rate
17 stability, hedging costs. Is that what you are
18 referring to?

19 Q Yes. And I guess I wanted to get a better
20 understanding -- as I understand your response,
21 that's a process that is currently being
22 undertaken. It hasn't been completed.

23 A No, that's correct. And we wrote this
24 Data Response -- I am sorry, the Response to Data
25 Request prior to embarking on that survey. We do

0891

1 have feedback, informal feedback from customers,
2 particularly from our commercial, industrial
3 customers that they do look and value price
4 stability so it can help them in their budgeting
5 process.

6 Q I would like to discuss the BPA wheeling
7 chart issue. And if you could turn to Exhibit 82
8 C, which is your rebuttal testimony. And page
9 14, pages 14 and 15, include your discussion of
10 that issue; is that right? I am looking at the
11 section Roman numeral 6, transmission costs.

12 A I am sorry. I think I am on the wrong
13 page. Could you tell me again?

14 Q Page 14 of your rebuttal testimony.

15 A Page 14. Excuse me.

16 Q 82 C is the exhibit number.

17 A Uh-huh. Okay. So I am turned to page 14.

18 Q And is it correct that the dispute between
19 the Company and Staff on the Company's proposal
20 to increase BPA wheeling charges revolves around
21 the notion on whether or not that is a known and
22 measurable amount?

23 A That is my understanding of Dr. Mariam's
24 testimony. I don't have a copy of it, but it
25 sounds familiar.

0892

1 Q Is it correct that in your direct
2 testimony the Company proposed to recover a 15
3 percent increase in those costs which translated
4 into about \$2.2 million?

5 A That's correct. And in ICNU's testimony
6 they put forth a proposal --

7 Q Excuse me, Ms. Ryan --

8 A Excuse me. May I finish?

9 Q I don't think you are answering my
10 question any longer. I asked you in your direct
11 testimony your Company's proposal was for a 15
12 percent increase. I wasn't asking about ICNU's
13 testimony on the subject. So your answer to my
14 question is "yes"?

15 A Yes.

16 Q And in your rebuttal testimony that was
17 filed in November, the proposed increase was
18 reduced to 14 percent which translated to \$1.9
19 million; is that right?

20 A That's correct. And we have provided an
21 update to that last week of 17.7 percent, based
22 upon a settlement of the parties.

23 Q Well, we will get to that. But just to
24 summarize, when you filed your direct, it was a
25 15 percent increase. When you filed the

0893

1 rebuttal, it was a 14 percent increase. When you
2 revised the rebuttal, it went to a 17.7 percent
3 increase; is that correct?

4 A That's correct.

5 Q And you referred to a quote, unquote,
6 settlement. If you could turn to Exhibit 107.

7 A (Complies).

8 Q Is that the settlement that you are
9 talking about?

10 CHAIRWOMAN SHOWALTER: Can you hold for a
11 minute?

12 JUDGE MOSS: We don't have 107 in our
13 notebooks. I'm not sure why. Do you have extra
14 copies, by chance, Mr. Cedarbaum? None of us
15 seems to have it.

16 MR. CEDARBAUM: I don't have -- I don't.

17 MS. DODGE: It was filed last Thursday.

18 CHAIRWOMAN SHOWALTER: Yes, here it is.
19 It's out of order. Mine is after 96.

20 JUDGE MOSS: So it was a Company exhibit,
21 and it was numbered out of sequence. Now, I
22 think we can all find it.

23 MR. CEDARBAUM: This was the
24 out-of-sequence exhibit, but it's part of the
25 Company's prefiled testimony.

0894

1 Q BY MR. CEDARBAUM: So Exhibit 107, is this
2 the settlement that you just referenced?

3 A Yes. This is is a settlement of
4 Bonneville and the parties. And effective
5 January 7 Bonneville will receive signed
6 agreements from all the customers who formally
7 signify their acceptance.

8 And then on January 11, Bonneville
9 proceeds with their process. And that
10 information is provided on page 1 of 16 of this
11 exhibit.

12 Q Okay. I would like to clarify your
13 statement. You said Bonneville will receive
14 agreements. First of all, this letter is dated
15 December 6 from Bonneville regarding its 2006,
16 2007 transmission rate case settlement agreement.
17 And is it correct that it was sent, as stated in
18 the first paragraph, to Bonneville's individual
19 customers and umbrella organizations; is that
20 right?

21 A I would like to clarify when you
22 paraphrased what I said. I believe I said --

23 Q First of all, excuse me. If you could
24 answer my question, and then we will back up if
25 we need to.

0895

1 MS. DODGE: Your Honor, I would ask that
2 the witness be allowed to respond.

3 JUDGE MOSS: Do you not understand the
4 question that you need to go over it?

5 THE WITNESS: I will ask him to repeat the
6 question, but I don't think he correctly restated
7 what I said. So I wanted to clarify that. But
8 if you would like to ask the question again --

9 CHAIRWOMAN SHOWALTER: Also, could you
10 speak up a little bit. It's not coming through
11 as well as it should.

12 JUDGE MOSS: Restate the question for us,
13 Mr. Cedarbaum.

14 Q BY MR. CEDARBAUM: All I asked is that on
15 page 1, is it correct that that letter from
16 Bonneville on December 6 was sent to individual
17 customers and umbrella organizations as
18 referenced in the first paragraph of the letter?

19 A That is what it says in the third line.
20 "We are sending this email to TBL's transmission
21 customers and umbrella organizations," yes.

22 Q For the record, what is an umbrella
23 organization? Do you know?

24 A I don't know. I was not a participant in
25 the discussion. We have included the settlement

0896

1 to demonstrate the rate impact.

2 Q Do you know how many umbrella
3 organizations there are?

4 A As I said, I was not a participant in the
5 discussions.

6 Q Do you know how many individual customers
7 there are?

8 A No, I am sorry. I don't know how many
9 there are exactly.

10 Q If you could drop down to the third full
11 paragraph, the paragraph that starts, On "January
12 11," is it correct that Bonneville characterizes
13 this document as an initial proposal outlined in
14 the settlement agreement?

15 A (Reading document.) They have given --
16 yeah, they called the settlement an initial
17 proposal.

18 Q And they also say that that "TBL," which
19 is the Bonneville Power Administration
20 Transmission Business Line, "will decide whether
21 to proceed with the initial proposal outlined in
22 the settlement agreement based on whether it has
23 received signed agreements from all or nearly all
24 customers by close of business the 7th of
25 January," as you noted earlier; is that right?

0897

1 A Correct. And our expectation is that will
2 be accepted, and we feel this is the best
3 representation of cost as we know it to be. And
4 that's why we filed it.

5 Q But you just told me that you didn't know
6 how many individual customers there were, how
7 many umbrella organizations there were. So what
8 is the basis upon which you say you expect this
9 to be accepted by all of those individual
10 customers, and all of those umbrella
11 organizations?

12 A By a briefing of participants in our
13 Company who were at the process.

14 Q Were you at the briefing?

15 A I received a written briefing.

16 Q And that written briefing from the
17 Company?

18 A From our representatives who participated
19 in the discussions.

20 Q It appears from this letter that
21 Bonneville is looking for, if not complete
22 consensus, pretty close to consensus when it
23 says, "signed agreements from all or nearly all
24 customers"?

25 A I am sorry. Was that a question or a

0898

1 statement?

2 Q That's a question.

3 A Yes. And they do use the words all "or
4 nearly all customers by close of business on
5 Friday, January 7th."

6 Q And then earlier, maybe this is the place
7 where you need to clarify your testimony, I
8 thought I heard you say that the individual
9 customers and umbrella organizations will sign
10 off on the settlement agreement by January 7, as
11 if you knew it was definitely going to happen?

12 A I believe what I said -- and I might ask
13 if we can go back, but I believe that I said that
14 Bonneville expects to get signatures back from
15 all the parties who will be accepting the
16 agreement.

17 Q Is the Company paying rates at the levels,
18 the increased levels and wheeling charges that
19 are in this initial proposal?

20 A The increase in the Bonneville rates will
21 be effective October 1, 2006 at the tail end --
22 sorry, 2005, which is in the latter part of the
23 rate year. And we have applied the 17.7 percent
24 only to that portion of our transmission costs
25 that fall under the integrated resources

0899

1 contract. It's about 80 percent of our costs.

2 Otherwise, the other 20 percent of our
3 transmission costs do not reflect the rate
4 increase. Just those costs under the IR
5 contract, which we know to be costs that we will
6 incur.

7 Q I guess my question is, that you are not
8 incurring -- at the earliest you would incur them
9 October 1, 2005?

10 A That's correct.

11 Q And if rates go into effect in this case
12 around March 1, say, customers will be paying a
13 certain amount of those costs, or will they not
14 be paying --

15 A No. We have only included the rate
16 increase in the months where we see the increase
17 would be effective, subject to check. But that's
18 my understanding.

19 Q And I guess, just for -- it probably goes
20 without saying, but these rates have not been
21 part of -- haven't been approved either by the
22 administrator in BPA in a rate case, or approved
23 by FERC?

24 A This is an alternative to a fully
25 litigated rate case, so it's a settlement

0900

1 discussed between the parties.

2 Q But the rates eventually still have to be
3 approved by FERC, don't they?

4 A I don't know that full process for
5 approval. I'm sorry. I would assume it would be
6 that, but I believe by doing a settlement they
7 then don't have to do the litigated rate case.

8 MR. CEDARBAUM: Thank you. Those are all
9 of my questions. I would offer Exhibits 104, 105
10 and 106.

11 JUDGE MOSS: Apparently there's no
12 objection. Those will be admitted.

13 (EXHIBITS 104 to 106 RECEIVED.)

14 JUDGE MOSS: And let's see, Mr. ffitich,
15 you said you don't have any questions, so I will
16 ask if there are questions from the bench for
17 Ms. Ryan.

18

19 EXAMINATION

20

21 BY CHAIRWOMAN SHOWALTER:

22 Q Yes. I am trying to get a handle on what
23 the corporate credit rating means to the
24 Company's ability to engage in various
25 activities, as distinct from the senior secured

0901

1 credit rating -- I can't think of the exact term.

2 But Mr. Hill and Dr. Wilson, and I think
3 Mr. Baldwin, all engaged in some discussion about
4 which one is important and why. And starting
5 with Company acquisitions of new resources, in
6 that instance, is the senior secured -- what is
7 the phrase, first of all?

8 A It's somewhat complex because the Company
9 has a number of different ratings. The rating
10 that counterparties will typically look at when
11 valuating the creditworthiness of a counterparty
12 is a senior unsecured rating.

13 Q Now, when you say a counterparty, what
14 context are you in? This is my problem. I'm
15 imagining different kinds of activities, and I'm
16 not sure I'm imagining the right buckets of
17 activities.

18 A I can speak best to the activities of
19 hedging risk management. And you asked me a
20 question about the resource acquisitions, and
21 Mr. Markell knows more about that than I do.
22 I will do my best to answer the question.

23 Q Well, actually, if you want to distinguish
24 your testimony by saying, you are not talking
25 about those things, you are talking about the

0902

1 other things; is that correct? And by things, I
2 think I mean there was a fair amount of focus on
3 what it means to the Company when it goes out for
4 actual acquisition of major infrastructure. So
5 maybe what we can do is not talk about that
6 category.

7 Let's talk about the other categories. I
8 did take most of your testimony to be focused on
9 those other categories. Am I right so far?

10 A That's right. Mr. Baldwin and Mr. Gaines
11 and Mr. Markell overlap in terms of addressing
12 the credit challenges and financing acquisitions.
13 And my testimony focuses on the issues associated
14 with risk management, entering into transactions
15 for hedging purposes.

16 Q And just so we fill it all out, hedging
17 what?

18 A Oh, because we're deficit resources in
19 comparison to our load requirements, we're a net
20 buyer of energy. We're buying gas. We're buying
21 power, oil. And we operate in a wholesale market
22 with other companies who have energy to sell,
23 because we're usually a buyer.

24 And in that environment, companies are
25 very careful about how much exposure they will

0903

1 take on with one another. So when you enter into
2 a transaction with a counterparty, not only are
3 you concerned about the price and the delivery
4 terms, and the contract, but you are also
5 concerned about their ability to perform.

6 So the industry develops assessments --
7 let me say that differently. Each of us in the
8 industry look at credit risk management, and we
9 look at each individual counterparty, and make a
10 determination of how much exposure or risk we're
11 willing to have with that counterparty.

12 Q Now, first of all, when you are talking
13 about trading partners, are you talking about
14 both short-term and longer-term transactions?
15 Tell me the environment of trade that you are
16 referring to.

17 A I am referring to trade that could go from
18 a short time frame of next month, or next week,
19 out to a longer time frame of five or 10 years.
20 So these would be gas purchase contracts, power
21 purchase contracts as opposed to an acquisition.

22 Q And now, Mr. Baldwin in response to a
23 question, said that if you -- let's say PSE has a
24 higher credit rating. You would not necessarily
25 want to do business with someone with a lower

0904

1 credit rating, or at least that would be a
2 greater risk to you than to the group or the
3 partner with the lower credit rating; is that
4 correct?

5 A I think that is correct. I would add to
6 that that we look at every counterparty and make
7 an assessment of their financial strength, and
8 the likelihood of their being able to perform
9 their obligations under the contract. And the
10 bigger the contract, or farther out in time, the
11 more exposure there is potentially in that
12 contract and with that counterparty.

13 So we're more comfortable transacting with
14 a strong counterparty that has an A credit rating
15 as opposed to a counterparty that has a lower
16 credit rating, because there's a greater
17 likelihood that the stronger company will be able
18 to perform their obligations throughout the term
19 of the agreement.

20 Q But by the same token, if they are
21 stronger and you are weaker, they are not as
22 interested in you?

23 A Right. There's a hierarchy, a pecking
24 order.

25 Q It would seem to lead toward like trading

0905

1 with like; that is, your bargaining power would
2 make it difficult to trade with someone much
3 higher. At least that higher person will look
4 around for a better partner; is that correct?

5 A You are right on on the second thought
6 there, that given a choice, an A rated
7 counterparty would prefer to transact with
8 somebody that had a stronger credit rating than a
9 company that had a weaker one.

