BEFORE THE

WASHINGTON STATE UTILTIES AND TRANSPORTATION COMMISSION

WASHINGTON UTILITIES AND TRANSPORTATION COMMISSION, Complainant, v. PUGET SOUND ENERGY, INC., Respondent.	**DOCKET NOS. UE-011570** **UG-011571**

DIRECT TESTIMONY

OF

JIM LAZAR

ON BEHALF OF

THE PUBLIC COUNSEL SECTION OF

THE WASHINGTON STATE ATTORNEY GENERAL'S OFFICE

LINE EXTENSION

Q. PLEASE STATE YOUR NAME, ADDRESS, AND A BRIEF SUMMARY OF YOUR EXPERIENCE.

A. My name is Jim Lazar, I am a consulting economist based at 1063 Capitol Way S. in Olympia, Washington, and have been engaged in electric and natural gas utility rate consulting since 1979. I have appeared before the Commission on more than fifty occasions, testifying in proceedings involving each of the regulated gas and electric utilities.

Q. WHAT WAS THE NATURE OF YOUR INVOLVEMENT IN THE LINE EXTENSION PORTION OF THIS PROCEEDING?

A. I was retained by Public Counsel to review many issues in this proceeding, including the Company's proposed changes to its line extension policy. I participated in the collaborative discussions which resulted in the Stipulation on line extension.

Q. WHAT IS YOUR PRINCIPAL CONCLUSION WITH RESPECT TO THE FAIRNESS OF THE LINE EXTENSION STIPULATION?

A. The Stipulation is a compromise between sharply divergent perspectives. In my opinion, it reasonably balances those interests in producing a gradual transition to a new approach which, we believe, will save electric consumers a great deal of money over time.

Q. WHAT WERE THE PRINCIPAL ELEMENTS THAT PUBLIC COUNSEL WAS CONCERNED ABOUT WITH RESPECT TO THE LINE EXTENSION POLICY?

A. There were two general areas. First, we were concerned about the adverse energy efficiency implications of the original proposed line extension policy. These have been completely addressed by the Stipulation. Second, we were concerned that new customers not add more to costs than to revenues, through over-generous allowances

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for the extension of distribution facilities. The Stipulation fully deals with these concerns as well, but on an 18-month phased-in basis.

Q. WHAT WERE YOUR EFFICIENCY CONCERNS, AND HOW ARE THEY ADDRESSED BY THE STIPULATION?

A. The original changes proposed by PSE linked the amount of line extension allowance that developers received to the expected usage of electricity by the new customers. We concluded that it created an incentive for developers to choose electric heat over gas heat, to build in peripheral "urban sprawl" areas where gas service is not available, and to build to the minimum efficiency levels required by state energy codes rather than to the greater efficiency levels justified by future energy costs. This efficiency impact was not the Company's intent, and within the Collaborative we quickly developed an approach to ensure that builders would not be biased against efficiency or economic fuel choice in the residential sector. The Stipulation provides that the developer's COST of securing a line extension will go DOWN if they install efficiency measures beyond code, or choose gas heat, but the amount of Company-paid investment in the facilities extension will NOT go down. In my opinion, this makes for a very progressive line extension policy that will help to enhance the energy efficiency of new homes, which are being added to Puget's service territory at a rate of about 20,000 per year.

Q. WHAT WERE YOUR CONCERNS ABOUT THE AMOUNT OF CONTRIBUTION THE COMPANY MAKES TOWARD NEW LINE EXTENSIONS, AND HOW ARE THEY ADDRESSED BY THE STIPULATION?

A. There are two factors here, the <u>cost</u> of line extensions, and the <u>allowance</u> for line extensions. The first is the amount that the Company computes as the cost of extending facilities. The second is the portion that the Company pays for, with the remainder borne by the developer. Whatever portion is not paid by the developer becomes a

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component of the distribution rate base, and is paid for by all electric consumers. We were concerned that new development not create severe upward pressure on rates for existing customers.

The Company had last updated its schedule of charges for construction of distribution facilities in the 1980's, and the rates in the tariff were far below current costs. These have been fully updated to reflect current costs. The Company also updated the formula by which it computes the credit that is allowed against those costs. The Stipulation sets those credits based on the expected distribution margin that will be paid by the new customers over a 30-year period. This ensures that developers receive a fair line extension allowance, but that existing customers do not face severe upward pressure on rates to subsidize new developments.

Q. WHAT IMPACT DID THE COMPANY ESTIMATE THAT THE NEW LINE EXTENSION POLICY WOULD HAVE?

A. During the Collaborative discussions, it was estimated that this proposal would reduce the growth in rate base by about $12 million per year. This translates to about a $2 million per year reduction in future rate increase requirements.

Q. WHAT IS THE IMPACT ON NEW HOMEOWNERS OF THE CHANGE IN LINE EXTENSION POLICY?

A. More developers will be required to pay line extension fees to the Company in order to secure electric service. These cost-based charges will be reflected in the selling price of new homes. First, this will create a disincentive to develop in peripheral areas, compared with urban infill. This will likely have spin-off beneficial impacts on factors other than utility cost, including transportation, parks, emergency services, and other costs of providing needed services to new developments, although these factors had no bearing on the calculation of the elements of the electric line extension policy.

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The cost of the line extensions will be paid by new homeowners through their mortgage payments. Since mortgage interest rates are lower than the Company's cost of capital, and because mortgage interest is a federal income tax deduction, while electric bills are not deductible for residential customers, this will significantly reduce the cost to ratepayers (as a whole) for supporting the incremental distribution system investment.

Q. TURNING TO THE COMMERCIAL SECTOR, WHAT WERE THE MOST IMPORTANT CHANGES IN THE LINE EXTENSION POLICY FROM THE PERSPECTIVE OF PUBLIC COUNSEL?

A. The principal element we were concerned about was energy efficiency. As originally proposed, the Company's line extension policy would have provided a smaller line extension allowance to builders of commercial facilities who went beyond the requirements of the Washington State Energy Code than it would to those who built facilities that barely meet the code. We did not think that the utility line extension policy should discourage efficiency. The policy was revised to provide that beyond-code improvements in efficiency will not reduce the line extension allowance. This was a compromise, driven by our interests as well as those of other parties which participated in the Collaborative, and who represent developers of large commercial facilities.

As with the residential line extension policy, the Company proposed updating and lowering the formula for computing the allowance for line extensions. Commercial customer representatives were concerned that this would unfairly penalize development projects already "in the pipeline" which were conceived, designed, and even financed based upon the existing line extension policy. The Stipulation addresses this with a three-step phase-in of the new (lower) allowances, so that projects already underway will be able to vest their line extension charges at lower levels, but in the long run,

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prospective developments will be facing more accurate costs of providing electric service.

Q. TAKEN AS A WHOLE, WHAT IS YOUR RECOMMENDATION WITH RESPECT TO THE PROPOSED LINE EXTENSION POLICY CHANGES?

A. These changes are consistent with the public interest. The Stipulation should be approved.

Q. DOES THIS CONCLUDE YOUR TESTIMONY?

A. Yes.

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