

**Exhibit No. MDF-1T
Dockets UE-090704/UG-090705
Witness: Michael D. Foisy**

**BEFORE THE WASHINGTON STATE
UTILITIES AND TRANSPORTATION COMMISSION**

**WASHINGTON UTILITIES AND
TRANSPORTATION COMMISSION,**

Complainant,

v.

PUGET SOUND ENERGY, INC.,

Respondent.

DOCKET UE-090704

DOCKET UG-090705

TESTIMONY

OF

MICHAEL D. FOISY

STAFF

OF

**WASHINGTON UTILITIES AND
TRANSPORTATION COMMISSION**

***Revenue Requirement Adjustments: Miscellaneous Operating Expenses and Property
Taxes***

November 17, 2009

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EXHIBIT LIST

Exhibit No. MDF-2 Staff Miscellaneous Operating Expenses Adjustment, Electric

Exhibit No. MDF-3 Staff Miscellaneous Operating Expenses Adjustment, Gas

I. INTRODUCTION

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Q. Please state your name and business address.

A. My name is Michael D. Foisy. My business address is The Richard Hemstad Building, 1300 S. Evergreen Park Drive S.W., P.O. Box 47250, Olympia, Washington 98504. My email address is mfoisy@utc.wa.gov.

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

A. I am employed by the Washington Utilities and Transportation Commission (“Commission”) as a Regulatory Analyst.

Q. Would you please describe your educational and professional background?

A. I graduated from Regis University in Denver, Colorado with a Bachelor of Science degree in Technical Management in 1982. In 1985, I earned a Masters of Arts degree in Personnel Management from Central Michigan University.

I began my employment at the Commission in February 2009. During my employment at the Commission, I have performed accounting and financial analyses of regulated utility and transportation companies.

I attended the New Mexico State University, Center for Public Utilities, “Practical Regulatory Training for the Changing Electric, Natural Gas Industries” course in September 2009.

1 **II. SCOPE AND SUMMARY OF TESTIMONY**

2

3 **Q. What is the purpose of your testimony in this proceeding?**

4 A. My testimony presents the results of Staff's review of fifteen ratemaking adjustments
5 proposed by Puget Sound Energy, Inc. ("PSE" or "the Company") related to the
6 Company's electric and natural gas revenue requirements determination.

7

8 **Q. Which Company adjustments have you reviewed that are uncontested by Staff?**

9 A. Staff does not contest the following eleven electric and natural gas adjustments
10 proposed by PSE:

- 11 • Adjustments 10.05 and 9.05, Tax Benefit of Pro Forma Interest
- 12 • Adjustments 10.12 and 9.09, Pass Through Revenues and Expenses
- 13 • Adjustments 10.21 and 9.14, Rate Case Expense
- 14 • Adjustment 10.18, Montana Electric Energy Tax
- 15 • Adjustments 10.22 and 9.15, Deferred Gains/Losses on Property Sales
- 16 • Adjustments 10.35 and 9.23, Fleet Vehicles

17

18 **Q. Staff does not contest Adjustments 10.05 and 9.05, Tax Benefit of Pro Forma**
19 **Interest. Nevertheless, the Staff numbers do not agree with the Company's**
20 **corresponding adjustments. Please explain the reason for the difference.**

21 A. Although Staff agrees with the Company's methodology, Staff's adjustments differ
22 from the Company's as a result of other contested adjustments that affect gas and

1 electric rate base. Moreover, Staff's weighted cost of debt used in calculating the tax
2 benefit of pro forma interest is different from the Company's.

3
4 **Q. Please explain the tax benefit of pro forma interest.**

5 A. The pro forma interest adjustment adjusts the book interest expense to the amount
6 reflected by the weighted cost of debt and rate base. The pro forma interest expense
7 is a component in the computation of the regulatory income tax. As the rate base and
8 cost of debt changes, the tax benefit of pro form interest also changes.

9
10 **Q. Which Company adjustments have you reviewed that are contested by Staff?**

11 A. Staff contests the following four Company adjustments:

- 12 • Adjustments 10.14 and 9.09, Miscellaneous Operating Expenses
- 13 • Adjustments 10.15 and 9.10, Property Taxes

14
15 **Q. Please summarize your testimony regarding these contested adjustments.**

16 A. For the contested adjustments identified above, Staff proposes the following:

- 17 1. Company Adjustments 10.14 and 9.09, involving Miscellaneous Operating
18 Expenses, include increases in service contract baseline charges using
19 estimated contract amounts. These contracts are not signed and finalized and,
20 therefore, are not known and measurable. Staff proposes that the unadjusted
21 test year amounts be used, instead.

1 deferral of unrecovered residential exchange benefits". Also, included within these
2 adjustments are costs of the Wire Zone Vegetation Management Program and
3 contractual rent for the Summit Building. Other components move the following
4 expenses below the line: the Company store which sells items with PSE logos to
5 employees; airport and hotel parking; and athletic events expenses. None of these
6 items included in the Miscellaneous Operating Expense are contested by Staff.

7
8 **Q. Please describe the components of the Miscellaneous Operating Expense**
9 **adjustments that Staff does contest.**

10 A. Two components that are contested by Staff are the increases in service contract
11 baseline charges for both transmission and distribution.² PSE's electric adjustment
12 increases transmission expense by \$23,515 and distribution expense by \$874,539.
13 The corresponding gas expenses increases are \$3,005 for transmission and \$695,231
14 for distribution.