10 In the same token, and here's where it
11 becomes difficult for us, we have to be cognizant
12 of our counterparty. So if we're looking at a
13 BBB minus company that has the same corporate
14 credit rating that we have, we don't want to take
15 on a huge amount of risk with that company,
16 because they are only barely at investment grade.

17 So it's more wise of us to also be careful
18 about credit exposure to counterparties,
19 depending upon their financial strength. It's a
20 way to mitigate the risk of the nonperformance,
21 and in the event of nonperformance, the ability
22 to collect damages.

23 Q In this environment of trading on the
24 wholesale market, what ratings are you and your
25 trading partners looking at? In other words, of

0906

1 the list, there's about five or six that were
2 typically given to a company, what is the one or
3 the ones that make the most difference?

4 A Let me --

5 Q And I am talking about the corporate
6 credit rating and the senior unsecured -- I'm not
7 very adept at the terms.

8 A Okay. I was going to turn to an exhibit
9 which listed our counterparties, and you could
10 see where we were relative to them. And most of
11 the counterparties are significantly better
12 credit ratings than us.

13 But in answer to your question, in our
14 environment, the first thing a credit manager
15 looks at is the senior unsecured credit rating.
16 And that's because when a party enters into a
17 transaction with another party, they are an
18 unsecured creditor. And so they look at the
19 ratings that the credit rating agencies assign to
20 entities of the senior unsecured.

21 During the discussions over this week we
22 haven't spoken about Puget's unsecured -- senior
23 unsecured rating, because we no longer have one.
24 We used to have one, and it was below investment
25 grade. It was a BB plus with S&P, Standard and

0907

1 Poors. We changed our shelf registration, and
2 Mr. Gaines can go into more detail.

3 We now have only the corporate credit
4 rating, and the senior secured, which is a notch
5 higher. Most of our counterparties do have
6 senior unsecured ratings, and that is the norm of
7 the industry to look at those ratings when
8 assessing credit risk.

9 So when we provide exhibits here, we put
10 Puget's credit rating, and it's the corporate
11 credit rating. In most cases, all the other
12 credit ratings are the senior unsecured ratings
13 of our counterparties.

14 Q If PSE has a less desirable credit rating
15 for whatever purpose, one consequence that we
16 have talked about is that the price may be higher
17 to PSE in engaging in that transaction. Another
18 thing you hear about is credit crunch, or I'm not
19 sure that is even the right phrase. But the idea
20 that trading partners themselves are
21 disappearing.

22 In other words, it's not simply a matter
23 of price, but it could be an inability to make a
24 trade at all, or there are fewer people to make
25 it with. And I think what I am trying to

0908

1 understand here is if there are fewer trading
2 partners, is there just one consequence? The
3 price goes up, or could there be a consequence of
4 you simply can't do as much trading per se?

5 A There are two important themes. One is
6 the market liquidity theme, and the other is
7 credit and how does that impact you within the
8 market. The market liquidity, whether there is
9 good liquidity or poor liquidity, can be
10 reflected in the difference between what is the
11 best bid or buy price in the market, as opposed
12 to the lowest offer price, which someone would
13 sell.

14 And if there's a big difference between
15 those two, that will be described as an illiquid
16 market. Or if a market doesn't transact very far
17 in the future, if it's a short-term nature, that
18 would be a measure of illiquidity.

19 The point you raised earlier about credit
20 constraint, if you are a lower credit rating,
21 one, you just can't do as much hedging. So the
22 Company today uses most of its credit to engage
23 in short-term hedging of up to about a year. In
24 our gas portfolio, we can hedge approximately 55
25 percent of our winter supplies, 45 percent of our

0909

1 summer. We could change the ratio a little bit,
2 but that gives you a sense of the scale of the
3 hedging.

4 And in our power portfolio, we can buy our
5 gas and power requirements going out about a
6 year, as well.

7 Q So just, if you say you can't do as much
8 hedging, does that mean for a certain portion you
9 simply wait until the moment that you might or
10 might not need the power, and then you buy the
11 power on the market if you need it, as opposed to
12 planning in advance for certain contingencies?

13 A Well, the first priority is to make sure
14 you have power or gas to serve gas customers, or
15 to fire up the power plants for next hour, next
16 day, next week. So on a short-term basis, we
17 have adequate credit to procure all that we
18 need.

19 And when it's looking forward to locking
20 in prices and entering into purchase transactions
21 that would hedge risk, that we look at and say,
22 well, how much credit do we have, and how much
23 hedging can we do? And I will stop there. Did
24 that answer the question?

25 Q Yes, it prompts actually another question

0910

1 I was going to ask in response to the earlier
2 questioning. When you purchase gas, say this
3 past fall for the upcoming time period, did I
4 understand you correctly that you may purchase a
5 certain amount, but if you get a better deal, if
6 you can make a better deal later, you would
7 replace that amount you bought with something
8 that was more economical?

9 A In the power portfolio we can buy gas from
10 the plants, or we could leave -- not anticipate
11 to run the plants, and purchase power from a
12 third-party if that was more attractive.

13 So as we look forward in hedging in the
14 power portfolio, we look at the relative price
15 differences between power and gas. We look at
16 what we think will be the dispatch rate of all
17 the different facilities. And we also look at
18 for every time frame and different types of
19 instruments, what would give the best risk
20 reduction for the amount of credit that we would
21 be using. Kind of a marginal incremental hedging
22 decision. What would you do -- what is the next
23 best hedge to do?

24 And then once those hedges are in place,
25 and let's use the example where we purchase gas

0911

1 for the summer period, this coming summer. If
2 then -- well, if then, we bought gas, because we
3 anticipated needing a certain volume of gas based
4 on the estimated dispatch rate of the plants this
5 summer, but then if market conditions change, and
6 let's say power prices come down relative to gas
7 prices, then we will say, why don't we optimize
8 this, be cost effective to now sell out the gas
9 that we have purchased, and turn around and
10 purchase the power.

11 So we will optimize the portfolio when we
12 can make an incremental decision beyond the first
13 hedge to improve upon the hedging portfolio.
14 What we don't do -- and I was trying to answer
15 this earlier in the cross, we don't sell the
16 hedge because the market has gone up. Because if
17 we do sell it, what if the market continues to go
18 up? We wouldn't have the protection anymore. So
19 once we engage in the initial hedge, we may
20 improve upon it, but we maintain the hedge in the
21 portfolio.

22 And, frankly, that's because we are not
23 buying over and above what we need. We're buying
24 to meet the load. So we don't find ourselves in
25 a place where we have surplus hedges.

0912

1 Q Okay. I am also trying to get an
2 understanding of the history of the Company's
3 credit ratings, and this Company in particular.
4 First, do you have a sense of the credit ratings
5 of this Company over some long period of time,
6 let's say the last 15 years?

7 A I don't have as much knowledge of that as
8 Mr. Gaines does, so you may want to ask him more
9 about that. It is fair to say that credit
10 ratings have become much more important
11 subsequent to the collapse of Enron, and some of
12 the other merchant companies. So the focus on a
13 company's credit rating has increased in
14 importance since 2001, 2002.

15 Q So is it fair to say that because of
16 the -- volatility, might be the wrong word, but
17 that in the electric industry, it seems, anyway,
18 it seems that there are or has been much more
19 volatility in the credit of all members of the
20 industry? And is that what makes it more
21 important?

22 In other words, was life 10 years ago, was
23 it easy enough to find a trading partner that it
24 didn't matter as much what your credit rating
25 was, or if you had a similar credit ratings,

0913

1 would people have worried the same way?

2 A Well, there have been a couple of trends.
3 More recently we have seen the new participation
4 in the markets, the energy markets of banks,
5 investment banks, and commercial banks. They
6 tend to transact in financial derivatives, energy
7 derivatives. And they are more demanding,
8 perhaps others would say sophisticated, in their
9 assessment of the credit and credit risks. It's
10 been a key part of their business strategies for
11 many years.

12 So have you a new injection of new parties
13 who make credit management their business, in
14 addition to investment banking and other lines of
15 business.

16 At the same time there was a radical
17 change in the credit rating of a lot of the large
18 energy firms. So I will give you a couple of
19 examples. Williams Company was a strong
20 investment grade rated company, and they have a
21 large amount of energy gas production, and
22 interstate and intrastate gas pipelines, and
23 generation positions across the country, and
24 large trading floor and large trading activity.

25 And they are -- I have it in here, but

0914

1 subject to check, they, I think, have a credit
2 rating of a BB or maybe BB plus. They are one of
3 many. El Paso Energy, which is another very big
4 energy company with pipelines and production,
5 same thing for them, and Mirant.

6 And there are eight to 10 companies that
7 suffered significantly, and a lot of it was
8 because they had overextended into merchant
9 power, and they built generation during the 1999,
10 2000, 2001 time frame, and there was a huge
11 overbuild. And then the market collapsed and
12 that's caused a lot of financial woe for them.

13 Duke is another company, which as a side
14 bar we haven't seen -- not much in the way of new
15 generation constructed because of that. The
16 industry is in a bust cycle, part of the cycle.

17 Q Well, but is a BBB senior unsecured credit
18 rating today as good and useful as it was 10
19 years ago, or is the not?

20 A I think it's much more useful today.

21 Q Does that -- I guess if I were to look
22 back, is there any value to be gained -- maybe
23 that's one way to put it, by asking the question
24 historically where have utilities been, or is
25 that not a useful metric because the world is

0915

1 different? I would think on the surface that
2 Standard & Poors and Moody's BBB means BBB,
3 meaning a certain degree of risk.

4 But I think where I am struggling is,
5 well, a certain degree of risk within what
6 environment? Are they taking into account the
7 environment, or BBB is different today than it
8 was 10 years ago because the environment is
9 riskier? I wouldn't have thought that would be
10 the construction. I would have thought that a
11 BBB is a measure of riskiness.

12 A As to how the rating agencies have changed
13 over the years and their view of companies, I
14 would defer to Mr. Gaines. In terms of how
15 counterparties look at one another and the
16 importance of the strong credit rating, I think
17 it's much more important today.

18 And where a couple of years ago a BBB
19 minus, we may have -- I wasn't with the Company
20 prior to late 2001, but in my industry experience
21 companies didn't focus a lot on your credit
22 rating.

23 I would also say, though, that the
24 utilities, I believe, had much stronger credit
25 ratings in the BBB plus to A minus range. So it

0916

1 is rather stark to look at us as a BBB minus
2 compared to the entities in the wholesale market
3 who are, for the most part, BBB plus or better
4 credit ratings. And it limits how much we can
5 transact on an open credit basis.

6 And the benefits of hedging that we put
7 into the rebuttal testimony was to try and
8 demonstrate that with an extension of additional
9 credit to the Company resulting for an upgrade of
10 our current rating up two notches, we estimated
11 it would be \$430 million of additional credit
12 that we could deploy into hedging, and we provide
13 various scenarios.

14 The benefits we put in here, I think there
15 may be some confusion with what came out with
16 Mr. Gaines's testimony, are annualized
17 benefits --

18 Q This goes back to the 10-year net present
19 value?

20 A Correct. There's a reference in Exhibit
21 84 that says annualized benefits.

22 Q So does that mean --

23 A It's on page 13 of 15.

24 Q -- it's the net present value of 10 years
25 of benefit annualized?

0917

1 A Yeah. And I will describe how we
2 approached it. For the hedging scenarios we
3 developed, we provided some illustrative
4 transactions that range from one-year
5 transactions up to 10-year transactions. And the
6 way we come up with the annualized benefit, let's
7 use an example of a seven-year transaction, a
8 seven-year gas purchase contract.

9 We looked at the hedge on a net present
10 value and divided by seven and said one-seventh
11 of that is the annualized benefit of that
12 particular transaction. So we developed the
13 annualized number by taking that approach to all
14 the transactions that were in the scenarios.

15 Q But I think you pointed out elsewhere in
16 your testimony that to some degree trying to
17 quantify the benefits of a hedge is almost
18 impossible, because you don't know whether the
19 events you are hedging against ever play out.
20 Isn't that the case?

21 A It is the case, but I qualify that a
22 little bit. We think it's really important to
23 enter into these hedges, because there has been
24 volatility in the market, not just going back to
25 the Western Energy Crisis, but over an extended

0918

1 period. So it's important to have the capacity
2 to enter into hedges.

3 When we look at all the supply demand
4 fundamentals and the risk analysis, we feel the
5 capacity to do that today is very limited. And I
6 have to go back to your question. Did I --

7 Q Well, it was about the degree to which you
8 can ever quantify hedging benefits, in the sense
9 that you are hedging against a probability of
10 something happening. Maybe you do know what the
11 probability of it happening is? I don't know.

12 A It is difficult to ascertain the benefits.
13 Because dependent on what point you pick in terms
14 of saying where prices go, that defines the
15 benefits.

16 So we have taken a couple of different
17 approaches both in the rebuttal testimony and in
18 a data request. And all of them are valid. They
19 show directionally that one engages in risk
20 management transactions, hedging transactions to
21 protect against a significant price move.

22 And we can see that there's been
23 volatility over a period of time in the Western
24 gas markets and the Western power markets. We
25 tried to pick examples that made sense, had

0919

1 relevance.

2 One of the scenarios we used was to model
3 with a price stress of 30 percent in the next 12
4 months, and 20 percent beyond that time frame.
5 And it was a methodology that S&P is using for
6 liquidity assessment of energy companies. We
7 looked at prices over the last year and said,
8 well, they have moved 60 percent in the first 12
9 months, and 40 percent beyond that. So that has
10 happened already. What are those benefits, if we
11 assumed that?

12 So it is true that there's no one
13 methodology to measure it, and the benefits --
14 and we do provide a range of high, medium, low --
15 they are somewhat subjective, but we believe the
16 benefits are real.

17 The number may be hard to pinpoint as a
18 single number, but they are driven by protecting
19 against negative price movements that we have
20 seen before.

21 Q Can you turn to 14 of your rebuttal?

22 A (Complies.)

23 Q You have a diagram on the top half of the
24 page. I just don't know how to interpret this --
25 Oh, it's the second exhibit. It's Exhibit 84.

