BEFORE THE WASHINGTON UTILITIES AND TRANSPORTATION COMMISSION

In the Matter of the Proposal by PUGET SOUND POWER & LIGHT COMPANY to Transfer Revenues from PRAM Rates to General Rates.	DOCKET NO. UE-951270
In the Matter of the Application of PUGET SOUND POWER & LIGHT and WASHINGTON NATURAL GAS COMPANY For an Order Authorizing the Merger of WASHINGTON ENERGY COMPANY and WASHINGTON NATURAL GAS COMPANY with and into PUGET SOUND POWER & LIGHT COMPANY, and Authorizing the Issuance of Securities, Assumption of Obligations, Adoption of Tariffs, and Authorizations in Connection Therewith.	DOCKET NO. UE-960195 VOLUME 3 Pages 160 - 288

A hearing in the above matter was held on July 31, 1996, at 1:40 p.m. at 1300 South Evergreen Park Drive Southwest, Olympia, Washington before Commissioners RICHARD HEMSTAD and WILLIAM R. GILLIS and Administrative Law Judges MARJORIE R. SCHAER and JOHN PRUSIA.

Cheryl Macdonald, CSR
Court Reporter

The parties were present as follows:

WASHINGTON UTILITIES AND TRANSPORTATION COMMISSION STAFF, by ROBERT CEDARBAUM, Assistant Attorney General, 1400 South Evergreen Park Drive Southwest, Olympia, Washington 98504.

FOR THE PUBLIC, ROBERT F. MANIFOLD, Assistant Attorney General, 900 Fourth Avenue, Suite 2000, Seattle, Washington 98164.

PUGET SOUND POWER & LIGHT COMPANY, by JAMES M. VAN NOSTRAND, Attorney at Law, 411 - 108th Avenue NE, Bellevue, Washington 98004.

WASHINGTON NATURAL GAS COMPANY, by MATTHEW R. HARRIS, Attorney at Law, 6100 Columbia Center, 701 Fifth Avenue, Seattle, Washington 98104.

NORTHWEST INDUSTRIAL GAS USERS, by PAULA PYRON, Attorney at Law, 101 SW Main, Suite 1100, Portland, Oregon 97204.

INDUSTRIAL CUSTOMERS OF NORTHWEST UTILITIES, by CLYDE H. MACIVER, Attorney at Law, 601 Union Street, 4400 Two Union Square, Seattle, Washington 98101.

WASHINGTON WATER POWER COMPANY, by DAVID MEYER, Attorney at Law, 1200 Washington Trust Building, Spokane, Washington 99204.

PUBLIC POWER COUNCIL, by SHELLY RICHARDSON, Attorney at Law, 1300 SW Fifth Avenue, Suite 2300, Portland, Oregon 97201.

SEATTLE STEAM COMPANY, by FREDERICK O. FREDERICKSON, Attorney at Law, 33rd Floor, 1420 Fifth Avenue, Seattle, Washington 98101.

WASHINGTON PUD ASSOCIATION, by JOEL MERKEL, Attorney at Law, 1910 One Union Square, 600 University Street, Seattle, Washington 98101.

CITY OF SEATTLE, by WILLIAM H. PATTON, Director Utilities Section, 10th Floor Municipal Building, 600 Fourth Avenue, Seattle, Washington 98104.

APPEARANCES (Cont'd.)

PUD NO. 1 OF SNOHOMISH COUNTY, by ERIC E. FREEDMAN, Associate General Counsel, 2320 California Street, Everett, Washington 98201.

IBEW LOCAL 77, by LEWIS ELLSWORTH, Attorney at Law, 27th Floor, One Union Square, 600 University Street, Seattle, Washington 98101.

I N D E X

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P R O C E E D I N G S

JUDGE SCHAER: This hearing will come to order. This is a hearing in docket No. UE-951270, which is a proposal by Puget Sound Power and Light Company seeking approval to transfer revenues from PRAM rates to general rates and docket No. UE-960195 which is the application of Puget Sound Power and Light Company and Washington Natural Gas Company for an order authorizing the merger of Washington Energy Company and Washington Natural Gas Company with and into Puget Sound Power and Light Company.

This hearing was set by a notice of hearing dated July 10, 1996. It's taking place on July 31, 1996 at Olympia, Washington. The hearing is being held before Commissioners Richard Hemstad and William Gillis and administrative law judges Marjorie Schaer and John Prusia. Chairman Sharon Nelson is unable to attend today but will join us tomorrow.