15 Company Adjustment 10.14 in total decreases electric expense by \$682,311.
16 Company Adjustment 9.09 in total decreases gas expense by \$213,943. PSE's
17 adjustments increase net operating income by \$994,791 on the electric side and
18 \$440,899 on the gas side.

19
20 **Q. Please explain who the contractor is and the purpose of these service contracts.**

21 A. Quanta/Potelco is the contractor. It provides construction-related services to PSE for
22 both the electric and gas transmission and distribution systems. Quanta/Potelco's

² Exhibit No. JHS-10 at 20:14-15 and Exhibit No. MJS-9 at 9.09:10-11.

1 services include facilities design, project management, construction and related
2 billing for new customer construction, system construction, operation and
3 maintenance related construction, storm response related construction, and street
4 lighting construction.³

5
6 **Q. Why does Staff contest the Company's proposal to include increases in service
7 contract baseline charges in the Miscellaneous Operating Expense adjustments?**

8 A. The Company projects increases in the contract amounts based on estimates from
9 historic data. However, no new contracts have been signed and none will be in place
10 prior to the start of the rate year.⁴ PSE's adjustments to service contract baseline
11 charges, therefore, are inappropriate because they fail to meet the Commission's
12 "known and measurable" criteria for a pro forma adjustment.

13
14 **Q. Please explain why the Company's adjustments for service contract expenses do
15 not meet known and measurable criteria for a pro forma adjustment.**

16 A. While estimates and projections are budgetary necessities in the operations of any
17 company, they do not meet regulatory requirements for ratemaking. WAC 480-07-
18 510 specifies that pro forma adjustments "... give effect for the test period to *all*
19 *known and measurable changes* that are not offset by other factors." (Emphasis
20 added). Accordingly, pro forma adjustments are not merely estimates added to test
21 year results. Instead, they are rooted in historical data. Historical test-year data that

³ PSE Response to Staff Data Request No. 51.

⁴ PSE Response to Staff Data Request No. 50.

1 have been affected by a measurable change may be adjusted to recognize the impact
2 on future revenues or the impact on future costs.

3 In other words, pro forma adjustments are not merely forecasted estimates of
4 future expenses based on someone's "judgment." Accordingly, because the
5 Company's service contract baseline charges adjustments are based solely on
6 management's judgment, they are not "known and measurable" and should be
7 rejected by the Commission. Unadjusted test year amounts should be used instead,
8 as Staff proposes. Had the Company and its contractors finalized a service contract
9 with firm dollar amounts, a pro forma adjustment might be appropriate.

10 Staff witness Parvinen discusses in more detail these issues surrounding the
11 proper application of a pro forma adjustment.

12
13 **Q. What effect does Staff's removal of the increases to service contract baseline**
14 **charges have on net operating income?**

15 A. For PSE's electric operations, Staff's treatment increases net operating income by
16 \$1,578,527 after income taxes and decreases the overall revenue requirement by
17 \$2,540,839. My Exhibit No. MDF-2 shows the calculation of these amounts.

18 For PSE's gas operations, Staff's proposal increases net operating income by
19 \$1,194,096 after income taxes and decreases the overall revenue requirement by
20 \$1,920,104. My Exhibit No. MDF-3 shows the calculation of these amounts.

21 The calculations of my adjustments are also reflected in Exhibit No. KHB-2,
22 page 2.21 for the electric operations and Exhibit No. KHB-3, page 3.14 for the gas
23 operations.

1 **B. Adjustments 10.15 and 9.10, Property Taxes**

2

3 **Q. Please summarize the Company's adjustment to its property tax expense.**

4 A. The Company's Adjustments 10.15 and 9.10, Property Taxes, decrease net operating
5 income by \$1,603,695 and \$850,450, respectively.

6

7 **Q. Does Staff contest the Company's Property Tax adjustments?**

8 A. Yes. The Company's adjustments utilize estimated property tax levy rates to be paid
9 in 2009. Staff contests these adjustments because they fail to meet the
10 Commission's "known and measurable" criteria for a pro forma adjustment.

11

12 **Q. Did you apply the same reasoning as in the prior adjustments for Miscellaneous
13 Operating Expenses?**

14 A. Yes, as stated previously, WAC 480-07-510 specifies that pro forma adjustments "...
15 give effect for the test period to all known and measurable changes that are not offset
16 by other factors." Since the Company's property tax adjustments are estimates based
17 on management's judgment, they are not "known and measurable" and should be
18 rejected by the Commission.

19

20 **Q. Do the Staff gas and electric results of operations presentations remove the
21 Company's property tax adjustments?**

1 A. Yes. The Company's adjustments have been removed to reflect the most current
2 actual property tax liability. This treatment returns the property tax liability to test
3 year values.

4

5 **Q. What affect does removal of these adjustments have on net operating income?**

6 A. Staff disallows the Company's Adjustments 10.15 and 9.10, therefore net operating
7 income is unaffected. This treatment is reflected on Exhibit No. KHB-2, page 2.22
8 for PSE's electric operation and Exhibit No. KHB-3, page 3.15 for PSE's gas
9 operations.

10

11 **Q. Does this conclude your testimony?**

12 A. Yes, it does.