0920

1 A Would you like me to talk to it?

2 Q I just don't know how to go about -- and I
3 see a little figure, a bigger one, and a bigger
4 one. And I don't know how to make heads or tails
5 of that diagram.

6 A Okay. This is a confidential piece, but I
7 think I can speak to it without touching on
8 matters that would be specifically confidential.
9 I think I can speak to it grammatically.

10 We looked at the amount of credit we
11 believed would be extended to the Company by
12 physical counterparties, as well as by financial
13 counterparties. So the key underneath the graphs
14 has a reference there. There are four boxes, and
15 it says, Ratings Upgrade from BBB Minus or
16 Current Rating Up To BBB. And it says
17 physical --

18 Q And physical means -- meaning that there
19 would be more people willing to sell you more
20 power or gas?

21 A What we did with our physical
22 counterparties is we believe we're transacting
23 with most everybody in the market. But that with
24 a stronger credit rating they would be willing to
25 transact more, that they would extend more credit

0921

1 to Puget Sound Energy.

2 And then we looked at -- for financial
3 counterparties, the ones that we currently
4 transact with, would they extend more credit to
5 us. And then there are more financial
6 counterparties out there than we currently do
7 business with so we made an assumption there that
8 we could also attract some new counterparties
9 with a higher credit rating.

10 This chart is capturing a lot of
11 information. It's looking at what we believe to
12 be the incremental hedging benefits if we were
13 upgraded, and then the benefits are provided
14 as a result of transactions with physical
15 counterparties and financial counterparties. We
16 also provide some information about what would
17 happen if we're downgraded.

18 Q I see, I believe, four different colors of
19 shading. There's a box that is the lightest
20 shade. There's a little, thin rectangle below
21 that. The box that is a slightly darker shade,
22 and then on the upper part of each figure is a --
23 the third darkest shade, that has a kind of a
24 parabola, or something about it. And then
25 there's the darkest shade that has something that

0922

1 looks like a missile.

2 And what are each of those boxes trying to
3 show, or what are they compared to? Where is the
4 status quo, if there is one?

5 A If you look at the numbers below the
6 shaded bars --

7 Q Yes.

8 A The top box, and let's look at the first
9 column that is labeled Bank.

10 Q Yes?

11 A So that's the low end of our estimates.

12 Q And what does that mean, Bank?

13 A What we did is internally we did a price
14 stress of the 30 percent for the first 12 months,
15 and 20 percent thereafter, that was using the S&P
16 methodology that they had in their liquidity
17 assessment. And then also in the 60/40. But
18 we --

19 Q 60/40 what?

20 A We took the price -- the transactions
21 we're looking at are a number of different
22 transactions that have a term, a delivery period
23 that begins in one year. And some of them are
24 one-year transactions, some are three years, some
25 are five-year transactions, and some are 10-year

0923

1 transactions. And we assumed that we buy them
2 at a price, and we used a price curve that is
3 consistent with what the resource planning team
4 is using. And then we said, you enter into the
5 transaction, and what if the market moved?

6 So the market moved up 13 percent for the
7 first year, and then 20 percent from the prices
8 at which we entered into these theoretical hedges
9 in the years thereafter.

10 Q So just tell me, what does 30 percent, 20
11 percent, what are the terms attached to, those
12 percentages?

13 A So for example, this isn't the exact
14 price. I am doing this theoretically. If the
15 first year price of the contract -- the
16 theoretical contract was \$5 and we would say,
17 well, 30 percent price stress of that would be --
18 30 percent of \$5, or \$1.50. So that the benefit,
19 at least on the first year with a hedge would be
20 \$1.50.

21 And then let's say the second through 10
22 years happen to be the \$4. We would say, and a
23 price stress of 20 percent on \$4 is 80 cents. So
24 there would be a hedging benefit of 80 cents for
25 the subsequent years of that 10-year contract.

0924

1 It is a fairly simplistic price stress.

2 And then we did the same thing with a
3 higher price stress, the 60 percent, multiplied
4 on the first year, 40 percent on the years
5 thereafter on the sample transactions.

6 The Bank, to go back to your earlier
7 question, we asked a banking counterparty for
8 this list of gas and power transactions. What do
9 you see to be the hedging benefits associated
10 with those? And then we took their answers and
11 aggregated them in the same scenarios that we
12 built, and provided that as another data point
13 for potential hedging benefits.

14 So is a way to look at these three
15 different figures, is that -- we will call it
16 column 1 and column 2 and column 3 -- is that it
17 shows the range of benefits under these different
18 scenarios?

19 A That's correct. So that in the event that
20 we look at what happens in an upgrade of
21 incremental two notches up, we add the physical
22 and financial -- I'm looking under the Bank
23 column -- and that adds up to \$21.9 million --

24 MS. DODGE: Could I ask, are we --

25 CHAIRWOMAN SHOWALTER: That might be

0925

1 confidential. I don't need the numbers. I think
2 you can stick with the diagrams.

3 MS. DODGE: It might be easier to walk
4 through the chart if you could refer to numbers,
5 because then you would know you were tracking.
6 That would be my only suggestion.

7 Q BY CHAIRWOMAN SHOWALTER: That's okay. I
8 think in some sense if you look at the dollar
9 values along the left-hand side, that's almost
10 like line numbers. And you could direct me by
11 column in the row as defined by those dollar
12 numbers where you are looking.

13 I still haven't got it conceptually. I
14 see what is happening is the very darkest is
15 attempting to show the consequence of a
16 downgrade. And the next to the darkest is
17 attempting to show the consequence of an upgrade.
18 And since the upgrade is going up in value, the
19 downgrade is going down in value, I take it that
20 is some indication --

21 A That is correct. If there's a zero line
22 that is a horizontal line you see in between --

23 Q Yes. Yes.

24 A Positive 10 million and negative 10
25 million.

0926

1 Q Uh-huh.

2 A So the numbers below that are an example
3 of what we believe the cost to be in the event of
4 a downgrade. And those are a combination of
5 costs -- we're saying we would be using our
6 current credit. In the event of a downgrade,
7 parties would ask us to post collateral, and
8 here's the cost to post that collateral. And
9 it's broken down into the physical transactions
10 and the financial transactions.

11 So those would be the two bottom rows that
12 have negative brackets on them in the key
13 underneath the chart.

14 Q Okay. I recognize this is discussed in
15 the testimony that is preceding this chart, and
16 so we will study it more carefully. But footnote
17 No. 1 to this chart suggests that there was a
18 survey.

19 If this is already in your testimony, then
20 just tell me if it is, and I will find it. But
21 the source of your information here is people
22 that you asked, that PSE asked about this; is
23 that correct?

24 A Correct. We went to all of our
25 counterparties and asked them how much credit do

0927

1 you extend to us today, and they all provided
2 that information. And then how much credit would
3 you extend to us in the event we were upgraded,
4 and our credit rating improved? And some of them
5 provided that information. A few were
6 uncomfortable, and they said, "Well, I can't just
7 tell you that. I have to know more about why you
8 received the upgrade."

9 And we also asked what they would do in
10 the event of a downgrade. And it's interesting
11 to note, that the amount of credit that we lose
12 in a downgrade is more significant than the
13 amount of credit we gain with a one-notch
14 upgrade.

15 But that makes sense that we're just at
16 investment grade today. There's a perception of
17 a cliff when you go below investment grade.

18 Q And how many total partners are reflected
19 in this chart?

20 A (Looking at documents.) We have a couple
21 of exhibits that provide the list of the
22 counterparties and their responses.

23 Q Is that Exhibit 85?

24 A Yes, that's correct. We have -- there's
25 an exhibit for gas counterparties. There's

0928

1 information for power counterparties, and also
2 for financial counterparties.

3 Q And then I think it's on page 2 of this
4 same exhibit, but this was using a credit rating
5 going from BBB minus to BBB plus, and is that the
6 corporate rating?

7 A That is the corporate rating, yes.

8 Q I just had one more question, which is on
9 your direct, page 19 on lines 4 to 5 -- 3, 4, and
10 5. This is an example you are giving?

11 A This is Exhibit 71?

12 Q Yes, I am sorry.

13 A Uh-huh.

14 Q So if the gas were delivered over a
15 10-year period at \$4.35, and the market moves a
16 dollar to \$3.35, then that translates into a 30
17 million net present value market-to-market
18 exposure.

19 And is what you mean by that is that you
20 bought higher than the market turned out to be?
21 I couldn't quite figure out the direction going
22 from \$4.35 to \$3.35, and why that is an exposure
23 for you.

24 A Usually in the big scheme of things it's
25 beneficial when prices go down. But in this

0929

1 instance where we're a buyer, if prices go down
2 subsequent to us entering into a transaction with
3 a counterparty, the counterparty is concerned
4 Puget will still perform under this agreement.

5 So if we had a counterparty who extended
6 \$30 million for us, which is at the high end of
7 the range, most of the credit extended to us
8 ranges between 5 million and 15 million, the
9 counterparty would do a calculation of a
10 market-to-market and say, "We have a \$30 million
11 exposure to Puget. If anything happens and they
12 don't perform, we will have these damages.
13 Because if we want to resell this, we no longer
14 have the benefit of the \$4.35 contract price with
15 Puget. The market is now at \$3.35."

16 Q So if you fall through because of
17 financial problems, you owe them \$4.35, but they
18 can only sell it for \$3.35, so that's the
19 exposure?

20 A Exactly.

21 Q But it seems like they are exposed, you
22 aren't. It's a net exposure to your partner; is
23 that right?

24 A Correct. So we bought it at \$4.35, and
25 the market moves down, we continue to perform at

0930

1 \$4.35 because that's what we committed to.

2 But their concern would be if we didn't
3 perform, then they would have this exposure. And
4 the market looks at this not only as an actual
5 market-to-market, in other words, yesterday the
6 price was \$4.35 and today the price is \$3.35,
7 they also look -- industry purchasers also look
8 at it as a potential risk?

9 So when they are extending credit, if they
10 have decided we're comfortable doing up to \$10
11 million of exposure with Puget, they are not
12 going to be very interested in doing a deal that
13 has this kind of exposure, because this is in
14 excess of the open credit that they are
15 comfortable extending to the Company.

16 Q So does this mean if you lock in the
17 prices at some kind of rate, and then the market
18 price goes down, that then at the point it's gone
19 down, that itself can trigger this requirement on
20 line 6 to post collateral?

21 A Yes. An actual move can trigger that.
22 And then on a prospective basis -- I'm sorry.

23 Q So I hadn't realized this. In other
24 words, as time goes along, your credit rating
25 makes a difference as to whether something will

0931

1 trigger in response to the current market price,
2 not particularly either the price or your
3 standards at the time that you entered
4 the market -- or entered the transaction. I
5 mean, they want to know how are you doing now
6 relative -- and how has the price moved since we
7 first entered into this deal?

8 A That's correct.

9 CHAIRWOMAN SHOWALTER: I didn't understand
10 that. Thanks. That's all my questions.

11 JUDGE MOSS: Before we have any further
12 questions, while we're still on this page, you
13 earlier had corrected the 36 million on line 5.
14 I assume that correction would also apply to the
15 references on line 6?

16 THE WITNESS: Yes, that's correct.

17 JUDGE MOSS: Thank you.

18 COMMISSIONER HEMSTAD: I have only one
19 question.

20 EXAMINATION

21

22 BY COMMISSIONER HEMSTAD:

23 Q I believe you testified in response to a
24 question from Mr. Van Cleve that the market is
25 trending up. Isn't -- earlier I had heard that

0932

1 the market more recently is trending down?

2 A Both are correct. The market went up
3 significantly in October. It has come down, but
4 the three-month average price ending December 13
5 is still higher than the price we submitted in
6 the rebuttal.

7 And we have completed the bench request.
8 I think it's going through processing. The price
9 is \$6.15 using a three-month price ending on
10 December 13. And I believe we submitted
11 originally a price of \$5.60. I say originally --
12 excuse me, to clarify that, \$5.60 in rebuttal
13 testimony.

14 Q In your operations, do you have any views
15 on the question of the efficiency of the futures
16 market?

17 A Uh-huh. I'm not a statistician. Given my
18 professional experience, I believe the futures
19 market is relatively efficient.

20 When we compare forecasted prices that are
21 prepared by some of the best thought of
22 consulting companies, and we happen to subscribe
23 to two of them, a company called PIRA and another
24 called CERA, C-E-R-A, Cambridge Energy Research
25 Associates, what we notice is that their

0933

1 forecasts when they are released very much track
2 the forward markets.

3 And that makes sense, because they are
4 using information in the markets about projected
5 supply and demand to develop their price
6 forecasts. And participants in the market have
7 access to very much the same information, and
8 that is driving their projections of the forward
9 price.

10 Over time we find that the futures prices,
11 which we do use for setting up the forward
12 prices, there's a market every business day so we
13 can update prices. And there's also prices by
14 month. And so when a rate year, like this rate
15 year is March through February, it's not a
16 calendar year, we can use forward prices. The
17 forecasts tend to be more in blocks of annual
18 pricing.

19 But going back to my point, I believe
20 there is efficiency in the market, and in the
21 natural gas futures market.

22 Q Dr. Mariam, I believe testified that the
23 more recent market prices have risen, but the
24 supply and demand balance is largely the same.
25 Do you agree with that?

0934

1 Yes and no. I think he's correct in
2 that there have been small incremental changes
3 on year -- say, from 2002 to 2003, and 2003 to
4 2004. There's been a small uptakes of a couple
5 of percentage in demand. And a very small
6 change in supply going down, maybe. But only
7 one or two percent per year.

8 So if you are looking in absolute terms,
9 they don't seem very significant. But the issue
10 here is that the North American Gas Market, the
11 production capacity, the utilization of
12 production capacity is almost at full capacity.
13 And we're seeing -- and the demand is close to
14 the production capacity.

15 So when demand ticks up a little bit,
16 there's not more supply because the wells -- the
17 producers are already producing the wells at a
18 very high production rate. And there's a lot of
19 discussion in the market, and also among policy
20 makers, about the importance of having fortified
21 natural gas imports, or more pipeline supplies,
22 because more supply is needed to basically meet
23 this increasing demand.