I believe that appearances by counsel are the same as those this morning. If there are any new counsel who have joined us or any parties who have different counsel here, please so indicate now.

The first matter this afternoon then is going to be the testimony of James P. Torgerson. Would you call your witness, please, Mr. Harris.

MR. HARRIS: Joint applicants call as their first witness James Torgerson.

DIRECT EXAMINATION

BY MR. HARRIS:

Q. Mr. Torgerson, would you state your name and business address for the record.

Whereupon,

JAMES TORGERSON,

having been first duly sworn, was called as a witness herein and was examined and testified as follows:

Q. You may proceed answering the question regarding your name and address.

A. My name is James P. Torgerson. My business address is 815 Mercer Street, Seattle, Washington 98111.

JUDGE SCHAER: Sorry, I'm going to interrupt you again, but since the commissioners were not with us this morning and are not familiar with all of the counsel at table, I would like to have you each give a brief appearance so that they will know who you are and whom you are representing so starting with counsel for the company, please.

MR. HARRIS: Matthew Harris for Washington Natural.

MR. VAN NOSTRAND: For Puget Sound Power

and Light Company James M. Van Nostrand.

MR. MEYER: David Meyer for Washington Water Power.

MR. ELLSWORTH: Lewis Ellsworth IBEW Local 77.

MR. MERKEL: Joel Merkel for the Washington PUD Association.

MS. RICHARDSON: Representing Public Power Council, Shelly Richardson.

MR. FREEDMAN: Eric Freedman for Snohomish County PUD.

MR. MACIVER: Clyde H. MacIver for ICNU.

MR. PATTON: William Patton for the city of Seattle.

MR. FREDERICKSON: Frederick O. Frederickson for intervenor Seattle Steam Company.

MS. PYRON: Paula Pyron for the Northwest Industrial Gas Users.

MR. MANIFOLD: Rob Manifold, public counsel.

MR. CEDARBAUM: Rob Cedarbaum for Commission staff.

JUDGE SCHAER: Thank you. Please proceed.

Q. Mr. Torgerson, do you have before you what has previously been marked for identification as

Exhibit T-4?
A. Yes, I do.
Q. Would you identify it, please.
A. Exhibit T-4 is my prefiled direct testimony.
Q. Do you also have before you what's previously been marked for identification as Exhibits 5 through 12?
A. Yes, I do.
Q. Could you please identify each of Exhibits 5 through 12?
A. Yes. Exhibit 5 is the joint proxy that was provided to investor shareholders. Exhibit 6 is a schedule showing debt ratings. Exhibit 7 is information from Standard and Poor's which extends for 11 pages -- or four pages, I'm sorry.
Exhibit 8 is again a schedule of Standard and Poor debt ratings along with historical financial ratios for the companies. Exhibit 9 is Standard and Poor's information from their Credit Week. Exhibit 10 is information from Moody's Investor Services. Exhibit 11 is a schedule showing the capitalization of the companies, and Exhibit 12 are various analyst reports.
MR. HARRIS: Joint applicants would move

for the admission of Exhibits T-4 and Exhibits 5 through 12.

JUDGE SCHAER: Is there any objection? Hearing none those documents are admitted in the record.

(Admitted Exhibits T-4 and 5 - 12.)

MR. HARRIS: Mr. Torgerson is available for cross-examination.

JUDGE SCHAER: At this point I would like to mark for identification two additional documents. The first is a one-page document entitled Response to WUTC Staff Request No. 71. That will be Exhibit 31 for identification. Second is -- states Response to Public Counsel Request No. 110. I've been told that this is just attachment 6 to the response to request No. 110 and that's been marked Exhibit 32 for identification. Please proceed, Mr. Cedarbaum.

(Marked Exhibits 31 and 32.)

MR. CEDARBAUM: Thank you, Your Honor.

CROSS-EXAMINATION

BY MR. CEDARBAUM:

Q. Mr. Torgerson, just to start off looking at what's been marked for identification as Exhibit 31, do you recognize this as your response to staff data request No. 71?

A. Yes, I do.

Q. And is this response is true and correct to the best of your knowledge and belief?

A. Yes, it is.

MR. CEDARBAUM: Your Honor, I would offer Exhibit 31.

JUDGE SCHAER: Any objection? That document is admitted.

