EXHIBIT NO. ___(JHS-26T)
DOCKET NO. UE-060266/UG-060267
2006 PSE GENERAL RATE CASE
WITNESS: JOHN H. STORY

BEFORE THE
WASHINGTON UTILITIES AND TRANSPORTATION COMMISSION

WASHINGTON UTILITIES AND TRANSPORTATION COMMISSION, **Complainant,** **v.** **PUGET SOUND ENERGY, INC.,** **Respondent.**	**Docket No. UE-060266** **Docket No. UG-060267**

PREFILED SUR-SURREBUTTAL TESTIMONY (NONCONFIDENTIAL) OF
JOHN H. STORY
ON BEHALF OF PUGET SOUND ENERGY, INC.

SEPTEMBER 12, 2006

PUGET SOUND ENERGY, INC.

PREFILED SUR-SURREBUTTAL TESTIMONY (NONCONFIDENTIAL) OF JOHN H. STORY

Q. Are you the same John H. Story who submitted prefiled direct testimony in this proceeding on February 15, 2006, supplemental prefiled direct testimony in this proceeding on July 10, 2006, and prefiled rebuttal testimony in this proceeding on August 23, 2006, each on behalf of Puget Sound Energy, Inc. ("PSE" or "the Company")?

A. Yes.

Q. What is the purpose of your prefiled sur-surrebuttal testimony?

A. My prefiled sur-surrebuttal testimony responds to several statements made in the prefiled surrebuttal testimony of Mr. James M. Russell of the Commission Staff, Exhibit No. ___(JMR-7T), regarding PSE's proposal for post-test period plant additions as an alternative to a Depreciation Tracker mechanism.

Q. Mr. Russell claims that there is "no way to verify, at this late stage of the proceeding (or ever), that the projects included in the proposal are in fact

pure non-revenue producing and non-expense reducing rate base additions."[1] Do you agree?

A. No. There is no need to individually investigate every single project included in the Company's proposed alternative adjustment, and that is not how Commission Staff verification of a Company filing typically proceeds.

It is quite common for a utility filing to summarize or aggregate a vast amount of detail. "Verification" of the filing does not require that an auditor investigate each item of detail. Rather than looking at every detail of the information, an auditor will typically select a sample from each of the areas of the filing for detailed review. For example, Commission Staff has never investigated each and every entry in the Company's general ledger down to the work order and invoice, and should not be expected to do so. A sampling approach is the typical way of conducting an audit and should as well be applied to the Company's proposed alternative adjustment or depreciation tracker if so accepted. PSE's workpapers and the data request process provided sufficient information for Commission Staff to audit the Company's adjustment.

To the extent Mr. Russell is objecting to being provided with this information at the rebuttal stage of the case, a "known and measurable" adjustment for post-test year infrastructure investments necessarily requires that additional information be provided later in the case in order to capture a sufficient amount of additional

[1] Exhibit No. ___(JMR-7T) at page 2, lines 14-16.

investment to meaningfully address the regulatory lag described in the Company's prefiled direct testimony. Although the Company tries to keep such adjustments to a minimum, the Company should not be penalized because the information is not known at the time of the original filing.

Finally, Mr. Russell's concern about auditing would tend to support the Company's original proposal for a Depreciation Tracker mechanism. By having an established mechanism that is filed annually, other parties would have ample time to audit various aspects of the filings.

Q. Mr. Russell's asserts that "Puget's proposal unfairly includes capacity additions."[2] Do you agree?

A. As described in Ms. McLain's sur-surrebuttal testimony, Exhibit No. ___(SML-7T), the capacity additions included in PSE's proposed alternative adjustment are not expected to produce revenues in the immediate or near future. Recovery of such investments in the revenue requirement for this case through PSE's proposed alternative adjustment will not result in any double recovery to PSE because there are no revenues that can be anticipated to result from such investments during the rate year or in the immediate years beyond the rate year.

Q. What is your reaction to Mr. Russell's objection that PSE's proposal does not include "an offset to account for the change in accumulated depreciation on

[2] Exhibit No. ___(JMR-7T) at page 3, lines 5-6.

existing transmission and distribution plant." [3]

A. The Company's proposal logically does not include an offset for accumulated depreciation on *all* existing transmission and distribution plant. Such an offset would not be appropriate because the Company's proposed adjustment does not include *all* such additional plant.

During the nine months from September 30, 2005 through June 30, 2006 the Company made gross additions to transmission and distribution plant of $158.7 million to the electric plant accounts and $103.7 million to the gas plant accounts. The amount of electric transmission and distribution included in the proposed known and measurable adjustment is $98.8 million ($63.7 million on an average of monthly average basis) for the electric service and $46.6 ($25.3 million on an average of monthly average basis) for the gas service.

