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BEFORE THE WASHINGTON

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UTILITIES AND TRANSPORTATION COMMISSION

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WASHINGTON UTILITIES AND)
TRANSPORTATION COMMISSION,) Docket PG-060215
Petitioner,) Volume II
) Pages 14-54

5

vs.

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PUGET SOUND ENERGY, INC.,)
Respondent.)

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A hearing regarding the proposed settlement agreement in the above-entitled matter was held at 9:34 a.m. on Tuesday, March 25, 2008, at 1300 South Evergreen Park Drive, S.W., Olympia, Washington, before Administrative Law Judge ADAM TOREM, Chairman MARK SIDRAN, Commissioner PATRICK OSHIE and Commissioner PHILIP JONES.

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The parties present were as follows:

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COMMISSION STAFF, by Donald T. Trotter, Assistant Attorney General, 1400 South Evergreen Park Drive, S.W., P.O. Box 40128, Olympia, Washington, 98504-0128.

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PUGET SOUND ENERGY, INC., by Sheree Strom Carson, Perkins Coie, 10885 N.E. Fourth Street, Suite 700, Bellevue, Washington 98004.

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24 Barbara L. Nelson, CCR

25 Court Reporter

0015

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2

INDEX OF EXAMINATION

3

4

WITNESS PANEL:

PAGE:

5

STEVEN KING, PATRICIA JOHNSON, DUANE HENDERSON,

6

SUSAN McLAIN

7

Examination by Chair Sidran

20

8

Examination by Commissioner Oshie

32

9

Examination by Commissioner Jones

34

10

MICHAEL HOBBS

11

Examination by Commissioner Jones

38

12

13

14

INDEX OF EXHIBITS

15

16

EXHIBIT:

MARKED:

ADMITTED:

17

Numbers 1 through 6

18

19

18

Numbers 7 through 9

19

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19

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0016

1 P R O C E E D I N G S

2 JUDGE TOREM: We'll be on the record. Good
3 morning. My name is Adam Torem. I'm the
4 Administrative Law Judge for the Washington Utilities
5 and Transportation Commission. Today is Tuesday,
6 it's March 25th, 2008, a little after 9:30 in the
7 morning.

8 This is Docket PG-060215. This is a
9 complaint filed by the Utilities and Transportation
10 Commission Staff against Puget Sound Energy. And
11 today -- there was a full settlement filed back on
12 March the 3rd, 2008, under WAC 480-07-730, sub one.
13 It's a full settlement.

14 A week later, on March 10th, 2008, we had a
15 narrative and support of that settlement agreement
16 filed. So today's hearing is on the settlement.
17 It's to assist the Commissioners in exercising their
18 discretion as they decide whether they want to
19 accept, reject, or impose conditions on the
20 settlement terms and they will be exercising their
21 authority under the terms of WAC 480-07-750.

22 We'll take appearances from the parties.
23 There are two parties to this case, Puget Sound
24 Energy and Commission Staff. Start with Commission
25 Staff.

0017

1 MR. TROTTER: For Commission Staff, Donald
2 T. Trotter, Assistant Attorney General.

3 JUDGE TOREM: PSE.

4 MS. CARSON: For Puget Sound Energy, Sheree
5 Strom Carson.

6 JUDGE TOREM: All right. I understand the
7 parties intend today to present a panel of witnesses
8 that's already seated. They are Steven King and
9 Patricia Johnson for the Utilities and Transportation
10 Commission, Susan McLain and Duane Henderson for
11 Puget Sound Energy. And I'll ask all of you to
12 please rise and raise your right hands.

13 Whereupon,

14 STEVEN KING, PATRICIA JOHNSON, SUSAN McLAIN and
15 DUANE HENDERSON,

16 having been first duly sworn, were called as
17 witnesses herein and were examined and testified as
18 follows:

19 JUDGE TOREM: Witness panel's been sworn and
20 I understand, Counsel, that you don't intend to
21 present any opening statements this morning unless
22 asked by the individual Commissioners, and that the
23 panel of witnesses is here to answer questions, but
24 not necessarily make any opening remarks.

25 However, in your response to Bench Request

0018

1 One, you made it clear that there were nine proposed
2 exhibits and that you stipulate to their admission.
3 Let me identify those for the record and indicate the
4 sequential numbering I'll give them, and then I'll
5 hear from counsel as to any other comments on the
6 exhibits.

7 Exhibit 1 was the complaint filed in this
8 matter May 23rd, 2007. What I'll mark as Exhibit 2
9 is the first amended answer of Puget Sound Energy.
10 That was filed July 31st, 2007. Exhibit 3 is the
11 settlement agreement. As I indicated, that was March
12 3rd, 2008. There is an Attachment A to that
13 document.

14 Exhibit 4 is the narrative supporting that
15 settlement agreement, filed March 10th, 2008. Those
16 first four joint exhibits are, again, numbered 1
17 through 4.

18 Then Ms. Johnson is going to sponsor Exhibit
19 5, the Staff report of investigation. That's dated
20 March 10th, 2007. Is that correct, the year, or
21 2008?

22 MR. TROTTER: That is incorrect, Your Honor.
23 I'm sorry. It should be 2008.

24 JUDGE TOREM: All right. Thank you. Then
25 Mr. Henderson is going to sponsor Exhibits 6 through

0019

1 9. They are first Exhibit 6, PSE's response to the
2 UTC Data Request Number 003. It has an initial
3 response and a supplemented response and it's filed
4 without the attachments, as is the case for the
5 following exhibits, as well.