24 So global oil markets are similar in that
25 there is a -- there are a lot of reports out

0935

1 there of production capacity maximization. And
2 when we have both the oil markets and the gas
3 markets in this type of scenario, it creates
4 volatility in the prices. So I think he's
5 correct about the percentages, but it makes sense
6 to me that we have this volatility because of
7 where the supply and demands are, and where we
8 are relative to production capacity.

9 COMMISSIONER HEMSTAD: Thank you. That's
10 all I have.

11

12 EXAMINATION

13

14 BY COMMISSIONER OSHIE:

15 Q Ms. Ryan, I want to clarify a couple of
16 things, and we can start with the issue of -- at
17 least my issue with financial hedges. And it's
18 really how that contract is performed and whether
19 consideration is paid up front with the financial
20 hedge, or whether there is payment obligation at
21 some date in time -- I suppose it would depend on
22 whether you are buying an option, or I don't know
23 what the term is, a put of some kind.

24 So if you buy a physical hedge for natural
25 gas, do you pay for that hedge up front, or do

0936

1 you have to post credit for that? You pay a fee,
2 and then post credit?

3 A With a physical contract, when it's a
4 fixed price contract, you pay after the delivery
5 occurs.

6 Q I think I made a mistake. What I meant
7 was the financial hedge. Excuse me. Let's start
8 with the financial.

9 A When a financial hedge is a fixed price
10 hedge, and the terminology for that that is
11 sometimes used is a fixed price swap. But we
12 will call it a fixed price contract. Parties
13 agree to the price, and they agree to the volume,
14 and they agree to the commodity, and they agree
15 to the location. And you pick an index that is
16 representative of the market.

17 So for example, we engage in Sumas
18 transactions. And we will use the posting price
19 of a publication called Inside FERC Gas Market
20 Report.

21 So if we entered into a contract for
22 next month with a counterparty, and let's say
23 the price was \$5, and so it will settle on the
24 January posting, if the price is higher, \$5.50,
25 the counterparty will make a payment to us of

0937

1 the difference between our contract price of \$5
2 and the index posting price of \$5.50. So it
3 will be a payment of 50 cents times the number
4 of units. And similarly if the price drops and
5 it was to go down to \$4.50, we would make a
6 payment to the other party.

7 And we enter into those transactions to
8 mirror -- to go along with physical transactions
9 that we make on an index price basis. So we may
10 have the \$5 transaction with a financial
11 counterparty, and then we will have a contract
12 with a gas supplier. And the agreement is that
13 we will pay the gas supplier on the first of the
14 month January index price. We don't know what it
15 is yet. For us, we have locked in our price of
16 \$5, because if the price settles at \$4.50, we
17 will make the 50 cent payment to the bank
18 counterparty, but we will be paying the physical
19 supplier \$4.50.

20 So whether the price goes up or down, the
21 two transactions together provide a hedge
22 together, and help us by locking in the price at
23 \$5.

24 Q And let's go to the financial side. So
25 there's consideration for the right to exercise

0938

1 the hedge, or for the hedge itself, let's put it
2 that way, so that will be paid up front?

3 A That's correct. That would be for a
4 transaction that would be an option. Where, as
5 you have described, if we bought a put, which
6 would protect against prices falling, or a call
7 that would protect against prices going up, so
8 some kind of option premium, there's a premium.
9 And it's typically paid up front.

10 And then when you come to the delivery
11 period, and there can be these options in either
12 physical or financial markets, then you decide "I
13 would like to exercise that."

14 So you have the right to buy -- if prices
15 keep going up, you would exercise your right to
16 buy at that fixed price. Again, let's say it was
17 a call option, the right to buy at a \$5 strike
18 price.

19 Q So the first situation that you described,
20 and in that situation there would be some
21 reconciliation of what was owed by either party
22 when the price was known, and the delivery was
23 taken of the gas?

24 So in other words, if the price increased
25 at \$5.50 from \$5, you would receive a payment

0939

1 from whatever institution or party you had
2 executed the contract with for your end of --

3 A That's correct. And in the physical
4 contract we would pay the counterparty, the
5 supplier to us, the full \$5.50, and they would be
6 delivering over the month.

7 Q And so is there a requirement under the
8 first situation that we talked about that the
9 Company post credit to the counterparty, or the
10 counterparty with you?

11 A Very few of our counterparties extend zero
12 credit to us. The only exception I can think of
13 is one of the gas pipelines. So they do extend
14 some portion of open credit, and that's what we
15 use for the hedging activity we engage in.

16 So, no, they don't require us to prepay or
17 post collateral as long as their exposure to us
18 is under the level that they have established.

19 Q Now, in a physical gas delivery, the
20 Company would accept the commodity, and then
21 there would be a reconciliation at a later date.
22 Let's say 30 days from the time of the delivery
23 to where the Company would actually have to pay
24 the cash to the counterparty?

25 A That's correct.

0940

1 Q Is that a common term, 30 days?

2 A Uh-huh.

3 Q To reconcile the account?

4 A It's slightly different than that. We pay
5 on the 25th of the month following the delivery
6 period. So we pay February 25th for the month of
7 January deliveries.

8 Q So that's where you described the \$5 to
9 \$15 swing, and credit exposure with any credit
10 party, because that would be the amount that you
11 would be obligated to pay that party within any
12 given month?

13 A Right. We look at the credit. There are
14 different slices in time. Let's use the example
15 of a \$10 million credit extended to us, and let's
16 say we had a transaction occurring where we
17 received delivery last month in November. We're
18 continuing to receive delivery from this
19 counterparty in December, and we have a forward
20 transaction with this counterparty for January.

21 So the counterparty looks at all of these
22 contracts. They will look at the product they
23 have already delivered, and take the contract
24 price, multiply that, and they will be looking
25 for the full face value.

0941

1 That's an obligation we have to pay them.
2 For the deliveries occurring this month they will
3 calculate every day of delivery, and monitor as
4 we're marking through the month what our
5 obligation will be to them for their deliveries
6 this month. And for the contract that is in
7 January they will do a market-to-market where
8 they say, "Well, we entered in that contract at a
9 certain price, and here's the current market, and
10 look at that difference." And they also are
11 likely to look at where the market could go.

12 So it might be that prices have gone up 50
13 cents, but that doesn't mean that they will stay
14 there in January, and may correct or change. So
15 they also do what we call potential exposure
16 assessment for the forward transaction that no
17 delivery has occurred on yet.

18 Q Now, assuming that the price would go
19 down, is it common for the counterparty to net
20 out its exposure?

21 A Absolutely. And we try to enter into
22 netting agreements with parties, because it frees
23 up more credit that way.

24 Q I would like to go to your Exhibit 74 C.

25 A (Complies.)

0942

1 Q On page 1 of 2, it's a confidential
2 exhibit. And you have on the right-hand column
3 your list of credit approved power and
4 counterparties as of March 2004. A couple of
5 questions about that.

6 One is, has that list been expanded since
7 March? And I believe you filed some testimony
8 that it contained names of other counterparties,
9 but maybe just give us -- or give me some sort of
10 range. Has it been expanded by another five or
11 six or three or four?

12 A We have no additional power
13 counterparties, and we have a couple of
14 additional gas parties and financial
15 counterparties. And I can look for the exhibit
16 if you --

17 Q No, that's fine. I can find it in there.
18 One thing that I would like to focus on a bit, I
19 don't see in your list of counterparties any of
20 the Mid-Columbias, and so there's got to be an
21 explanation, either they don't want to contract
22 with you any more than they are already obligated
23 to, which I doubt, but they are not on the
24 list --

25 CHAIRWOMAN SHOWALTER: Do we need to be

0943

1 careful about what is on here as confidential, as
2 what is not sensitive?

3 THE WITNESS: It might be better -- I can
4 answer the question, but I will be talking about
5 a counterparty that might be more appropriate to
6 do that confidentially, or I can try to answer it
7 without --

8 COMMISSIONER OSHIE: Well, I think there's
9 some obvious counterparties that aren't on your
10 list. If we have to go into confidential
11 session, let's do that.

12 THE WITNESS: I can answer thematically
13 why they are not on the list.

14 MS. DODGE: Can I request we go into
15 confidential session, because it's quite
16 important matters, and at the same time it's
17 quite important that they remain confidential.
18 And there's a lot of detail.

19 JUDGE MOSS: All right. Anyone who is
20 present in the room who is not a signatory to the
21 appropriate nondisclosure agreements under the
22 protective order that is in effect in this
23 proceeding will need to leave the room, and we
24 will send somebody out in the hall to let you
25 know when it's okay to come back in.

0944

1 I'm going to mute the send function of the
2 conference bridgeline, because we cannot be
3 certain here who is on that line. So you will
4 have to do without hearing for a few minutes.

5 And, of course, the court reporter knows
6 that this portion of the transcript will have to
7 be under seal until we move out of confidential
8 session.

9 (The following proceedings are
10 CONFIDENTIAL - FOR ATTORNEYS' EYES ONLY.)

11

12

13

14

15

16

17

18

19

20

21

22

23

24

25

0945

1

2

3

4

5

6

7

8

9

10

11

12

13

14

15

16

17

18

19

20

21

22

23

24

25

0946

1

2

3

4

5

6

7

8

9

10

11

12

13

14

15

16

17

18

19

20

21

22

23

24

25

0947

1

2

3

4

5

6

7

8

9

10

11

12

13

14

15

16

17

18

19

20

21

22

23

24

25

0948

1

2

3

4

5

6

7

8

9

10

11

12

13

14

15

16

17

18

19

20

21

22

23

24

25

0949

1

2

3

4

5

6

7

8

9

10

11

12

13

14

15

16

17

18

19

20

21

22

23

24

25

0950

1

2

3

4

5

6

7

8

9

10

11

12

13

14

15

16

17

18

19

20

21

22

23

24

25

0951

1

2

3

4

5

6

7

8

9

10

11

12

13

14

15

16

17

18

19

20

21

22

23

24

25

0952

1

2 END CONFIDENTIAL SESSION/BEGIN OPEN PROCEEDINGS

3 JUDGE MOSS: And that does complete
4 questions from the bench, I take it. Is there
5 any follow up at all based on the questions?

6 MR. CEDARBAUM: Not at this time.

7 JUDGE MOSS: Mr. Van Cleve.

8 MR. VAN CLEVE: No, Your Honor.

9 JUDGE MOSS: Any redirect.

10 MS. DODGE: Just a small amount, Your
11 Honor.

12

13 REDIRECT EXAMINATION

14 BY MS. DODGE:

15 Q Ms. Ryan, first, I wanted to follow up
16 on a question in which you discussed the
17 Company's use of PIRA and CERA forecasts. You
18 mentioned with respect to market efficiency,
19 that those tend to track the forward markets
20 when issued, or something to that effect. Does
21 that tracking hold true over time?

22 A Over time the actual spot prices are
23 different from the forward market prices and the
24 forecasts. So to the degree that the forecasts
25 are reflecting the forward markets at the time

0953

1 they are developed, there's that same difference
2 between them and the spots prices.

3 So directionally there's really not much
4 difference between the ability of the forecast to
5 actually project what the spot prices would be,
6 and the forward market taken about the same time.

7 Q But by over time, I mean if you were to
8 revisit those forecasts several months later, are
9 they continuing to track the forward markets?

10 A Well, I think someone used the word
11 stale -- maybe it was Dr. Dubin. And I think
12 that's a good adjective to use for the forecasts,
13 because they are not updated frequently. They
14 become old. And the forward markets continue to
15 march along.

16 Q Getting back to the combustion turbine oil
17 issue for the moment, there was some discussion
18 regarding why peaking costs are projected outside
19 the Aurora model. And why doesn't the Company
20 deal with peaking costs inside the Aurora model?

21 A Well, the Aurora model takes a price input
22 of a gas price that is a monthly price. And
23 that's helpful for projecting average costs. To
24 the degree that there is a demand spike, a
25 peaking event, Aurora doesn't effectively model

0954

1 that very well.

2 The oil prices, by the way -- I mean, we
3 hadn't really talked about planning for extreme
4 peak. And I did get a question from Mr. Van
5 Cleve over revenues. And my department focuses
6 on power costs, and we have a revenue
7 requirements team. And Mr. Story could speak
8 more to it.

9 But revenue or projections are based on
10 historical data that include winter peaking
11 events. So I think winter peaking events are
12 captured in the revenue projections or the
13 revenue requirements.

14 The power cost planning that we have, we
15 focus on meeting average load, but we also focus
16 on having costs -- not costs, but the capacity to
17 serve customers on peaking days.

18 Q And then there was -- you had stated a
19 couple of times that you used the combustion
20 turbine oil cost as a proxy. Can you explain
21 what that means?

22 A Yes. We have oil inventory, and we have a
23 projection of eight days. That's the 200 hours
24 of peaking -- capacity to meet an extreme peak
25 event.

0955

1 And the oil inventory is an important back
2 up. If there is a winter peaking event, and
3 there is no available uninterruptable
4 transportation on the gas pipeline supply system,
5 we have the oil, and we can rely on the oil. And
6 the pricing on the oil is not significantly
7 different than the forward winter gas prices.

8 However, it might be that we never use
9 that oil. And, in fact, last year we only used
10 oil in January when we couldn't access gas, and
11 more times than not, we actually use gas or buy
12 power in the market.

13 So the budget item there for oil is
14 inclusive of other sources of energy to meet that
15 peaking event.

16 MS. DODGE: That's all.

17 JUDGE MOSS: Mr. Van Cleve.

18 MR. VAN CLEVE: I would like to ask one
19 follow up on that. We had a Records Requisition
20 request for the Company to identify where in its
21 case that these revenues from these peak load
22 experiences are reflected in the rates, and is
23 that something that that answer was intended to
24 provide? Or is there going to be an additional
25 answer?

0956

1 MS. DODGE: Was there a Records
2 Requisitions outstanding on that topic?

3 MR. VAN CLEVE: I think there was.

4 MS. DODGE: I don't recall one.

5 JUDGE MOSS: Well, he's making it now
6 then, so let's find out if the witness's response
7 was the response to that question. She did
8 discuss how the revenues for the peaking event
9 could be accounted for.

10 MR. VAN CLEVE: She stated she -- I made
11 it a Records Requisition Request at the time, and
12 that was to identify where in the Company's case
13 that the revenues associated with these peaking
14 events were reflected.