The Company did deduct accumulated depreciation through June 30, 2006, on the plant that was included in the Company's proposed adjustment. In addition, the accumulated deferred taxes associated with this plant for the same time period was deducted. Finally, rather than the end of period approach, the Company used the average of monthly averages approach to calculating the rate base additions (the Company used this methodology even though there are no additional revenues associated with this plant and this methodology is generally used to match plant growth with the growth of revenues and expenses during the test

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[3] Exhibit No. ___(JMR-7T) at page 3, lines 6-8.

year). As shown above, this reduces the actual amount of new plant being added to ratebase and that is actually in-service for the customer during the rate year.

Q. Do you agree that PSE's proposed adjustment violates the "matching principle" described in Mr. Russell's surrebuttal testimony?[4]

A. No. Under the matching principle that Commission Staff and other parties have advocated, the concept is that future revenues and expenses will grow or decrease in the same relationship to each other as revenues and expenses in the historical general rate case test period. As Mr. Valdman discusses in his prefiled direct and rebuttal testimony, the Company has not earned its allowed return in the most recent years which is impacting the Company's financial health. *See* Exhibit No. ___(BAV-1CT), pages 12 through 16, and Exhibit No ___(BAV-7CT), pages 24 through 27. This inability for the Company to earn its return, and the impact that it has on the Company in the financial markets, is a strong indication that the historical test year matching principle is not working. This is the reason the Company has identified two transmission and distribution related costing alternatives for the Commission's consideration that will help address regulatory lag. Mr. Russell's comment on page 2, line 17, of his surrebuttal testimony that non-revenue producing and non-expense reducing investments are made every year as part of the normal course of business is just an argument for maintaining the status quo. As Ms. McLain states in her rebuttal testimony and surrebuttal

[4] Exhibit No. ___(JMR-7T) at page 4, lines 7-13.

testimony, if the Company is restricted in its ability to recover its costs, the Company will be forced to scale back planned transmission and distribution system investments.[5]

Q. Do revenues from new customers cover the cost of the investments included in PSE's proposed alternative adjustment?[6]

A. No. Mr. Russell appears to be suggesting that there are sufficient additional revenues from new customers to cover not only their line extensions but also the investments PSE is making that are included in its proposed alternative adjustment. This is incorrect. As stated in Mr. Amen's rebuttal testimony, Exhibit No. ___(RJA-11T), pages 14 and 15, the Company's gas line extension policy applies a "life-of-asset" test to ensure that expected revenues from a customer over time will provide the Company with an adequate rate of return on the associated capital investment. As this is a levelized calculation this does not mean that in the first few years of adding a new customer that the revenues collected from that customer will be adequate to provide the Company an "allowed rate of return" on the investment associated with that customer. The electric line extension policy has a similar type of calculation associated with it and would have under recovery of the return in the early years of the associated plant investment.

[5] *See* Exhibit No. ___(SML-5T) at page 2.
[6] *See* Exhibit No. ___(JMR-7T) at page 5, lines 19-26.

Q. Do you agree with Mr. Russell's claim that "standard regulatory accounting help[s] address earnings impacts during periods of larger capital investments"?[7]

A. I do not agree with Mr. Russell's statement as he applies it to the types of investments included in the Company's proposed alternative adjustment. As I explained in my prefiled direct testimony, Exhibit No. ___(JHS-1T), pages 68 and 69, there are limitations on a company's ability to accrue AFUDC on plant investments. A large portion of the expenditures made on infrastructure accrue very little AFUDC as they are constructed and placed in-service in a very short time period. This is one of the reasons that the AFUDC earnings shown on the table in my rebuttal testimony, page 18 of Exhibit No. ___(JHS-19T), are so much lower than the allowed return.

With respect to the new investment for transmission and distribution as proposed in the Company's alternative, the amount of AFUDC booked on this plant was $2 million for electric and $0.5 million for gas. When compared to the capital dollars that were placed in service this amounts to a 2.67% return on the electric plant (excluding the Novelty Hill Substation[8]) and 1.10% return on the gas plant.

Q. Does that conclude your prefiled sur-surrebuttal testimony?

A. Yes, it does.

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[7] Exhibit No. ___(JMR-7T) at page 6, lines 6-8.

[8] Novelty Hill Substation is excluded from this calculation as this project took several years to complete and the total AFUDC accrued over this time period was $3.4 million.