6 Exhibit 7 is PSE's response to UTC Data
7 Request Number 005. Exhibit 8 is the Company's
8 response to Data Request 007. And Exhibit 9 is PSE's
9 response to Data Request 012, and that, again, has
10 supplemental responses, as well.

11 So those are Exhibits 1 through 9. And I
12 understand, Mr. Trotter and Ms. Carson, that those
13 are stipulated for admission to support the
14 settlement agreement and the offer today?

15 MR. TROTTER: Yes, Your Honor.

16 MS. CARSON: That's correct.

17 JUDGE TOREM: Any other preliminaries we
18 need to get to before I turn it over to the
19 Commissioners for questions of you or the panel?

20 MS. CARSON: Just one preliminary matter.
21 We also made clear in Bench Request Number 1 that Mr.
22 Michael Hobbs is also available if there are
23 questions regarding the third party audit that can't
24 be answered by the panel. He is here.

25 Also from PSE are Mr. Steve Secrist, who's

0020

1 a deputy general counsel, and Mr. Bert Valdman, who's
2 executive vice president in charge of operations and
3 has been involved with Mr. King in several
4 initiatives related to operations, improvements,
5 customer service, and other things. So they're very
6 concerned and are here today, as well.

7 CHAIR SIDRAN: Good morning. Mark Sidran,
8 Chair of the Commission. First, I want to commend
9 the Commission Staff. And Mr. King, I don't know who
10 all was involved in this, but the fact that it was a
11 Commission audit that caught this I think is
12 important and commendable. It's something that
13 easily could go undetected, and in fact did go
14 undetected by the Company and perhaps by Pilchuck for
15 a number of years.

16 So this is exactly I think what the public
17 has a right to expect of the Commission and its
18 Staff, and I applaud all of the good work that has
19 gone into this, both in terms of detecting it and in
20 arriving at what on the whole I think is a fair and
21 reasonable settlement.

22 I also want to commend Mr. Trotter in this
23 regard. I read all of the materials, including the
24 Staff's investigative report, and it's a positive
25 reflection on the agency. So thank you all for a lot

0021

1 of good work.

2 I did not hear in -- Ms. Carson, in your
3 recitation of some of the people here, is there
4 anybody here from Pilchuck? And your name, sir?

5 MR. THIBODAUX: Paul Thibodaux.

6 CHAIR SIDRAN: Paul Thibodaux. And what's
7 your connection with Pilchuck?

8 MR. THIBODAUX: I'm the senior vice
9 president.

10 CHAIR SIDRAN: All right. Thank you. And
11 thank you for being here. Well, before I get to one
12 principal question that I have about the substance of
13 the settlement, I'd like to know, is Pilchuck bearing
14 any of the cost associated with the proposed penalty?

15 MS. CARSON: There is an indemnification
16 provision in the contract between PSE and Pilchuck,
17 and PSE and Pilchuck worked together in the
18 investigation of this matter and in defending it.
19 But that's certainly an issue that will be addressed
20 between PSE and Pilchuck. But it was decided, you
21 know, until this matter was resolved, that was not
22 going to be decided. So that's a matter to yet be
23 decided.

24 CHAIR SIDRAN: The reason I ask that
25 question is the Commission has a number of concerns,

0022

1 but one of the concerns is the health of the Company.
2 And for the Company to pay a penalty of this
3 magnitude, which, by our standards, is a substantial
4 penalty, we don't enter into that lightly, and it is
5 obvious that Pilchuck bears a substantial amount of
6 responsibility here, although it is ultimately the
7 responsibility of Puget Sound Energy. I would hope
8 that the Company does something on behalf of its
9 shareholders in this case to make sure that Pilchuck
10 bears some of the responsibility for this.

11 My principal concern about this settlement
12 has to do, as you probably can tell from bench
13 request -- I believe it was Number Two, related to
14 the forbearance provision. And I guess I'll address
15 this question to Counsel, including Mr. Trotter,
16 because I'm not entirely familiar with the specifics
17 of the prior docket that decided the precedent in
18 response to the bench request. I understand from
19 Judge Torem that there's not a lot of detail in that
20 prior order, which I will simply note was entered
21 before my arrival here and so I'm not personally
22 familiar with it.

23 But here's the concern. And I understand
24 the parameters around this forbearance provision, so
25 I understand it's limited in a number of ways,

0023

1 including limited in time to acts that occurred
2 before July 1st, 2007, and that there are other
3 exclusions for intentional acts that were --
4 intentional acts that were performed or directed as a
5 result of PSE's management or that intentional acts
6 that are, quote, significantly more widespread,
7 unquote, than the conduct that's within the current
8 complaint.

9 The concern I have is if we say, in effect,
10 that Staff is going to forbear from enforcement for,
11 quote, less serious violations, meaning those that
12 involve less than \$50,000 of property damage or less
13 than, quote, serious injury, meaning not requiring
14 hospitalization, then, in effect, we're saying all
15 those other incidents, which I understand presumably
16 we already know about if there was such an incident
17 that resulted in injury or property damage, that is
18 to say it happened before July 1, 2007, what we don't
19 know is -- we don't necessarily know, given the fact
20 that this complaint is based on just a sampling, we
21 don't necessarily know if incidents that may have
22 occurred before July 1st, 2007, that actually
23 resulted in ignition or property damage less than
24 \$50,000 or injury that did not require
25 hospitalization, we would view any of those as

0024

1 significant incidents, I believe, an actual explosion
2 that did, for example, \$40,000 of property damage or
3 sent somebody to the hospital, but they didn't
4 require a hospital stay, we would consider, under our
5 rules, to be a fairly significant incident, as these
6 things go.