15 JUDGE MOSS: And what we need to know now
16 is if the witness just answered that question, or
17 whether that question remains unanswered.

18 MS. DODGE: Could I ask a follow up
19 redirect?

20 JUDGE MOSS: Sure.

21 Q BY MS. DODGE: Ms. Ryan, you have been
22 asked -- I believe this is going back to Mr. Van
23 Cleve's question about you have got costs for
24 peaking that are being asked for. But if you
25 have peaking events, wouldn't there be additional

0957

1 sales that would bring in revenue, and so why
2 does that match? Do you have any information on
3 this question of whether there's an issue about
4 peaking with respect to revenues?

5 A No. My testimony is focused on power
6 costs and risk management benefits. The
7 inclusion of peaking events in our revenue
8 forecasts and load forecasts is more of a revenue
9 item, and that would not be my area to respond.

10 MS. DODGE: I guess we're onto a Records
11 Requisition.

12 JUDGE MOSS: Sounds like it will be a
13 fairly simple and succinct response for the
14 appropriate person.

15 I am just pondering, since it's pretty
16 clear we're going to finish today -- you would
17 probably intend to move this as an exhibit,
18 wouldn't you?

19 MR. VAN CLEVE: Yes, Your Honor.

20 JUDGE MOSS: It's not automatic, so I am
21 trying to -- is it a straightforward enough
22 matter that the Company would have no objection
23 at this point so when it's furnished we make it
24 an exhibit?

25 MS. DODGE: Yes, Your Honor. I believe

0958

1 there may be some other outstanding items like
2 that that we should probably tick through.

3 JUDGE MOSS: I hope you remind me. I
4 don't have my notes with me, but I can go get
5 them.

6 So we will have to make this 108. And I
7 apologize for the out of sequence, but we do our
8 best.

9 (RECORDS REQUISITION.)

10 (EXHIBIT 108 MARKED.)

11 JUDGE MOSS: And we can take care of the
12 housekeeping matters at the end, and after we let
13 the Commissioners take a break.

14 All right. I believe that completes the
15 questioning for you, Ms. Ryan. And I appreciate
16 you giving your testimony. You may step down.

17 We should take our afternoon break. I
18 think we have one more witness, and that will be
19 Mr. Schoenbeck, who we will have after the
20 afternoon recess. So let's be back at 3:35.

21 (Brief recess.)

22 JUDGE MOSS: Let's be back on the
23 record. Raise your right hand.

24

25 DONALD SCHOENBECK,

0959

1 produced as a witness in behalf of ICNU, having been
2 first duly sworn, was examined and testified as
3 follows:

4

5 JUDGE MOSS: Please be seated.

6

7 DIRECT EXAMINATION

8

9 BY MR. VAN CLEVE:

10 Q Could you state your full name for the
11 record?

12 A Donald W. Schoenbeck, S-c-h-o-e-n-b-e-c-k.

13 Q And, Mr. Schoenbeck, on whose behalf are
14 you appearing in this proceeding?

15 A I am appearing on behalf of the Industrial
16 Customers of the Northwest Utilities, and also
17 the Northwest Industrial Gas Users.

18 Q Have you prepared direct testimony in this
19 case that has been designated as Exhibit 371 HC?

20 A Yes, I have.

21 Q And have you prepared supporting exhibits
22 to your testimony that have been about designated
23 as Exhibits 372 through 386?

24 A Yes, I have.

25 Q And did you prepare cross answering

0960

1 testimony that was designated as Exhibit 387?

2 A Yes, I did.

3 Q And do you have any corrections or
4 additions to Exhibits 371 through 387?

5 A No, I do not.

6 Q Are these exhibits true and correct to the
7 best of your knowledge?

8 A Yes, they are.

9 MR. VAN CLEVE: Your Honor, we would offer
10 Exhibits 371 HC through 387, and make
11 Mr. Schoenbeck available for cross-examination.

12 JUDGE MOSS: Thank you. Any objections?
13 Hearing none, those exhibits will be admitted.

14 (EXHIBITS 371 HC to 387 RECEIVED.)

15 JUDGE MOSS: And we previously admitted
16 388 and 389, which were on behalf of the
17 Northwest Industrial Gas Users and related only
18 to the matters stipulated by settlement.

19 PSE indicated 20 minutes for this witness.

20 MS. DODGE: I think I will have less.

21

22

23

24

25

CROSS EXAMINATION

0961

1

2 BY MS. DODGE:

3 Q Mr. Schoenbeck, will you please turn to
4 your testimony, Exhibit 371, at page 10.

5 A (Complies.) Yes, I have that.

6 Q Okay. And this is your discussion of
7 wheeling expense, and the negotiations that were
8 pending at the time of your testimony on the BPA
9 2006-2007 transmission rate case; is that
10 correct?

11 A That's correct.

12 Q And your recommendation here is that the
13 state of the potential settlement should be known
14 when the Commission produces its final order, and
15 should a settlement be reached, that the amount
16 of the settled rate increase should be
17 substituted for the assumed -- or the estimated
18 transmission rate that the Company had initially
19 included in its case; is that correct?

20 A That's correct.

21 Q And are you familiar with the BPA
22 settlement that has been marked Exhibit 107 in
23 this proceeding?

24 A Yes, I am.

25 Q Are you satisfied that that is -- that

0962

1 that now ought to be rolled through into the
2 rates in this case?

3 MR. CEDARBAUM: Your Honor, I object on
4 the basis of this being friendly cross, which is
5 not allowed.

6 JUDGE MOSS: Well, given that the
7 settlement agreement came in late, and the
8 uncertain nature that we went through earlier
9 today, if Mr. Schoenbeck has some knowledge
10 whether that settlement agreement is likely to
11 survive the signature process, I think that would
12 be helpful to have that.

13 And I agree with you to the extent that it
14 supports the Company's position, and it is in the
15 range of friendly cross. And I think it's
16 important enough information for us to have, if
17 Mr. Schoenbeck has information on it.

18 THE WITNESS: Well, I do have information
19 on it with respect -- yes, I am familiar with the
20 Bonneville Transmission Settlement Process. The
21 last technical meetings regarding a rate matter
22 for a rate charge that would not go into effect
23 until October of 2006 was held yesterday
24 afternoon.

25 As far as I know, there is still no party

0963

1 that is objecting to the settlement as it is
2 currently constructed. It does have a process to
3 go through. I thought the process would be done
4 prior to a Commission order in this proceeding,
5 but given the fact that the process could only
6 result in a higher increase than what has been
7 reflected in the exhibit, I think it would be a
8 reasonable substitution, as PSE has done, to
9 allow the 17.7 percent for the five-month period.

10 JUDGE MOSS: Thank you. Does that
11 complete the questions?

12 CHAIRWOMAN SHOWALTER: Could I ask a
13 follow up? I didn't understand why you said
14 given that it would could only result in a higher
15 rate during the settlement.

16 THE WITNESS: Sure. For all the major
17 customer groups, which Bonneville has
18 approximately 130 to 140 individual customers
19 generally represented by six major groups, in
20 addition to the investor-run utilities and
21 individual DSI companies, they are all in
22 agreement with where the settlement is today.

23 It still has to be approved first by the
24 Bonneville Power Administrator, because this is a
25 TBL, or transmission business line settlement.

0964

1 If he would not accept this settlement, it would
2 be because he felt it would not give the
3 financial revenue to the transmission business
4 line that he felt he needed.

5 If he approves the settlement, FERC has
6 the exact same responsibility, and the exact same
7 tasks.

8 So, again, their rejection of the
9 settlement would mean a higher rate, not a lower
10 one.

11 CHAIRWOMAN SHOWALTER: Thank you. I now
12 realize the parties were not all of the
13 interested parties. The parties are the
14 customers, not --

15 THE WITNESS: It's the transmission
16 customers.

17 CHAIRWOMAN SHOWALTER: Thank you.

18 Q BY MS. DODGE: Just a point of
19 clarification, Mr. Schoenbeck. I believe you
20 stated these would go into effect October 1,
21 2006. Did you mean 2005?

22 A No. I was talking about the rate issue
23 that was being discussed yesterday at the
24 settlement meeting that has to do with generation
25 ancillary service rates. That particular rate

0965

1 would go into effect 2006.

2 The IR rate that has the 17.7 percent
3 increase associated, that transmission rate would
4 be October 2005.

5 Q Thank you.

6 MS. DODGE: I don't have any further
7 questions, but would like to move for admission
8 of Exhibit Nos. 390 and 391, which are a couple
9 of Data Request Responses.

10 MR. VAN CLEVE: No objection.

11 JUDGE MOSS: Those will be admitted as
12 marked.

13 (EXHIBITS 390 and 391 RECEIVED.)

14 JUDGE MOSS: Are there any questions for
15 Mr. Schoenbeck from the bench?

16 CHAIRWOMAN SHOWALTER: Yes.

17

18 EXAMINATION

19

20 BY CHAIRWOMAN SHOWALTER:

21 Q Mr. Schoenbeck, I am looking -- trying to
22 find in your testimony where you talk about the
23 importance in a PCA of setting the mid-point
24 correctly. And I wanted to go into that, and I
25 can't seem to find it in your testimony.

0966

1 At a certain point you said, "I can't
2 overemphasize enough" -- a certain point. And I
3 remember the point, but not the page.

4 A I think it was -- I cannot tell you the
5 exact page at the moment, but I think it had to
6 do with the introduction of the gas price
7 discussion.

8 MR. VAN CLEVE: Could I suggest pages 5
9 and 6?

10 THE WITNESS: That is probably the correct
11 page references.

12 Q BY CHAIRWOMAN SHOWALTER: There's a
13 place where you give an example of supposingly
14 knew what the future costs are. I apologize for
15 not being ready --

16 A There's another possibility towards the
17 bottom of page 7, when I give the example of,
18 "Knowing several extraordinary conditions, would
19 it still be inappropriate to set the base costs
20 using those means?"

21 Q Yes. That's right. I think I read it on
22 page 7 here that you were using the illustration
23 in lines 15 to 24 to say that if we try to
24 predict too precisely what will happen next year,
25 in effect, we haven't hit a more abstract

0967

1 standard, or normal range?

2 A Normalized.

3 Q And, therefore, the PCA sharing mechanism,
4 which assumes that, would be operating on, in
5 this example, on a nonnormal year, as opposed to
6 a normal year. And the principles of the sharing
7 would get skewed. Is that more or less your
8 point?

9 A That is exactly the point, yes.

10 Q And I wanted to ask you, then, if we knew
11 with this kind of precision what the cost would
12 be, well, then, wouldn't we just dispense with
13 the PCA and other kinds of projections, and lock
14 in the costs for that year?

15 My point being, because we don't know with
16 this precision, is that what gets us to
17 projecting some kind of standard? And then I
18 want to talk about what that standard should be.

19 A Yes, that's right. Because you do not
20 know the term that the rates will be in effect.

21 And that is really the kernel for my mind
22 with regard to the gas issue, what period should
23 we be focusing on for the gas issue, given that
24 under the PCA mechanism as currently exists,
25 there is this cumulative cap, if you will, that

0968

1 will allow Puget to recover 99 cents on the
2 dollar up until July 1 of 2006.

3 Q And so your recommendation is to adopt a
4 normalized, or what I think of as more of -- a
5 more abstract standard. It's less a prediction
6 of what will happen than a projection of normal
7 cost over a longer period of time. Is that
8 a fairer way to put it?

9 A I believe it is.

10 Q And to get to that, you start looking at
11 what I think you call the fundamentals, or
12 someone calls them the fundamentals. But you get
13 down to more the real costs of -- is that
14 correct?

15 A That's correct. It's usually more of a
16 fundamentalist approach, looking at supply and
17 demand as opposed to near term market pressures.

18 Q So here's my question. It seems to me
19 that to accept that, we then also have to accept
20 that the market is going to get down to those or
21 get -- approach those fundamental costs.

22 In other words, it's expressing a certain
23 degree of faith in the market mechanisms to
24 achieve prices that are close to the
25 fundamentals; is that correct?

0969

1 A Yeah, that's correct. It's the notion
2 that there is a competitive market that would
3 allow there not to be any extraordinary profit
4 margin on the sale of that gas.

5 Q And if that were correct, wouldn't we see,
6 over time, in the future, which isn't here, this
7 efficiency, or would we not?

8 A You would certainly hope that what people
9 are giving is their current example of what could
10 make the price of gas get more competitive than
11 it has been recently. It's just the additional
12 potential of LNG facilities being on the West
13 Coast. Such fundamental type forecasts uses the
14 price of gas for that, the price of gas of LNG Of
15 around \$4.50 MCF.

16 And so looking at that as another measure
17 of a potential long-term cost of gas, in a
18 competitive market, if the facilities can be
19 built, arguably net would be more of a market
20 price for that commodity.

21 Q And it's the "if." It seems to me that
22 you are proposing that we adopt a price the way
23 the market should work, and maybe it should. But
24 I'm not sure it will. And it's the difference
25 between "should" and "will." And so far, at

0970

1 least, in the more near-term immediate past, and
2 near future, it doesn't look as if the market is
3 operating according to -- or at least it's not
4 getting those prices.

5 A Potentially it's overreacting to the
6 short-term price signals now.

7 Q And I suppose you could say that's why
8 LNG and other things may fall into place. But
9 how am I supposed to make the judgment that the
10 market is actually going to behave as it, quote,
11 "ought to" under the fundamental analysis?

12 A It is difficult. It is difficult. But I
13 would contrast it -- again, in doing the PCORC
14 case, I brought up the notion that the Aurora
15 model is also a fundamentals model based on the
16 price of gas that's used as an input. It
17 determines what a market price should be.

18 And it is that type of analysis that
19 people in this case, at least in the form of the
20 Company, are willing to put their faith on, their
21 revenue requirement for their short-term
22 purchases and sales on that type of fundamental
23 model.

24 And that's what you are basically doing,
25 putting your faith in a similar approach using a

0971

1 gas fundamentals model.

2 Q And so then there arises this question of,
3 is a fundamentals model or analysis as reliable
4 in gas as it is in electricity? I don't know the
5 answer, but what is your answer? And by saying
6 as reliable, one answer is neither one is very
7 reliable.

