

Exhibit No. \_\_\_ (MPG-11)

Docket Nos. UE-121697/UG-121705 and UE-130137/UG-130138

Witness: Michael P. Gorman

**BEFORE THE WASHINGTON UTILITIES AND TRANSPORTATION COMMISSION**

WASHINGTON UTILITIES AND	)	
TRANSPORTATION COMMISSION,	)	
	)	
Complainant,	)	Dockets UE-121697 and UG-121705
	)	<i>(Consolidated)</i>
v.	)	
	)	Dockets UE-130137 and UG-130138
PUGET SOUND ENERGY, INC.,	)	<i>(Consolidated)</i>
	)	
Respondent.	)	
_____	)	

**RESPONSE TESTIMONY OF MICHAEL P. GORMAN**

**ON BEHALF OF**

**THE INDUSTRIAL CUSTOMERS OF NORTHWEST UTILITIES**

**April 26, 2013**

1 Combined, the rate moratorium and these settlement regulatory mechanisms do  
2 not provide for a transparent assessment of PSE's earned return on equity nor cost of  
3 service during the rate moratorium. This lack of assurance that rates are no higher  
4 than necessary to permit PSE to recover its reasonable and prudent cost of service, is a  
5 material deficiency in the proposed ERF settlement.

6 **Q. DO YOU BELIEVE THAT THE COMPANY'S PROPOSED REVENUE**  
7 **DEFICIENCY IS REASONABLE?**

8 **A.** No. Table 2 below summarizes the necessary adjustments that will reduce the  
9 Company's proposed ERF revenue deficiency from \$32.2 million to \$11.9 million.

<b>TABLE 2</b>	
<b>ERF Revenue Deficiency</b>	
<b>(Electric)</b>	
<b>(Millions)</b>	
<u>Description</u>	<u>Amount</u>
PSE	\$32.20
<u>Adjustments:</u>	
Rate of Return	\$11.00
Pension Expense	2.60
Incentive Compensation	3.24
Effective Tax Rate	<u>3.45</u>
Total Adjustments	\$20.29
Revised Increase	\$11.91
Source: Exhibit No. ____ (KJB-3), p. 1.	

10 **Rate of Return**

11 **Q. PLEASE DESCRIBE YOUR PROPOSED RATE OF RETURN FOR PSE IN**  
12 **THESE PROCEEDINGS?**

13 **A.** I am proposing several adjustments to the development of PSE's rate of return. These  
14 adjustments include: (1) capital structure adjustments to reflect the Company's actual

1 capital structure for regulated utility operations; and (2) a proposed return on equity of  
2 9.30%, which is a reduction from PSE's requested 9.80% return on equity approved in  
3 PSE's last general rate case.

4 **Q. WHAT IS THE REVENUE REQUIREMENT IMPACT OF THESE RATE OF**  
5 **RETURN ADJUSTMENTS?**

6 **A.** PSE's rate of return is reduced from its proposed 7.80% to 7.60%. This reduced  
7 return reduces PSE's claimed electric revenue requirement by \$11.0 million (as  
8 developed on my Exhibit No. \_\_\_\_ (MPG-4)).

9 **Capital Structure**

10 **Q. WHAT CAPITAL STRUCTURE IS THE COMPANY PROPOSING TO USE**  
11 **IN THIS REGULATORY PROCEEDING?**

12 **A.** PSE's ERF revenue requirement is based on the capital structure approved in its last  
13 rate case – Order 08, in Dockets UE-111048 and UG-111049. This capital structure is  
14 shown below in Table 3.

1 **Q. WHY DO YOU BELIEVE THAT THE APPROVED RETURN ON EQUITY OF**  
2 **9.80% EXCEEDS THE CURRENT MARKET COST FOR PSE?**

3 **A.** Market costs of capital have declined since PSE’s last general rate case. This is  
4 illustrated by a comparison of bond yields in this case and in PSE’s last rate case. In  
5 Table 5 below, I show the change in utility bond yields.

<b>TABLE 5</b>			
<b><u>Capital Costs – PSE’s Rate Cases</u></b>			
<b><u>Description</u></b>	<b><u>Current Case</u></b> <sup>1/</sup>	<b><u>Docket No.</u></b> <b><u>UE-111048</u></b>	<b><u>Yield</u></b> <b><u>Change</u></b>
<b>“A” Rated Utility Bond Yields</b>	<b>4.14%</b>	<b>4.40%</b>	<b>-0.26%</b>
<b>“Baa” Rated Utility Bond Yields</b>	<b>4.67%</b>	<b>5.08%</b>	<b>-0.41%</b>
<b>13-Week Period Ending</b>	<b>04/19/2012</b>	<b>05/04/2012</b>	
<b>Source:</b>			
<sup>1/</sup> Exhibit No. ____ (MPG-20), page 1.			

6 As shown in the table above, the current market cost of debt for “A” and “Baa”  
7 (by Moody’s) rated utility bond yields has decreased in this case relative to PSE’s last  
8 rate case. The current “A” rated utility bond yields is approximately 25 percentage  
9 points lower now than it was in PSE’s last rate case. Similarly, the current “Baa”  
10 rated utility yield is approximately 40 basis points lower today.

11 Hence, the decline in utility bond yields suggests that PSE’s current capital  
12 cost should be much lower today than it was at the time the final order in the last rate  
13 case was issued.