7 In fact, we require reporting of incidents
8 that do not involve any of those things, that just
9 involve releases of gas for a period of time, say two
10 hours.

11 The question is we don't know if any of
12 those prior incidents that may have happened before
13 July 1st, 2007, were perhaps a result of exactly the
14 kind of misconduct that is the subject of this
15 complaint.

16 In other words, suppose there was, during
17 the window that this forbearance provides, an actual
18 ignition or explosion, actual property damage, or
19 actual injury that, if we went back and looked at the
20 records, we would find was the result perhaps of
21 intentional misconduct. The result of a leak
22 inspection done by the same person, for example, as
23 opposed to two different people.

24 We don't know that, do we? Has anyone gone
25 back and looked at every single incident that

0025

1 involved ignition or every incident that involved,
2 you know, potential property damage or anything of
3 that sort to make sure that the forbearance we're
4 granting here was not actually forbearance of an
5 ignition incident that was one of the incidents where
6 there was a violation of the rules that are at issue
7 in this complaint? Can you tell me that?

8 MR. TROTTER: This is Donald Trotter, for
9 Commission Staff. I have not investigated that
10 specific question, so I cannot answer it. But going
11 to the broader question, if I may --

12 CHAIR SIDRAN: Yes.

13 MR. TROTTER: -- feel free. Okay. The
14 concern here was, you know, forbearance on the one
15 hand and putting some parameters around it. You're
16 quite correct. There are a lot of restrictions, so I
17 think it would be an unusual case, but still, it
18 could happen. And the idea here is that if the
19 property damage, if there was a link between the
20 violation and the property damage was -- that led to
21 the property damage or personal injury and it was
22 below these parameters, that Staff would not
23 recommend an enforcement action in that context.
24 Again, with all the bells and whistles that are
25 attached, as you've noted.

0026

1 It's important to note that this is not a
2 forbearance of the Commission itself, and so if you
3 saw this or got this information and wished to file a
4 complaint, you could do so.

5 CHAIR SIDRAN: Mr. Trotter, much as I
6 enjoyed being a prosecutor in a former life, I
7 seriously doubt that, given a choice between the
8 Commission itself pursuing a complaint and asking
9 that Staff pursue a complaint, it's not in my mind
10 something that we would be likely to do.

11 MR. TROTTER: Well, I think -- let me just
12 state that the way I would see this working is if a
13 number of violations occurred or even one for which
14 forbearance applied that you thought was a serious
15 matter, you could ask ALD, Administrative Law
16 Division, to draft up a complaint. Staff could
17 participate in that. And I think if the Commission
18 issued it, Staff would -- the forbearance of Staff is
19 done and it could participate in that.

20 So I think there are -- it's a lot different
21 to me, categorically different from the Commission
22 saying it will not issue a complaint.

23 But to the extent you have concerns about
24 the practical side of that, then so be it. But this
25 was an attempt to draw kind of a bright line and give

0027

1 the Company some assurance of forbearance, but yet
2 have some protection if a matter was a serious one.

3 CHAIR SIDRAN: Well, I take your point.
4 Here's my concern. It's not just the practicalities.
5 It's also the policy and the precedent. For example,
6 in the response to a bench request, we're cited to a
7 prior order of the Commission where some similar
8 forbearance apparently was granted. Again, I don't
9 know the details in that docket.

10 What I do know is this docket will be cited
11 in some future context for this forbearance
12 provision, and that's why I'm concerned about the
13 precedent and the message it sends to the public
14 about how we use or how the Commission views
15 forbearance.

16 And the reason I'm troubled by this is that
17 it seems to me, from a public policy point of view
18 and from a precedent point of view, that for the
19 Commission to say where a company engages in willful,
20 intentional misconduct and fraud in non-compliance
21 with rules and regulations that directly relate to
22 public safety and where -- and again, I understand
23 that the likelihood that this will arise is extremely
24 remote, so I don't want anyone to think that, you
25 know, I'm obsessed here about what may be a small

0028

1 risk. I understand it's a small risk.

2 The issue here, though, is the public policy
3 and the precedent and the symbolism. That does
4 matter, even though the risk may be small, because a
5 commissioner five years from now who looks back and
6 is reading some order where somebody is citing this
7 docket for the proposition that forbearance is an
8 accepted practice with the Commission. I would like,
9 if I were in that situation, I would like to
10 understand how the line was drawn.

11 And I'm not comfortable with where this line
12 is drawn, because it suggests that there might be an
13 incident that we're not aware of that is linked to
14 this kind of misconduct. Even though the damage is
15 below \$50,000, I don't find any comfort in saying,
16 Well, our policy is \$40,000 of damage that resulted
17 from intentional, willful misconduct and fraud is not
18 that bad, because it's not a serious, quote, unquote,
19 incident.

20 So again, I understand the risk is low, but
21 I'm concerned about the policy and the precedent.

22 Mr. King.

23 MR. KING: Thank you, Mr. Chairman. I just
24 wanted to make a couple of points. One, in your
25 earlier comment, you pointed to incidents that have

0029

1 occurred in the past, reported to us under the
2 various provisions under our incident reporting rule,
3 480-93-200.