8 A That actually is an answer. And I think
9 in both cases they are generally indicative of
10 trend. They are not price. But it is a
11 yardstick that is used to measure where the
12 prices should be.

13 So just as the Nymex, using the historical
14 Nymex prices, R square of 30 or 35 percent, it's
15 showing that using historical prices is not all
16 of that robust for predicting the future. And
17 the exact same can be done with the fundamentals
18 model.

19 I think there was a bench request in the
20 PCORC proceeding that compared fundamental models
21 and their forecasts, as well as the fundamental
22 errors using the Nymex system price series. As I
23 recall, they are basically comparable. So
24 neither one is going to give you the exact
25 correct answer for what the future price is going

0972

1 to be.

2 Q I know you have made the point that we
3 should be looking at a point in time beyond 2006,
4 or in the middle of 2006 and beyond; is that
5 correct?

6 A That's correct.

7 Q But if we chose to look at the rate year
8 in this case, and if we are, in fact, just trying
9 to predict the price in that rate year, then do
10 you agree or disagree that the most recent three
11 months is the best predictor of that price, or do
12 you think there's a better predictor of that
13 price?

14 A Actually, I looked at the testimony that
15 Dr. Dubin -- the rebuttal testimony of Dr. Dubin,
16 and he basically said using any monthly period,
17 60 days, 20 days, the number of different
18 periods, he said any one would be arbitrary.

19 And I actually agree with that, as well.
20 I believe if you are going to go to that type of
21 Nymex approach and focus on just the rate period,
22 using more than 10 days is better. I don't know
23 if using 60 is the best.

24 If you look at his statistics they are all
25 quite comparable. The only thing I would urge

0973

1 you to do if you would go to that approach, and
2 I'm not sure you have the ability to do it, is
3 you would require PSE to then update that gas
4 price forecast effective July 1 of 2006.

5 If you are just going to focus on the gas
6 prices now, even using the Nymex strip, the Nymex
7 strip drops off over 60 cents, I believe, from
8 the rate case period to the period starting July
9 1, 2006.

10 And that's really the concern I am
11 reflecting in my testimony is if you take into
12 account all of the actual costs now, and
13 hopefully we're in a very high gas price period,
14 and I certainly hope it will come down based on
15 more competitive offerings, the lowering price of
16 oil, then you would be -- the rate payers would
17 be overpaying. Because the base cost from the
18 PCA mechanism would be established on a gas price
19 that is not reflective of the prices beyond the
20 12-month rate period that you focused on.

21 And that's why I'm not sure how you can
22 get PSE to make that filing. And that's one of
23 the things I was struggling with Dr. Mariam's
24 testimony was that was what his recommendation
25 called for. Let's just focus on the rate year,

0974

1 and we won't worry about what happens after July
2 1, 2006.

3 Because I think I'm assuming that during
4 the rate period it doesn't matter if you use
5 \$3.50 or \$4.50 or \$10.50 for gas, because they
6 are going to get 99 cents on the dollar through
7 the PCA mechanism because they will have hit the
8 \$40 million cumulative cap. So I look at it as a
9 cash flow issue during that period. But once you
10 get beyond July 1, 2006, then it becomes real
11 rate payer money.

12 Q So setting aside for the moment how this
13 might be enforced, you are suggesting a periodic
14 update, or just an update before 2006 of the
15 bench mark?

16 A I think that the gas price used in the
17 bench mark would have to be updated effective
18 July 1, 2006.

19 Q And I understand the point of the cap
20 coming off, but just more theoretically, does it
21 make sense to require a periodic update of the
22 bench mark as part of the mechanism maybe every
23 year?

24 A Well, that's certainly what has happened
25 to date, and that's one of our disagreements.

0975

1 Again, ICNU did not support the PCA mechanism
2 when it was established. We are not a signatory
3 party, because we had some problems with it. And
4 certainly from our view, you are greatly
5 defeating the purpose of the PCA mechanism if you
6 go back to what you are discussing. Well, let's
7 use the best information for the next month, go
8 forward, and those will be the rates, because
9 there should be very little swing.

10 If I was one of the commodity risk
11 managers of PSE, and I knew you were setting the
12 price, you had just locked in the forward strip
13 of the Nymex price and the base rates, what I
14 would immediately do is make hedges around that
15 fact and enter into transactions to lock in that
16 price to greatly reduce my risk.

17 So then you are putting all the risk on
18 the rate payers, or the rate payer is effectively
19 bearing all of the cost of that solution as
20 opposed to what I thought was the original PCA
21 mechanism, that there be an equal sharing of risk
22 about some normalized level, whether it be gas,
23 as we have been discussing primarily so far, or
24 water.

25 Q Well, here's a small question on page

0976

1 29. You are talking here about the idea of
2 acquiring some of the Company's money to support
3 advocacy in rate cases. And you cite to
4 California, Oregon and Idaho on line 8.

5 And I wonder, do you know if those states
6 have a statutory Office of Public Counsel, or
7 some kind of equivalent, the way we do here?

8 A California definitely does not. I don't
9 believe Oregon does. And I'm not sure about
10 Idaho.

11 Q I believe I have a question on page 18.
12 And I am going off my memory when I read this, so
13 please correct me if I have not got things right.

14 But if you look at the chart, I believe
15 what you did here is -- well, maybe -- are you
16 recommending this average? Is that your
17 recommendation?

18 A That was definitely my recommendation when
19 I wrote this testimony. It's actually the
20 average of what I say -- it's the values on the
21 table on page 18, coupled with also the values on
22 the table that is reflected on page 17. Both of
23 those things were considered in my
24 recommendation.

25 Q Well, did you just take a broader average

0977

1 or an average that is an average based on more
2 years? Is that all that is going on here?

3 A It is, again, starting with the 2006 value
4 on the -- the table on page 18 has values for
5 2006 through 2011. And then what was reflected
6 in the Aurora run was a shorter term of 2006 to
7 2008. And based on both those forecasts at the
8 time, I selected the price that is on line 9 on
9 page 18.

10 Q I am still having a hard time. It's the
11 same as the average in the chart on the page,
12 correct?

13 A Yes, that's correct.

14 Q So what does that have to do, I guess,
15 with the chart on the previous page, which I
16 think is the Aurora? In other words, how do
17 these two fit together? It seems as if there's
18 just more years involved.

19 A Well, there are more years, plus the
20 different values.

21 Q Okay. I see. This is the difference one
22 is as you mass and the other is the Aurora model?

23 A And all I am saying is if you average the
24 years 2006 through 2008, using both sources, you
25 actually end up with the same exact value that

0978

1 you do if you use the average of 2006 through
2 2011 that is reflected in the table.

3 Q Right. And this was the source of my
4 confusion. In other words, the amount on line 9
5 is coincidentally the same as the amount on line
6 5?

7 A That's correct.

8 Q That's what I needed to know.

9 CHAIRWOMAN SHOWALTER: And I think that's
10 all my questions. Thank you.

11

12 EXAMINATION

13

14 BY COMMISSIONER HEMSTAD:

15 Q Well, I am pursuing the issue on page 18.
16 I had a question there, also. And the sentence
17 at line 5, both of these prices series advanced
18 by the Company reflect years, and the gas price
19 is in the --

20 CHAIRWOMAN SHOWALTER: That is the
21 confidential part.

22 COMMISSIONER HEMSTAD: I am sorry. Strike
23 that -- Judge Moss.

24 JUDGE MOSS: Should we go into
25 confidential session?

0979

1 COMMISSIONER HEMSTAD: (No response.)

2 JUDGE MOSS: The Court Reporter got that.

3 Q BY COMMISSIONER HEMSTAD: And then the
4 reference to the price which advanced as a
5 reasonable level in the recently completed PCORC
6 proceeding, I don't understand that point.
7 That's the futures price you are referencing
8 there?

9 A Yes, right. That was the notion that if
10 you still look at some fundamental type of
11 approach, you can still come up with the number
12 in that range.

13 I went with the higher number in
14 recognition of where the current prices are,
15 coupled with the notion that I alluded to
16 earlier, another substitution, another way of
17 looking at a substitution for a normalized --
18 instead of a normalized fundamentals approach is
19 something looking like a gas substitution, such
20 as the LNG, which is in the range of 4.50.

21 Q And this shows my lack of comprehension
22 of these different approaches, but where did the
23 confidential number come from? How did you
24 arrive at that?

25 A Well, that's really what I did. That's

0980

1 the difference between this case and the PCORC
2 case, was I thought there was some discomfort
3 from bringing in a fundamentals model that people
4 weren't comfortable with, people were unfamiliar
5 with that had a genesis in the state of
6 California.

7 So what I did was I used gas forecasts
8 from the Company, from PSE. So in the case of
9 the table that was reflected on page 17, those
10 prices were what they used in their Aurora run.
11 With regard to the table on page 18, those were
12 the prices that they used and filed at the SEC
13 with regard to creating and determining what they
14 believe their Tenaska write-off obligation to be.

15 So I looked at that as -- particularly the
16 SEC document as being a pretty serious
17 calculation, and it was certainly at the time of
18 the -- it was more current than the Aurora
19 forecast. And yet in both of these documents you
20 see the indication of where the Company expects
21 the gas prices to be going in the future. So
22 kind of compromising my position from what I
23 advocated earlier.

24 So what you had referred to is just where
25 I -- my continued belief and hope is, by

0981

1 recognition of the response to my proposal in the
2 PCORC case, I modified to where I am today on
3 line 9 of page 18.

4 Q Okay. I will let that go.

5 CHAIRWOMAN SHOWALTER: Can I ask a follow
6 up?

7 COMMISSIONER HEMSTAD: Sure.

8

9 FURTHER EXAMINATION

10

11 BY CHAIRWOMAN SHOWALTER:

12 Q Since your figure on line 9 is actually
13 a compromise that just happens to be the same,
14 what I was wondering is the chart on page 18 is
15 dated a certain date. I don't know if that's
16 confidential or not, but if you were -- we were
17 to ask for an updated version of this, first of
18 all, do you know if there is one that is a later
19 form?

20 A Well, certainly the Company has updated
21 its gas price inputs for the Aurora runs.

22 Q I was talking about the chart on page 18.

23 A I'm sorry. I'm not aware if they have
24 updated that document.

25 Q Well, let's assume there is a later

0982

1 version, and so it has a different number as an
2 average. Are you with me so far?

3 A Uh-huh.

4 Q Then if we wanted to use that later
5 version, but also use your sense of compromise
6 here, what would we be doing? What did you do
7 operationally with the chart on page 18 and the
8 chart on 19? Did you average the two of them?

9 A Yes. For three very specific years
10 2006, 2007 and 2008, thinking that would be a
11 bench mark for when the rates could still be in
12 effect from this case. And it was beyond the
13 cumulative \$40 million cap mechanism.

14 Q So if we were to adopt this particular
15 methodology, would it make more sense for us to
16 get the updated versions of the chart on page 17
17 and the chart on page 18?

18 A You could certainly do that. Again, where
19 my comfort level is with regard to my particular
20 recommendation is the relationship to the LNG,
21 which is being used as a cap in a long-term
22 fundamentalist approach in the price of gas
23 today.

24 CHAIRWOMAN SHOWALTER: Could we ask the
25 Company for the updated versions of these two

0983

1 charts, if they exist?

2 JUDGE MOSS: Sure. That will be Bench
3 Request 8. Do you understand the Bench Request,
4 Ms. Dodge?

5 (BENCH REQUEST NO. 8.)

6 MS. DODGE: Yes, Your Honor.

7 JUDGE MOSS: And I will reserve exhibit
8 No. 12 for that response.

9 JUDGE MOSS: Are you finished?

10 COMMISSIONER HEMSTAD: No.

11 Q BY COMMISSIONER HEMSTAD: Now I'm going
12 backwards in your testimony, or closer to the
13 beginning. I am looking at page 9, and your
14 discussions about the selection of water years.

15 And at lines 21 through 23 you recommend
16 that we continue the 40-year methodology that the
17 Commission had earlier determined. And then as
18 it states here, until the Commission determines
19 that a different standard should be used and
20 applied. And you go down and say for all three
21 investor-owned utilities in the state -- you are
22 aware of the views of both Dr. Dubin and
23 Dr. Mariam, and as I understand their testimony
24 and their response on examination here, they both
25 view that the 40-year rolling forward cycle

0984

1 apparently has some theoretical flaws.

2 Have you read their material?

3 A I have read the prefiled testimony. I

4 have not seen their transcripts of

5 cross-examination from the hearing this week.

6 Having read their testimony, what

7 Dr. Dubin -- he went through a very expensive

8 process to determine that, yes, there appears to

9 be no cyclical trend in the number of water

10 years. And that's basically what almost every

11 party, with one or two exceptions, argued back in

12 the 1992 process that was held by the Commission.

13 In fact, I was one of the parties

14 advocating that there was no pattern to the water

15 years, and every single water year should be

16 used. Of course, my difference was that I

17 maintained every single water year should be used

18 starting in 1878, not 1928. So I did not see

19 anything different or any surprises in either of

20 their testimony.

21 I believe what the Commission determined,

22 and I thought was a very fair process, was that

23 it wasn't so much the number of water years was

24 the issue, but it was more the rolling average to

25 try to keep the rates more current with respect

0985

1 to what the power cost had been.

2 That's where, in my mind, it really became
3 an issue that is no different than the weather
4 normalization issue where most utilities use the
5 last 20 years on a rolling average, the last 30
6 years on a rolling average.

7 I don't know anyone who would say there's
8 a sequential or seasonal pattern to the ambient
9 temperature. So you could do the exact same
10 tests that -- the exact same tests Dr. Dubin put
11 in with regard to no cyclical pattern to the
12 hydro water years, I think, could be made exactly
13 with respect to the temperature adjustments and
14 weather normalization.

15 So it's a question of how do you know --
16 do you want the rates to be more reflective of
17 what more recent term costs have been.

18 Now, in this particular case, why its
19 become such an important issue is primarily,
20 again, goes back to the price of gas that's being
21 used. The issue of 40 versus 60 water years for
22 Puget is only around 31 average megawatts. But
23 when you times it by a \$6 per MCF gas price, it
24 becomes thousands of dollars.

