

Exhibit No. ____T (KLE-1T)
Dockets UE-111048/UG-111049
Witness: Kenneth L. Elgin

BEFORE THE WASHINGTON STATE UTILITIES AND TRANSPORTATION COMMISSION

**WASHINGTON UTILITIES AND
TRANSPORTATION COMMISSION,**

Complainant,

v.

PUGET SOUND ENERGY, INC.,

Respondent.

**DOCKET UE-111048
DOCKET UG-111049
(Consolidated)**

TESTIMONY OF

Kenneth L. Elgin

**STAFF OF WASHINGTON UTILITIES AND
TRANSPORTATION COMMISSION**

*Fair Rate of Return
Attrition*

December 7, 2011

1 PSE's combined electric and natural gas operations have been below its authorized
2 returns on equity.

3

4 **II. SUMMARY OF TESTIMONY**

5

6 **Q. What do you recommend for the overall cost of capital for the regulated
7 operations of PSE?**

8 A. The overall cost of capital that I recommend for PSE's regulated operations is 7.59
9 percent. The following table shows the capital structure and cost rates that produce
10 this overall rate of return:

<u>Component</u>	<u>Percent</u>	<u>Cost</u>	<u>Weighted Cost</u>
Long-term debt	50.00	6.22%	3.11%
Short-term debt	4.00	2.68%	0.11%
Common equity	<u>46.00</u>	9.50%	<u>4.37%</u>
Cost of Capital	100.00		7.59%

16

17 **Q. The Company proposes an overall cost of capital of 8.42 percent. Please
18 summarize the differences between the Staff and Company proposals.**

19 A. There are four differences between my 7.59 percent cost of capital and the
20 Company's proposed 8.42 percent cost of capital: 1) I estimate a fair return on
21 equity ("ROE") of 9.50 percent compared to the Company's proposed 10.80 percent;
22 2) I recommend a capital structure with a 46 percent common equity ratio compared
23 to the 48 percent proposed by the Company; 3) I recommend a *pro forma* cost of

1 long-term debt of 6.22 percent compared to the Company's proposed 6.37 percent;
2 and 4) my cost of short-term debt is 2.68 percent compared to the company's 4.62
3 percent.

4

5 **Q. Please summarize your testimony regarding the issue of attrition.**

6 A. The Company's comparison of actual (per books) earned returns on equity to
7 authorized returns on equity does not meet the necessary burden to prove and
8 measure attrition, as established by Commission precedent. Nor has PSE specified
9 any specific attrition adjustment, as required by Commission rule.¹ Thus, the
10 Commission should reject the Company's claim of attrition.

11 Nonetheless, the Company's ongoing expenditures for infrastructure
12 additions and replacements warrant an appropriate regulatory response to address
13 regulatory lag. I present an option for PSE to address this issue through an expedited
14 rate making process that will enable the Company to receive timely rate relief. The
15 approach I present is consistent with the Commission's current practice and policy to
16 set rates on an historical test period with proper normalizing adjustments.²

17

18 **III. FAIR RATE OF RETURN**

19 **A. Background**

20

21 **Q. What primary steps are involved in estimating a fair rate of return for any**
22 **regulated utility?**

¹ WAC 580-07-510(4)(i).

² WAC 580-07-510(3)(e).