4 Just so that you understand this, the
5 Commission monitors all incidents that are reported
6 under the rule and investigates where we think it
7 appropriate, and obviously we investigate the most
8 serious ones, even if someone isn't injured or if the
9 damage is less than 50,000. So that history has
10 already been -- as those occur, those have been
11 reviewed and investigated as appropriate.

12 We have not gone back with this settlement
13 in mind and looked at prior incidents and tried to
14 figure out whether they could have been related to a
15 leak investigation, as described in the Staff report.
16 I just wanted to make that clear.

17 CHAIR SIDRAN: Yeah, I thank you for the
18 clarification and I appreciate your point. I'm still
19 left with this concern. It would not be, I would
20 think, and correct me if I'm wrong, it would not
21 normally occur to our investigators that, among
22 everything else that they need to think about when
23 they're looking at an incident, they need to actually
24 look for fraud in the leak inspection report because
25 someone has written the wrong name, a false name, in

0030

1 relationship to the inspection, or they have
2 post-dated the phantom leak.

3 The kinds of things that are at issue here,
4 I'm guessing, and you can correct me if I'm wrong,
5 are not routinely looked at in the context of a
6 typical incident investigation. And so that's why
7 I'm concerned.

8 MR. KING: All right.

9 CHAIR SIDRAN: Because if we were to go back
10 and connect the dot here, I would be concerned about
11 saying, well, we've agreed that even though it
12 involved this kind of misconduct, we agreed to
13 forbearance.

14 MR. KING: Okay. The other point I would
15 like to make, if I may, is Staff was looking --
16 believed that we need to preserve the Commission's
17 ability to act when it needs to act. And to a
18 certain extent, we drew this line here, and maybe it
19 was the wrong line, but we do believe that the intent
20 was -- preserved the Commission's ability to act when
21 it must.

22 CHAIR SIDRAN: Again, I appreciate that, and
23 it's -- I'm not suggesting that what is in the
24 settlement is unreasonable. I'm just suggesting that
25 if the standard that we're going to apply is the

0031

1 public interest standard and we think about precedent
2 and we think about the broader context of public
3 policy, I'm troubled by this provision, and now's the
4 opportunity for Staff and the Company to explain to
5 me why this is, again, recognizing the risk is small,
6 why this is a provision that we ought to accept,
7 because, as you can tell, I'm not inclined to accept
8 it.

9 MR. KING: Just so I understand, is it the
10 line we've chosen you're not willing to accept or the
11 sort of forbearance in question?

12 CHAIR SIDRAN: It's the line. The general
13 forbearance that's in here in terms of saying, you
14 know, we're not pursuing similar situations that fall
15 within the general parameters that are described here
16 in terms of time, things that may come to our
17 attention in the course of an audit.

18 Most of what is in here is reasonable. What
19 I'm troubled by is this one dimension which is the
20 exclusion of incidents that result in actual property
21 damage, actual injury to people, that we may not now
22 know is an incident in which there was this kind of
23 willful misconduct in a leak inspection related to
24 that incident.

25 And what I've heard this morning is we don't

0032

1 -- we cannot say, as we sit here today, that we know
2 that there are no such incidents; correct?

3 MR. KING: We haven't drawn that line, but I
4 did say that we do investigate the more serious
5 incidents and find out what was the cause and make a
6 decision whether to act or not on that basis and have
7 done so historically. But whether we drew it back to
8 whether the leak investigation records had been
9 falsified, no, we had not.

10 CHAIR SIDRAN: Thank you. All right. I
11 think I'm finished with that line of inquiry and I'm
12 going to defer to my colleagues here. I may come
13 back with another question. Thank you.

14 COMMISSIONER OSHIE: I just have one
15 question to follow up, and this is in Paragraph 23 of
16 the settlement agreement. And I'd like to understand
17 the intent of the parties.

18 I believe it's the sentence, the second
19 sentence. For each such violation that is
20 discovered, PSE will document the violation and
21 correct the deficiency to the extent possible. And
22 I'm just trying to figure out what the parties mean
23 by that, to the extent possible.

24 Is it that -- maybe you can explain. Is
25 that just waffle words or to give you a more passive

0033

1 approach to correcting the deficiency or is it that
2 the deficiency would be corrected? Maybe -- does it
3 have to do with a time? In other words, is it
4 related to time? It can't be corrected immediately,
5 but it could be corrected over a period of time? I
6 mean, I would expect that the deficiency would be
7 corrected, not corrected to the extent possible.
8 That's certainly a subjective way of approaching it,
9 so -- Mr. Henderson?

10 MR. HENDERSON: This is Duane Henderson.
11 The language there, and this was drawn out in our
12 answer in the investigation to the incidents that
13 Staff had identified. There were certain incidents
14 where we were unable to identify the actual chain of
15 events that occurred. We weren't able to identify
16 who actually performed the work or on what day the
17 work was performed. In absence of any exact records
18 to do that, we didn't feel that we could go back and
19 correct the deficiency to some other information.

20 COMMISSIONER OSHIE: You mean to a person
21 that had actually performed or not performed the
22 audit and -- because correcting the deficiency would
23 be some type of disciplinary action of that employee?

24 MR. HENDERSON: No, the deficiency was more
25 centered around the actual records themselves. So

0034

1 one of the complaints, one of the items in the
2 complaint here is that the records were not accurate.
3 So as we went through the investigation and we
4 identified what the actual records should reflect, we
5 went back and changed the records to reflect that.