25 In fact, if you would go back and use what

0986

1 would now be 120 water years record instead of
2 the three and a half percent you see between 40
3 and 60 years going downward, that will actually
4 be a 15 percent increase in the availability of
5 hydro to Puget for their resources.

6 So it would be a much more substantial
7 upward adjustment in hydro availability using the
8 full 120 years as opposed to limiting it to
9 either 50, 40 or 60.

10 Q Do I take it from that, then, after seeing
11 that testimony, at least that you continue to
12 think that the 40-year rolling average is
13 preferable?

14 A Well, I think I believe that this
15 Commission had no different information than what
16 the Commission had in 1992. And that basis is
17 there's no cyclical pattern to water years. And
18 that Commission chose, after hearing testimony
19 from every investor-owned utility, and every
20 expert that was brought in for the hearing, they
21 chose the 40-year rolling average.

22 And they subsequently said that unless a
23 new study could be shown, they would stick with
24 that method. I always considered that order to
25 refer to a new study that showed there would

0987

1 actually be a cyclical pattern to water years,
2 and I haven't seen that, but because Dr. Dubin
3 replicated work done by others 10 years ago
4 showing there is no pattern.

5 So that's why I am maintaining that this
6 is an issue that should stay where it is based on
7 the Commission's determinations that were made at
8 the time, and the evidence that was provided at
9 that time. And there's been no additional new
10 evidence addressing the issue that I think the
11 Commission was asking for in this proceeding.

12 Q On a different subject, on page 13 at the
13 bottom and going onto 14, addressing Nymex
14 contracts -- and, again, reading that, beginning
15 at line 1, "In other words, 96 percent of the
16 trades during these days are transactions from
17 outside the rate period. In fact, the trading
18 activity for each of the last eight months of the
19 rate period is so minimal that it rounds to a
20 zero value -- zero percent value. In my opinion,
21 this is not a meaningful or liquid market, and
22 therefore, not a meaningful price on which to
23 base this critical cost item."

24 This may be plowing ground already
25 covered, but what are we to make of this? You

0988

1 are saying it's not a liquid market, and
2 therefore, I assume your conclusion is it's not
3 an efficient market?

4 A For predicting what the normalized price
5 of gas should be for this case.

6 Q And does it follow from that that going
7 forward the spot market would also not be
8 efficient?

9 A Well, again, we're kind of talking about
10 two different things when you are talking about
11 in terms of a spot market versus futures market.
12 In my mind, when you are talking about a spot
13 market, you are talking about daily, monthly, and
14 you see a pretty robust volume on page 13.

15 But with respect to a futures market, once
16 you get 17 months out, then you see very little
17 difference. So that means your deviation about
18 that value actually being correct is greatly --
19 or the deviations increase your confidence and
20 the value is greatly reduced.

21 Q So the closer one comes to the actual
22 ultimate spot market, or the day of the event, is
23 it your view that that market does reflect what
24 ought to be the appropriate intersection between
25 supply and demand?

0989

1 A Certainly, if you are talking about in
2 terms of Henry Hub or Sumas. If you are talking
3 about the first month or quarter or three months
4 out, it is very reflective of what the market
5 price is.

6 Q And at the bottom of page 15, would you
7 elaborate for my understanding a bit more the
8 discussion beginning on line 19, the relationship
9 of PSE's portfolio risk approach to the Nymex
10 forward prices?

11 A Yes. Under the PSE software they
12 generally look at a whole series of gains or
13 cases with a range about a medium R in expected
14 value with respect to gas prices. That's what I
15 was referring to.

16 I believe we actually put it in the Data
17 Response in the PCORC case. And it showed the
18 number of gains they use to come up with their
19 total portfolio of risk on both the gas side and
20 the electric side.

21 So what I was pointing to is it's a much
22 more sophisticated analysis than simply taking 10
23 days of forward prices from a publication.

24 Q And would you conclude that that approach
25 is more like your fundamental analysis?

0990

1 A It depends on how long you go out, how far
2 you go out, because I believe PSE definitely
3 looks at fundamental factors with respect to
4 where the market prices are going.

5 And that gets into the tension between
6 using information that is too current to actually
7 reflect what the real value of gas will be,
8 versus where I believe is a correct measure is,
9 again, a normalized gas price. And that does not
10 necessarily equate to me to be the current market
11 price.

12 Q And then looking at pages 22 and 23, the
13 highly confidential material, I take it you
14 simply fundamentally disagree with the Company's
15 assessment of the amount of energy that they
16 would, under any reasonable expectation, need to
17 meet the peaking requirements?

18 A That's correct. It's actually pretty
19 important that you brought this up. The Company
20 did do rebuttal testimony, and in the rebuttal
21 testimony they went back to their approach they
22 had used for peaking resources that they
23 ultimately did in the PCORC case.

24 And if you recall, in the PCORC case, you
25 don't, I am sure -- but when I took the stand I

0991

1 said I was willing to accept rebuttal testimony
2 on the peaking issue, since they had reflected a
3 different approach. And that same thing has
4 happened in this case.

5 So with respect to the rebuttal testimony,
6 peaking capacity costs, I do not have an issue of
7 what the Company has done now, but we obviously
8 do have an issue with what the Company has done
9 with regard to what we can maybe term peaking
10 energy costs, or the CT oil burn.

11 COMMISSIONER HEMSTAD: I think that's all
12 I have. Thank you.

13

14 EXAMINATION

15

16 BY COMMISSIONER OSHIE:

17 Q I just have one area, Mr. Schoenbeck, to
18 ask you questions about, and that has to do with
19 the consulting contract wherein you made a
20 recommendation as to a limitation on recovery.

21 And there was a rebuttal testimony filed,
22 and I think I can use the name of the consulting
23 firm, can I not, or is that confidential?

24 MS. DODGE: The name is not confidential.

25 Q BY COMMISSIONER OSHIE: The contract with

0992

1 Navigant. And you made a recommendation in your
2 testimony to limit the recovery. And there was
3 rebuttal testimony filed, and I want to know if
4 you have changed your position on that -- on your
5 recommended adjustment in light of Puget's
6 rebuttal?

7 A The thing that struck me about the Puget
8 rebuttal testimony was more the notion that they
9 have geared up in-house to continue doing this
10 work.

11 We did not ask discovery on it, but given
12 Mr. Markell's testimony, which I presume he was
13 sworn and gave under oath, that the in-house
14 gear-up ongoing in-house expense is effectively
15 at the same level as the Navigant expense. I
16 have definitely softened my position with respect
17 to those outside service costs.

18 I have not, however, softened my position
19 with respect to the outside service costs that
20 are associated with the general rate case expense
21 or the PCORC expenses. I continue to believe
22 Puget has paid substantial sums of money for
23 work, and that should not be solely born by rate
24 payers.

25 That's why I continue to believe my

0993

1 recommendation on allowing the cap of \$500,000 on
2 the PCORC expenses, and allowing no more than 50
3 percent of the costs for the general rate case to
4 be flowed through to rate payers.

5 COMMISSIONER OSHIE: Thank you. I have no
6 further questions.

7

8 FURTHER EXAMINATION

9

10 BY CHAIRWOMAN SHOWALTER:

11 Q I have one follow up, and it has to do
12 with the hydro data. You said that earlier you
13 had advocated -- and maybe you still would --
14 using the full 128 years?

15 A It's about 120 now. It was about 110 ten
16 years ago.

17 Q It was my impression that both Dr. Dubin
18 and also Dr. Mariam actually would agree with
19 you, but Dr. Dubin, at least, felt -- and I can't
20 remember about Dr. Mariam -- felt constrained
21 from going any farther back than 1928 due to
22 other data, or lack of other data. And that was
23 the reason.

24 Now, since you said if you do go all the
25 way back to 128 years it has differential effect

0994

1 on Puget, it sounds to me as if you have either
2 made some projections or combined some kind of
3 data that they didn't want to do?

4 A Well, maybe it goes to not truly realizing
5 all of the assumptions that were made from the
6 1928 data series onto the current data series,
7 and what the accuracy of those data are. Of
8 course, no one can tell you with any degree of
9 accuracy how many cubic feet of water have gone
10 by a particular part of a river or a stream in a
11 day. And yet that is what the assumption is with
12 respect to the hydro study.

13 What you have to start with is a data set
14 that is reflecting of the natural flow of the
15 river, which no one truly knows what that was.
16 And then when you couple that, just from
17 measuring it, and then you couple it with other
18 adjustments that are made to that data, which
19 include a significant one, which, of course, is
20 irrigation depletion, in the earlier data prior
21 to approximately 1940, the irrigation depletion
22 from the Columbia River basin was approximately
23 200,000 million acre feet. By 1979 that value
24 was something like 12 billion 200 million acre
25 feet.

0995

1 These are all assumptions that are being
2 made to come up with the natural hydro flow.
3 Back in 1980 the Bonneville Power Administration,
4 coupled with maybe the University of Washington,
5 put together a study to come up with the natural
6 streamflow as measured at The Dalles to use in
7 hydro analysis. And one of the conclusions of
8 the study to make clear of all the assumptions
9 was that this study was only about plus or minus
10 10 to 15 percent accurate.

11 But what always intrigued me, and I point
12 it out, it may be one of the reasons the
13 Northwest Power Planning Council went to the 110
14 years, is in the earlier data, prior to 1940,
15 they believed it was accurate to within 8
16 percent. During the range of 1940 to 1979 they
17 thought the data was accurate to 12 percent.
18 Beyond 1979, they thought the data would only be
19 accurate to 15 percent.

20 And the reason was all the assumptions
21 they had to make with regard to irrigation
22 depletions, absorption into the sky, and those
23 types of things, and management of the dams where
24 they felt the river was much more pure prior to
25 1940 when there were not the dams on it.

0996

1 So the measurements at The Dalles were the
2 only major factor, because a much more modest
3 amount of irrigation depletion was actually a
4 physical measurement at the river. And they
5 estimated the error on the measurement at The
6 Dalles would be within 5 percent; that they could
7 only be within 5 percent of the daily readings to
8 truly know how much water passed by that point
9 during the course of a day.

10 So when you look at the error within the
11 data, the part that is being excluded turns out
12 to be what, at least the Bonneville Power
13 Administration and the Core of Engineers decided
14 was some of the more accurate natural streamflow
15 data.

16 Q Well, in any event, the Company and the
17 Staff have agreed that 50 years is a reasonable
18 number. I hope I am right on that.

19 A That's the rebuttal number on that, yes.

20 Q And what is your position on, vis-a-vis,
21 rolling, rolling 40 or rolling something?

22 A My position is retain the rolling 40, or
23 go to the 120.

24 Q And were you -- you may not have heard the
25 testimony we had here about the statistician

0997

1 Professor Slutsky saying that using a rolling
2 average when you are -- when your data have no
3 trends actually introduces an error, a cyclical
4 nature that is really not there. Was that
5 concept introduced, to your knowledge, at the
6 hearing 10 years ago?

7 A I can't recall that. But I would say if
8 it's introducing an error, why is that type of
9 rolling average used for weather and
10 normalization? You have weather normalization
11 records that go back far beyond the streamflow
12 records.

13 Q That is a good question, but we don't have
14 in front of us that argument on those other
15 factors. I think had somebody been here
16 advocating that we use 100 years of weather
17 instead of a rolling average, that would be the
18 issue in front of us.

19 A The issue that was decided in 1992 wasn't
20 so much the accuracy of the data versus some
21 other longer term measure. It has to do with
22 trying to just have the current costs be more
23 reflective of a recent past experience. That was
24 the logic I interpreted from the Commission
25 decision.

0998

1 Q Meaning that 40 years of recent data are
2 better than 50 years?

3 A It's to have the costs that the rate
4 payers pay, that they are currently paying be
5 closer to what had recently been incurred.

6 Q But that has to have a rationale to it?

7 A Right. And that's what I am suggesting,
8 that was the rationale.

9 Q I guess the rationale --

10 A It's no different.

11 Q -- is really a truism?

12 A I guess I was going to think in terms of a
13 PGA mechanism where you can set a price of gas.
14 But as long as there is 100 percent true-up to
15 the next year, that is, the customer is paying
16 the costs that were actually incurred, then it's
17 slightly extending -- you are setting a
18 benchmark, but you are slightly extending it from
19 one year to 40 years in this case, which is a
20 major extension.

21 CHAIRWOMAN SHOWALTER: Well, thank you.

22 JUDGE MOSS: I want to follow up on that a
23 little bit, Mr. Schoenbeck.

24

25 EXAMINATION

0999

1

2 BY JUDGE MOSS:

3 Q Is there -- you talked about the quality
4 and nature of the data at different periods of
5 time in terms of its accuracy and so forth. Was
6 1928 in any way a distinguishing point in time
7 along the lines of the periods you were
8 discussing a few moments ago?

9 A Generally when people talk in terms of
10 1928 they are taking in terms of more the
11 critical water year in the lowness of the
12 streamflow on that data. Other than that, I am
13 not aware of the use of the 1928 water year.

14 Q I was trying to get some more information
15 about the significance of 1928, because if I
16 recall Dr. Dubin's testimony was that he started
17 with 1928, because he didn't believe there was
18 any data prior to that, or at least not any that
19 was useful.

20 A Again, it has to do with where the data
21 point is. And the data point going back to 1878
22 is measured at The Dalles. And what the
23 Northwest Power Planning Council did, and that
24 was part of my recommendation in 1992, that when
25 they were just starting their planning process,

1000

1 relatively new planning organization that came
2 about because of the Act, they chose to use the
3 full 110 years of record in determining what
4 would be the power needs, and the availability of
5 energy from the hydro system of the Northwest in
6 a planning process.

7 JUDGE MOSS: Did the questions from the
8 bench, did they call for any follow up?

9 MS. DODGE: In general I think that a lot
10 of what has just been testified to is hearsay
11 interpretation of legal opinions.