6 This language, and I think there were four
7 or five incidents where we were not able to establish
8 exactly what happened on that record, we knew the
9 work was performed, but we weren't able, through
10 interviews with people or through time sheets or
11 whatever, able to establish who actually did the
12 work, so we weren't able to correct the deficiency,
13 we weren't able to change the record to something
14 that we had no evidence that could support it.

15 And that's what the language in Paragraph 23
16 is trying to establish, that we will do the
17 investigation, we will, to the best of our ability,
18 establish what the records should reflect, and we
19 will make that change when we're able to do so.

20 COMMISSIONER OSHIE: All right. Thank you.
21 Mr. King?

22 MR. KING: Oh, I agree. That is exactly
23 what the provision is for.

24 COMMISSIONER OSHIE: All right.

25 COMMISSIONER JONES: This is Commissioner

0035

1 Jones. I'd like to echo the Chairman's remarks on
2 the Staff work on this. I think the Staff did a good
3 job. I'd also like to commend the anonymous person
4 who tipped I guess the Commission Staff off that
5 these sorts of falsification of data is occurring.
6 It's important to the greater public when we have a
7 broad public safety in ensuring the safety of the
8 local distribution system of all our gas companies
9 that these rules be followed and be followed closely.
10 So thanks to whoever that person is.

11 My question is on the third party review of
12 mandated safety activities in the appendix to the
13 settlement agreement. So I have a few questions on
14 this, both to the Company, Ms. McLain, and to the
15 Staff.

16 Is it my understanding that this sort of --
17 this activity is going to be a joint effort between
18 the Company and the Staff?

19 MS. McLAIN: This is Sue McLain, and yes,
20 the intent is that this will be a joint effort, both
21 in the selection of the consultant who performed the
22 third party audit and to be involved as we scope the
23 work and as the audit takes place, along with the
24 findings of the audit.

25 COMMISSIONER JONES: In terms of the

0036

1 contractual activity, the contract, I assume, will be
2 between PSE and the contractor; correct?

3 MS. McLAIN: Correct. But Staff will be
4 involved in the selection of the contractor, as well.

5 COMMISSIONER JONES: So Mr. King, are you
6 going to be fully involved, from Staff's perspective,
7 in both the scope of the independent audit and the
8 selection of the contractor? And for example, what
9 would happen if Staff disagrees with the selection of
10 the independent evaluator or auditor? What would you
11 do then? Would it come to the Commission or could
12 PSE just proceed on its own?

13 MR. KING: I'm confident that we will be
14 able to agree, find a way to do that. The Commission
15 will retain jurisdiction of this. If we can't,
16 Counsel, what did we decide on this point?

17 MR. TROTTER: I think any -- I think, first
18 of all, every effort has been made to reach
19 agreement. We could get mediation, if that's
20 necessary, and the last resort, bring it to you.

21 MR. KING: Thank you.

22 MR. TROTTER: Meaning the Commission.

23 MR. KING: So we intend to be fully
24 involved. I hope you aren't directing me personally
25 to be fully involved.

0037

1 COMMISSIONER JONES: I'm directing your
2 Staff.

3 MR. KING: Yes, we intend to be fully
4 involved, as Ms. McLain described. We intend to
5 participate in the discovery, the interviews and the
6 inspections on a selective basis and review all
7 documents that are developed.

8 COMMISSIONER JONES: Mr. King, has the
9 Commission Staff ever done anything like this before,
10 been involved in a joint study paid for by the
11 Company on an issue of this sort?

12 MR. KING: No, sir. To my knowledge, this
13 is unprecedented.

14 COMMISSIONER JONES: Ms. McLain, how many
15 qualified bidders or firms are out there? And would
16 this company -- what sort of independents are you
17 contemplating? Would this be a company that would
18 have worked for either PSE or an IOU? Would it be
19 in-state or out of state? What sorts of things --
20 what sort of universe of companies are we talking
21 about and what sort of independents' procedures are
22 you putting in place?

23 MS. McLAIN: It probably makes the most
24 sense for Michael Hobbs, Mike Hobbs to answer that
25 question, in that he has been involved in the scoping

0038

1 and the request for proposal process.

2 COMMISSIONER JONES: Mr. Hobbs.

3 JUDGE TOREM: Mr. Hobbs, if you'd raise your
4 right hand. Is it Michael?

5 MR. HOBBS: Michael's fine.

6 Whereupon,

7 MICHAEL HOBBS,

8 having first been duly sworn by Judge Torem, was
9 examined and testified as follows:

10 JUDGE TOREM: Thank you.

11 COMMISSIONER JONES: So maybe you can just
12 describe what has -- my understanding, from reading
13 the third party review, the scope so far is that as
14 soon as we issue an order, there will be 30 days for
15 an RFP and then 60 days after to select a contractor.
16 But have you already been scoping out an RFP? And
17 what sort of activities have you been doing to date
18 in contacting perhaps qualified third party auditors?

19 MR. HOBBS: Commissioner, at this point what
20 we have done is looked at various contractors across
21 the country. We know there are some that reside East
22 Coast to West Coast. We will have a meeting in April
23 with Commission Staff to start the process of
24 identifying who we each agree should be on the list,
25 and then start developing the parameters to put into

0039

1 writing the RFP that will go out. At this time, we
2 have no preconceived ideas of who the consultant
3 would be. That would be something we would jointly
4 agree upon.

5 I think the first step is agree upon the
6 list that we all agree are the most qualified
7 consultants to perform the work and then, once the
8 RFP is put in place, see who responds, and then go
9 through the elimination process of selecting the most
10 qualified contractor.

11 COMMISSIONER JONES: And is this going to be
12 an ongoing activity or is this going to be a one-time
13 audit? Is this going to be an annual activity or
14 will it end at a date certain?

15 MR. HOBBS: I think with this direct third
16 party audit that we're envisioning here, this would
17 be a one-time effort that we would jointly agree.
18 There is a follow-up meeting that will take place
19 once the work that is identified and performed as a
20 result of the audit is completed.

21 The consultant will come back, evaluate how
22 well that work was done in regards to the
23 recommendations that were made. Staff and PSE will
24 agree, I think, with the results of what the auditor
25 comes back with.

0040

1 I think at that point in time, we will make
2 an evaluation internally to see if this is an issue
3 we should continue to go forward with on some regular
4 basis. We have in the past, on our own, had a number
5 of consultants come in over the last three years and
6 perform complete audits of various parts of our gas
7 system, so it isn't that we haven't done that in the
8 past. We've rigorously performed those audits. I
9 think it's just an agreement we'll have to reach with
10 the Staff to determine if we continue with this type
11 of process.

12 COMMISSIONER JONES: So what is your current
13 best guess of how long this is going to take and how
14 much totally it's going to cost?

15 MR. HOBBS: At this point, I don't know that
16 I have an estimate on the time. I think it's going
17 to be, once we agree upon the scope, pick the
18 contractor, find out what his availability is on when
19 he can start within our parameters, we're going to
20 have to go with that. I can't estimate how much
21 time. I don't know if it will be a sole proprietor
22 type business or a firm that can dedicate a lot of
23 employees to the audit. I just don't have that, you
24 know, knowledge to be able to answer that question
25 directly.

0041

1 COMMISSIONER JONES: This is more for Ms.
2 Carson and Ms. McLain. In the agreement, PSE will
3 pay and this is going to be below-the-line expenses;
4 is that correct? The first 250,000 is below the
5 line?

6 MS. CARSON: That's correct.

7 COMMISSIONER JONES: And then, as I read the
8 settlement agreement, nothing in this agreement
9 either binds the parties or binds -- you can't bind
10 the Commission, but nothing -- there's no direction
11 provided on costs in excess of 250,000?

12 MS. CARSON: That's correct. It's --
13 nothing prohibits the Company from seeking recovery
14 of it, but as you say, we can't bind the Commission.

15 COMMISSIONER JONES: So you could
16 conceivably come in, if this were to be 500,000, I'm
17 just throwing out numbers here, or a million dollars,
18 you would file a petition -- you could file a
19 petition with the Commission to recover those
20 expenses?

21 MS. CARSON: That's correct. I think it's
22 important to recognize that this third party audit is
23 very broad in scope. It's broader in scope, it
24 covers much more than the violations alleged in this
25 complaint. And that is the reason that a portion of

0042

1 it is not recoverable, but the Company has retained
2 the right to seek recovery of part of the cost of the
3 audit.

4 COMMISSIONER JONES: Sure. Mr. Trotter, in
5 paragraph H of this scope, in the third -- in the
6 second paragraph, in H, I'm a little confused about,
7 especially with the Chairman's remarks in the
8 beginning, could you explain this paragraph to me,
9 kind of summarize it?

10 It basically, as I read it, says that Staff
11 will not utilize or does not intend to utilize any of
12 the information gathered by let's say Consultant X.
13 And let's say the study takes a year. So in year --
14 in month nine, they develop some information that's
15 quite troubling on systematic -- systemic problems or
16 some willful violation and it comes up in the
17 consultant's report.

18 So what would be, in light of such
19 information coming to light in this independent
20 audit, this appears to be binding or putting a limit
21 on Staff's ability to use that information in an
22 enforcement action.

23 MR. TROTTER: Yes. Well, it is a
24 forbearance provision, as you know.

25 COMMISSIONER JONES: Right.

0043

1 MR. TROTTER: The first sentence there is
2 just intended to convey that the third party audit is
3 not a complaint -- is not fodder for future
4 enforcement actions by Commission Staff.

5 It's an effort to get to the root of some
6 issues and hopefully, if improvements are warranted,
7 that they'll be made and that the parties will be --
8 have candor with one another, so if there are
9 problems that come up that may be violations, that's
10 understandable. If intentional misconduct arises,
11 other than the type that we've come up with in the
12 complaint or conduct that's systematic or widespread,
13 all bets are off with regard to enforcement in that
14 context.

15 So that's the intent of it. And I think the
16 idea, if we're doing an audit of this scope, chances
17 are there will be some areas beyond compliance that
18 are found. The issue is what to do with that. And
19 to keep parties in full candor with one another, some
20 forbearance was desirable, and this is what we came
21 up with.

22 COMMISSIONER JONES: I understand. My last
23 question, of a more technical nature, at least on the
24 settlement agreement, refers to paragraph 16 of the
25 settlement agreement.

0044

1 This is more for Ms. McLain, but also, Mr.
2 King, could you chime in? There's a three-month
3 delay on the obligation between the obligations on
4 Pilchuck to comply to perform a QC plan. My
5 understanding is that's due in like next week, right,
6 by the end of March. But the settlement agreement
7 provides for more time for these other four
8 companies.

9 First of all, what percent of your work
10 generally on the gas LDC system is done by Pilchuck,
11 as opposed to these other companies?