12 JUDGE MOSS: I am just asking if you have
13 any more questions. I'm not looking for an
14 argument.

15 MS. DODGE: It's not on an argument. It's
16 for the record, I think, an objection.

17 JUDGE MOSS: Are you objecting to the
18 bench's questions?

19 MS. DODGE: No. No. To the testimony.

20 JUDGE MOSS: Is there any more redirect?

21 MR. VAN CLEVE: No, Your Honor.

22 MR. CEDARBAUM: Can I ask a couple of
23 clarifying questions?

24 JUDGE MOSS: Go ahead.

25 RECROSS EXAMINATION

1001

1

2 BY MR. CEDARBAUM:

3 Q This has to do with your testimony earlier
4 that ICNU did not join the PCA settlement for the
5 last rate case. Do you recall that?

6 A Yes, I do.

7 Q It's correct, though, that ICNU didn't
8 oppose the settlement either, did it?

9 A That's correct.

10 Q So none of the concerns that you brought
11 up today were addressed to the Commission at that
12 time?

13 A No, they were not. Actually, the entire
14 case ended up being settled.

15 MR. CEDARBAUM: Thank you.

16 JUDGE MOSS: I don't imagine that caused
17 you any redirect?

18 MR. VAN CLEVE: No.

19 JUDGE MOSS: Mr. Schoenbeck, we appreciate
20 you're being here and giving your testimony.
21 That completes the questions, and you may step
22 down.

23 Oh, I do have one bench request that I
24 need to put on the record for Staff, or it's
25 directed to Dr. Mariam's work. We would like to

1002

1 have Dr. Mariam, I guess, for lack of a better
2 question, rerun his analysis looking at the most
3 recent 12-month period of data.

4 MR. CEDARBAUM: On gas prices?

5 JUDGE MOSS: Yes. And we want him to not
6 eliminate months that he might consider
7 nonnormal; in other words, we want him to look at
8 the whole data set, and do his analysis that way.

9 MR. CEDARBAUM: The entire 12-month
10 period?

11 JUDGE MOSS: And the most recent that is
12 available. We don't know exactly what that is.
13 So that will be Bench Request 9. And I am going
14 to make that Exhibit 13 when we get the response.

15 (BENCH REQUEST NO. 9.)

16 MR. CEDARBAUM: Your Honor, on the timing
17 of that, we will do it as soon as we can. I
18 don't know if it can be done tomorrow or not.

19 JUDGE MOSS: If we can get it next week,
20 that will be satisfactory, to be sure.

21 I am going to go ahead on the bench's
22 motion, we will seek the admission of Exhibits 4
23 through 9, and 11 through 13, even though we
24 don't have some of the paper yet. Does anybody
25 have an objection or comment on that? These

1003

1 things are designed to help us understand what we
2 have.

3 Okay. There's apparently no objection.

4 So we will mark that as admitted today.

5 (EXHIBITS 4 to 9, 11 to 13 RECEIVED.)

6 JUDGE MOSS: Now, Public Counsel, I will
7 ask you, you will move the public comments. We
8 have given that Exhibit No. 10 -- do that this
9 evening?

10 MR. FFITCH: Well, Your Honor, in terms of
11 the physical exhibit?

12 JUDGE MOSS: Yes.

13 MR. FFITCH: I conferred with the
14 Commission Staff the Public Affairs Staff that
15 collects those. And they indicated to me that
16 they would be able to provide me with a full set
17 of those tomorrow. And then we would need
18 probably an additional day or two the first of
19 next week to duplicate and file and serve those.
20 There's, I think, around 200.

21 So we would ask that we be given until
22 Monday or Tuesday to complete that process out of
23 our office for Exhibit No. 10.

24 JUDGE MOSS: And I think, given the size
25 of that exhibit, let's have fewer copies of it

1004

1 submitted than we require in general. I think if
2 you will provide me with five, that will be
3 sufficient for everybody's needs.

4 MR. FFITCH: Thank you, Your Honor. You
5 anticipated a question that has become somewhat
6 routine to the bench with that particular
7 exhibit, which is how many copies of this exhibit
8 do you want? So we will give you five.

9 JUDGE MOSS: And we have reserved 10 for
10 that. And it's usually not controversial, so
11 I will assume there's no objection.

12 Now, the other matter that I need to
13 bring up, and you may have things that you want
14 to bring up with me, we need to look at the
15 calendar, establish a briefing schedule, and
16 also I want to distribute -- I've been working
17 on an outline for the briefs based on what I
18 perceive the issues in the case to be.

19 We feel, given the number and complexity
20 of the issues in the case, we need some
21 consistency in what we get back, and this is a
22 working document, a talking paper if you will.
23 And I want to hear back from the parties, and we
24 may decide to do this next week by telephone
25 conference, or something, about the outline.

1005

1 Because it may need some adjustment to meet your
2 needs, and all of our needs. But I will
3 distribute that now.

4 And I know, for example, that there are a
5 couple of things that had gone away, one at least
6 in the course of today. So we can eliminate
7 things, and add things, and I will talk to you
8 momentarily about that.

9 But I do want to resolve the schedule
10 while the Commissioners are still here, and then
11 we can let them go, I think, unless there's
12 something that the parties wish to bring up while
13 they are still here.

14 We had originally projected this hearing
15 to go through January 7. So we have picked up
16 three calendar weeks of time, saved three
17 calendar weeks of time, and almost three business
18 weeks. But I certainly am cognizant of the fact
19 that holidays fall in there, holidays of
20 significance to a lot of people, and that people
21 sometimes take off.

22 So what I want to propose is sort of
23 splitting the difference with you, splitting the
24 time with you in terms of adjusting our briefing
25 schedule. And what I would suggest is that we

1006

1 have our initial briefs on January 18, and our
2 reply briefs on the 27th.

3 And part of the reason for that is looking
4 at the Commission's schedule of other business,
5 that will make for efficacious deliberation and
6 writing process. So will those dates work for
7 everyone?

8 MR. CEDARBAUM: Your Honor, actually you
9 are very close to what parties had discussed
10 anyway. We had also been thinking about -- and I
11 think I can speak for the other parties --
12 January 18 as the day for opening. We had talked
13 about the 28th for replies, but from my own
14 perspective, if the Commission wants the 27th,
15 that's fine, as long as it could be the end of
16 the day.

17 CHAIRWOMAN SHOWALTER: It doesn't work to
18 have the end of the day, because we can't get it
19 processed. So we always say noon, but 2:00 p.m.
20 is all right.

21 JUDGE MOSS: How about mid afternoon?

22 CHAIRWOMAN SHOWALTER: Really, our
23 assistants need to know when it is coming in.

24 MR. CEDARBAUM: I am just asking.

25 JUDGE MOSS: Let's make it 3:00, and that

1007

1 will give our people the time to do the
2 processing and distribution internally. So we
3 will say 3:00 on both.

4 What happens is if we wait until the end
5 of the day, everything comes in at once and it
6 completely overburdens our system. So that's the
7 briefing dates.

8 Do the parties, any of the parties have a
9 matter of business that they wish to raise while
10 the Commissioners are still here? So the
11 Commissioners, if they wish, can retire from the
12 bench. And I want to keep you here for just a
13 another minute or so to talk about how we resolve
14 the brief outline.

15 CHAIRWOMAN SHOWALTER: Thank you,
16 everyone. It was an excellent hearing, and thank
17 you for somehow transforming a three-week hearing
18 into four days. We're all efficient.

19 (Commissioners left the bench.)

20 JUDGE MOSS: In terms of this outline, I
21 know it's sort of -- I actually came in early
22 this morning and did this, so it's no doubt got
23 some -- needs some work. What would the parties
24 want to do -- let's go off the record for this
25 discussion.

1008

1 JUDGE MOSS: On the record.

2 We have had some discussion off the record
3 concerning a brief outline, and we'll have a
4 conference call on Monday to discuss that some
5 more.

6 We have a couple of other housekeeping
7 exhibit matters that need to be discussed.

8 Ms. Dodge, go ahead.

9 MS. DODGE: On our list of the
10 outstanding items we have yet to submit a
11 substitute page for Exhibit 206 CT. That was
12 the Cicchetti page with parenthesis in the
13 correct place.

14 Exhibit 247 C will be a supplementation to
15 that exhibit, which is an updated information on
16 rate case costs.

17 JUDGE MOSS: And I had marked in my
18 notes also 249, but I think that was a mistake.

19 MS. DODGE: I don't think it's a mistake.
20 249, I think, ICNU had in mind a single page that
21 was easy to find with the costs summarized, and I
22 understand we will be providing a replacement for
23 their sheet that is an accurate summary of those
24 rate case costs. Essentially what is in 247, but
25 on a single page.

1009

1 JUDGE MOSS: This was probably a Data
2 Response that you had provided to ICNU.

3 MR. VAN CLEVE: I think she's accurately
4 characterizing it.

5 JUDGE MOSS: As long as we're in
6 agreement, then, we will expect to see that.

7 MS. DODGE: And that will be a
8 replacement page.

9 JUDGE MOSS: And you will send me a
10 cover letter reiterating these points, although
11 I am making notes. Anything else?

12 MS. DODGE: I don't know if we have on the
13 record that we provided the response to Bench
14 Request 7 today.

15 JUDGE MOSS: I didn't say anything on the
16 record, but I've made the bench responses
17 exhibits, so I think everybody has a copy of
18 that.

19 Anything else? Any other exhibit matters,
20 or housekeeping matters?

21 MR. CEDARBAUM: Just one reminder, sorry.
22 On housekeeping, we do have errata pages coming
23 from Dr. Mariam and Mr. Russell tomorrow, so we
24 will distribute those as soon as possible
25 tomorrow.

1010

1 JUDGE MOSS: We discussed that previously.
2 Mr. ffitch, did you having something along
3 these lines?

4 MR. FFITCH: Yes, Your Honor. We had a
5 Records Requisition, and I discussed this with
6 counsel for the Company, and I will state it for
7 the record. We're asking that the Company
8 provide copies of Puget Sound Energy's electric
9 and natural gas rate summaries, aka rate
10 brochures, for all rate changes beginning with
11 the 2001 rate case, both the interim and general
12 phase, up to the present. And this request
13 covers both residential and commercial and
14 industrial customers.

15 The summaries of this type are posted on
16 the Puget Sound Energy website from time to time
17 to show current rates as they change, and it's my
18 understanding these may also be bill insert
19 brochures. We have provided copies of the
20 current versions from the website to Ms. Dodge as
21 an example of what we're requesting.

22 And we would expect to submit these as an
23 exhibit once we get them from the Company.

24 JUDGE MOSS: And where would we put that
25 in our exhibit list?

1011

1 MR. FFITCH: With Mr. Reynolds. I believe
2 this is tracking back to an original question
3 that we asked him alternatively with Mr. Story,
4 who responded ultimately. I would be happy with
5 either one of those.

6 JUDGE MOSS: These will be documents from
7 the Company, so can we make that Exhibit 58.
8 Will that be satisfactory, Ms. Dodge?

9 MS. DODGE: Yes.

10 JUDGE MOSS: We will reserve number 58 for
11 that. So you furnish that when it's available,
12 Mr. ffitich.

13 MR. FFITCH: Yes, Your Honor. We actually
14 didn't talk about a specific time line for this.
15 I'm not sure, I assume -- I am not sure --

16 JUDGE MOSS: Can we have that by next
17 Wednesday?

18 MS. DODGE: I believe so.

19 MR. FFITCH: Thank you, Your Honor.

20 JUDGE MOSS: I think I have another matter
21 maybe.

22 I have a little bit of follow up on our
23 bench request responses. We need a little more
24 additional information to help us understand some
25 of the materials in the record.

1012

1 With respect to bench request No. 4, and
2 this refers to one of Ms. Luscier's exhibits, we
3 asked, please provide a description of how the
4 line 7 adjustment for municipal additions is
5 calculated.

6 And one thing we didn't get and need is a
7 direct calculation of the amount on line 7. I am
8 not looking at the response, but that should be
9 sufficiently descriptive, I think, a direct
10 calculation of the amount on line 7. And the
11 balance of it was responsive enough.

12 I want to just put the question to the
13 Company whether it would be -- I'll use the word
14 convenient for lack of another -- to furnish us
15 with responses to Data Request 1 and 2 in the
16 format that Staff responded? I think the Company
17 provided full workpapers in response to those
18 data requests, which is a lot of information, and
19 Staff perhaps provided in a more summary way.

20 So if you could take a look at that and
21 let me know, we would appreciate that. And,
22 again, we're not asking for anything new. We're
23 just asking for a different format.

24 Okay. That's all I have.

25 MR. FFITCH: I have one other matter, Your

1013

1 Honor, which is that we still had not -- we had
2 originally offered 227, and the ruling on that
3 was reserved. This is the excerpt from
4 Dr. Cicchetti's testimony in Kansas.

5 JUDGE MOSS: I have the full set and
6 since we reserved the ruling, I now have the
7 full set, and we will admit the full set.
8 I will say, too, if by inadvertence we missed
9 something that was intended to be admitted in
10 the normal course of the hearing, I think we
11 have covered every exhibit, but -- okay. I've
12 now marked 227 as admitted.

13 (EXHIBIT 227 RECEIVED.)

14 JUDGE MOSS: That's the last one.

15 MR. FFITCH: Your Honor, I am probably
16 behind the game, but there was a stack with 264
17 and 265 at my place. I don't know if those
18 needed to be dealt with or not.

19 JUDGE MOSS: I think we marked those as
20 admitted, but I will check. Yes, I have those as
21 admitted. All right.

22 Well, we're close. I would like to add
23 my statement of my appreciation for the conduct
24 of the parties in this proceeding, and counsel
25 and the experts. Everyone did an excellent job,

1014

1 and I have never seen a hearing of this
2 complexity completed with such efficiency, and I
3 think you all exercised appropriate restraint in
4 the cross-examination exhibit volume, and so
5 forth.

6 So I think you did an excellent job, and I
7 wanted to underscore that fact. So thank you
8 very much, and our evidentiary record --
9 Mr. ffitch.

10 MR. FFITCH: I am sorry. I don't know if
11 this needs to be on the record. I just wondered
12 if there was any need to talk about the public
13 hearing at 6:00, and anything you wanted to
14 discuss while we're here.

15 JUDGE MOSS: We can close the record, and
16 be off the record.

17 ENDING TIME: 5:05 P.M.

18

19

20

21

22

23