12 MS. McLAIN: In terms of the total scope of
13 work, Pilchuck performs the vast majority of our
14 construction work.

15 COMMISSIONER JONES: Okay.

16 MS. McLAIN: And then they --

17 COMMISSIONER JONES: That's greenfield work,
18 new buildings, new residences?

19 MS. McLAIN: Correct. New customer
20 construction, as well as replacement of existing
21 mains. So for example, if we are adding capacity,
22 they will perform that construction activity, as
23 well, or if we are eliminating an older system and
24 replacing it with a new system.

25 So they will perform the construction work.

0045

1 Some of the construction work is -- continues to be
2 bid out, so other contractors would bid on that work,
3 as well. They also perform the leak piece that has
4 been discussed in this complaint.

5 COMMISSIONER JONES: Right.

6 MS. McLAIN: And our own personnel perform
7 gas emergency response.

8 COMMISSIONER JONES: Right.

9 MS. McLAIN: Customer service. We also,
10 in-house, perform all industrial meter work and our
11 system controls and protection. So cathodic
12 protection work with the gas system.

13 COMMISSIONER JONES: So back to my question.
14 Why is an additional three months then given to these
15 other companies? From the Company's perspective.

16 MS. McLAIN: From our perspective, it's
17 making certain -- part of this is the documenting of
18 our own Puget Sound Energy work, which we had relied
19 on I'll say our own personnel to perform that work
20 activity and ensure its compliance. So we did not
21 have written documentation on the way in which we
22 would perform our own quality control for Puget Sound
23 Energy employees and then the quality assurance, the
24 third party, Mike Hobbs' shop, performing that check
25 on our own employees.

0046

1 We also want to make certain -- we did not
2 have a quality control requirement for all of our
3 contractors. We want to make certain that we have
4 that documentation, that we've reviewed it, and that
5 we have specific quality assurance documentation for
6 each contractor separately. So we feel that we need
7 to have that time in order to make certain all of the
8 records are accurate and that we're performing in
9 that fashion. I don't know, Duane, if you wanted to
10 add to that.

11 MR. HENDERSON: Yeah, if I could add maybe
12 just a little bit. Part of the process that was
13 outlined in Paragraphs 14 through -- really, I think
14 it's 18, involves a lot of interaction with Staff and
15 Staff's consultant.

16 So part of the thinking was that out of the
17 chute, there would be a lot of leg work required up
18 front in all parties agreeing on what the format and
19 structure needed to be to these quality control plans
20 and quality assurance plans. Once that's been ironed
21 out, then the application to the additional
22 contractors that are involved, the locating
23 contractors and the leak survey contractors, would be
24 really more around form, rather than the substance of
25 the discussions that occurred in outlining those with

0047

1 Pilchuck.

2 In fact, for the better part of this year
3 now, we've had those conversations ongoing with Staff
4 and with Staff's consultant, and just two weeks ago,
5 we actually submitted the quality control plan for
6 Pilchuck for satisfying this requirement.

7 So even though the order hasn't been issued,
8 we're well on our way to satisfying that particular
9 requirement. So that was kind of the thought behind
10 how it was structured out and why there was kind of
11 phasing of the different plans in meeting the order,
12 or the settlement agreement. Sorry.

13 COMMISSIONER JONES: So Ms. McLain, based on
14 the -- I'm a little more troubled now than I was
15 before. Based on what you just said, PSE itself has
16 had no QC, quality control plan in place to oversee
17 its relationships with its five contractors on issues
18 of this sort?

19 MR. HENDERSON: The comment that Ms. McLain
20 was making was quality control with regard to our own
21 crews performing work for itself. We relied on the
22 --

23 COMMISSIONER JONES: No, that's what I
24 meant.

25 MS. McLAIN: But these were our employees.

0048

1 MR. HENDERSON: The work performed by our
2 employees on our system. Not the work that the
3 contractors were --

4 COMMISSIONER JONES: No, I understand the
5 settlement agreement, the QC plan is a QC plan for
6 Pilchuck, for Quanta, for Potelco, right? Those are
7 going to be QC plans for the contractors. I'm
8 talking about a QC plan for PSE.

9 MS. McLAIN: Our own employees, yes.

10 COMMISSIONER JONES: So has that been in
11 place since 2001?

12 MS. McLAIN: We have not had a formal
13 program. What we expect is that our supervisors
14 oversee the work of our employees, and that this --
15 and what we are doing is formalizing and documenting
16 these processes.

17 COMMISSIONER JONES: I see. So it's more of
18 a formalization and documentation process?

19 MS. McLAIN: Yes. Thank you.

20 COMMISSIONER JONES: Well, to this
21 Commissioner, that's very important. I lived for
22 quite a period of time in Japan, and all companies,
23 most companies, companies of your size all have had
24 QC programs in place for years. So this -- the lack
25 of formality here surprises me a bit. That's all I

0049

1 have for now, Mr. Chair.

2 MR. KING: Commissioner Jones? If I may,
3 Mr. Jones?

4 COMMISSIONER JONES: Yes.

5 MR. KING: I think the amount of time is
6 reasonable. I agree with Mr. Henderson, we've been
7 actively involved with the Company since -- the
8 Pilchuck plan since I think just after the first of
9 the year, had several meetings or teleconferences, so
10 there is a bit of work involved in it.

11 As to the provision itself, I think the way
12 I think about this is while the Company or its
13 contractors have had some quality assurance, quality
14 control programs in place, this is more thorough
15 going, all gas safety activities, whether done by the
16 Company or the contractor, and the appropriate
17 self-auditing or self-inspecting of the work that the
18 people do, plus oversight in a quality assurance
19 manner. So it's a more comprehensive, complete
20 process that covers more activities and more
21 formalized.

22 COMMISSIONER JONES: And if, Mr. King, if
23 the QC or QA plans are not adequate or, in the view
24 of the independent auditor that is to be hired, he or
25 she, that firm could come back and make some

0050

1 recommendations on perhaps some changes or
2 enhancements or some changes to that; correct?

3 MR. KING: I would expect so. But I would
4 point out that we have our own contractor working
5 with us on this consultant, who has a lot of
6 experience in this area and he's been fully involved.

7 COMMISSIONER JONES: Sure. I understand.
8 Thank you.

9 JUDGE TOREM: Mr. Jones, I want to pick up
10 where you were on the third party agreement, page
11 two, Paragraph H. I think this is better answered by
12 Counsel, but the third paragraph, the last sentence,
13 has a tie-in to the settlement agreement and
14 references Paragraph 33 after discussing the
15 forbearance that we started our discussion with this
16 morning.

17 I think that paragraph number changed
18 somewhere along the way, because certainly we're not
19 referring back to whether the copies can sign the
20 counterparts, which is the current Paragraph 23.

21 MR. TROTTER: You're correct.

22 JUDGE TOREM: So for housekeeping, do you
23 have a different number for me?

24 MR. TROTTER: Yes, I apologize. I thought
25 we had dealt with that. Let me take a look. Just a

0051

1 moment.

2 CHAIR SIDRAN: While Counsel's looking for
3 that, I will go ahead and make some closing comments,
4 because Judge Trotter tells me that's the only --

5 JUDGE TOREM: Judge Torem.

6 CHAIR SIDRAN: Torem, I'm sorry.

7 JUDGE TOREM: You may have a different
8 preference, but you're stuck today.

9 CHAIR SIDRAN: No, I certainly did not mean
10 to insult Counsel, referring to you as a judge.

11 But first, I just want to say something that
12 must be said in a situation like this, although it
13 probably goes without saying. The size of the
14 proposed penalty is a reflection of the fact that, at
15 least since I've been here and as far as I know, this
16 rises to the top of serious violations in
17 relationship to both the Company's duty and public
18 safety.

19 That said, I commend the Company for taking
20 it seriously and for the manner in which the
21 Company's approached resolution of this matter.

22 I will only leave the Company with the
23 following observation. It is ultimately a business
24 judgment as to what extent and how the Company
25 chooses to contract out its work. But there have

0052

1 been two recent examples that suggest the Company
2 needs to take, if you will, a more proactive
3 approach, as is suggested in this settlement
4 agreement, with respect to quality control and
5 assurance plans.

6 This one is obviously an egregious example
7 of the need for those kinds of programs, but it is
8 also reflected in the consultant's report that
9 followed the aftermath of the Hanukkah eve windstorm
10 in relationship to challenges that arose in terms of
11 coordination and communication in the restoration of
12 service that, although, again, different, for sure,
13 from this particular kind of problem, reflects the
14 challenges that the company faces having chosen to
15 extensively contract out critical components of its
16 responsibilities.

17 So I encourage the Company to, as I know it
18 has in the context of this settlement, to, in the
19 broadest sense, make sure that it is doing everything
20 that can be done to guarantee that the services
21 provided by its contractors meet not only the letter
22 of the law with respect to the Commission's rules and
23 regulations, but also provides the customers with the
24 service and the safety that they're entitled to.

25 And with that, perhaps now Counsel has the

0053

1 paragraph.

2 MR. TROTTER: Yes, instead of 33, it should
3 read 23, so if you could make that correction. I'm
4 sure PSE Counsel agrees, also.

5 JUDGE TOREM: So 33 is going to be changed
6 to 23?

7 MR. TROTTER: Yes.

8 JUDGE TOREM: Thank you, Your Honor. All
9 right. Commissioners, anything else for the panel of
10 witnesses or this Counsel? Any closing statements
11 from Counsel or do you intend your witnesses to
12 provide any?

13 MR. TROTTER: No, Your Honor, unless you
14 wish one.

15 MS. CARSON: No.

16 JUDGE TOREM: Not necessary. Thank you for
17 the responsiveness. Mr. King has something, though.

18 MR. KING: I want to butt in, if I might.
19 Both the Chair and Commissioner Jones commented on
20 the Staff work. I want to point out that Patty Jones
21 -- Johnson, I've met her before, and Don Trotter --

22 COMMISSIONER JONES: This is Commissioner
23 Jones.

24 CHAIR SIDRAN: Just don't call her a judge.

25 MR. KING: -- have done an exceptional

0054

1 amount of work on this. And Patty was a bulldog and
2 sort of like Miss Marple or another famous detective,
3 comparing records against other records, and was
4 tireless in that. I just wanted to point out, a lot
5 of people worked on this, but we wouldn't be here
6 without Patty and Don and the work they did on it.

7 JUDGE TOREM: Thank you. And I know the
8 Commissioners are all very appreciative of the Staff
9 work and want to see more and more things like this.

10 CHAIR SIDRAN: Well, not exactly.

11 JUDGE TOREM: Not exactly, but this sort of
12 effort. Let me clarify that. This sort of effort.
13 Thank you to the Company's witnesses and to
14 Commission Staff's witnesses. Thank you to Counsel.
15 We'll get an order out in the next few weeks and let
16 you know what the Commissioners want to do with the
17 settlement agreement itself. Thank you. We are
18 adjourned.

19 (Proceedings adjourned at 10:25 a.m.)

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