(Admitted Exhibit 31).

Q. On page 20 of your testimony starting at line 13 you propose a question about the prospects for future gas general rate relief and you state that Washington Natural would likely file for general rate relief as soon as May 15, 1997. Do you see that testimony?

A. Yes, I do.

Q. And in the following pages from 21 through 24 you state that the ongoing effects of attrition led you to that conclusion despite favorable actions by this Commission and downsizing efforts at Washington Natural. Is that a fair generalization of your testimony?

A. Yes, I would say that's fair. The company has been experiencing or has future commitments that have to be incurred, as I state in the testimony, and also we have had very favorable responses from the Commission regarding certain activities, such as our line extension policy and rate relief.

Q. Going back to the question on page 20 at line 13, is it correct that the -- with the merger and favorable actions of this Commission that we've just been discussing the prospect of general rate relief for gas operations is eliminated at least for the next five years?

A. With the merger we are proposing we would not have any gas rate increases for the next five years. If we look at ourselves on a stand alone basis, which is what we were talking about here --

Q. Mr. Torgerson, I believe your answer to my question was yes. I don't think I called for any additional information in that.

A. Well, the question was going -- under the merger alone we said we would not have to have -- we would not be asking for any rate increases over the next five years. We are proposed to have flat rates.

Q. And is it true that the conclusions that you've reached about rate relief by May of 1997 and the elimination of that need for rate relief under the merger and the Commission's actions is the result of analysis and data that you reviewed?

A. As a result of the merger, and assuming we attain all of the synergy savings, the best practice savings, the power cost savings in the aggregate, and we are prepared to go forward without a rate increase for the gas business, but if the merger is not approved, as I state in the testimony, we would need a rate increase, and we would be filing for that in 1997, and it looks like that rate increase, at least on a very preliminary basis, would be something in the neighborhood of three, four, five percent increase that the gas business would need.

Q. Do you have any studies or data that would support that three or four percent increase?

A. We have an analysis that was done looking at forecasts we had put together, and you have to understand that this is -- it's rough, it's an estimate, but it was using the forecast we had put together, and then looking at ourselves on a stand alone basis making some adjustments for this forecast based on what we believe inflation will be and costs increases from not only O and M but also for capital, and it would indicate that that rate increase is in order, and so we do have some information that would indicate that.

Q. Can you provide us that information as record requisition No. 1?

A. Certainly.

(Record Requisition 1.)

Q. You state on page 21 of your testimony, line 5, that these cost pressures manifest themselves in eroded operating income relative to rate base; is that right?

A. Line 5, it says cause of continuous erosion in operating income relative to rate base, yes.

Q. And operating income as a percent of rate base represents rate of return; is that right?

A. Yes.

Q. Is it the level of this percentage rate of return that indicates the degree of attrition that the company would experience when compared to some benchmark?

A. The rate of return relative to the rate base -- for example, we're currently allowed, under an old order, 9.15, which doesn't reflect the settlement we had last May, but our rate of return would be less than that.

Q. So you're comparing -- the degree of attrition is based upon a comparison with the authorized rate of return?

A. Yes.

Q. And that's essentially what Mr. Story tries to demonstrate in his exhibit JHS-3 which is Exhibit 23? There he shows a comparison of actual rates of return against authorized rate of return?

A. Yes. He shows actual rates of return on a historical basis compared to allowed, and in the case of Washington Natural when you go back far enough into the '91, '92, '93 time frame it really reflected our estimate of what an appropriate return would have been in that time frame because at that point we were on a 16 and a quarter percent return on equity.

Q. So is it correct then that the rate of return on rate base was an important factor in your testimony on the prospect of rate relief arising from attrition?

A. We looked -- the estimate we did --

Q. Just generally speaking.

A. Generally speaking you look at the overall rate of return we're going to be getting.

Q. In staff data request 38 we asked each of the merger applicants for financial forecasts under stand alone merged scenarios for the period 1996 through 2001; is that right?

A. I believe that's right, yes.

MR. CEDARBAUM: Your Honor, I haven't distributed yet but we talked about this prior to going on the record. I have three documents that have been marked as confidential by the companies that raise the issue of sensitive information they don't want their competitors to receive. I think it's critical to the cross-examination to have those documents marked and entered into evidence. I think I can cross-examine on those documents without a closed session, so my proposal, again, would be to go ahead and distribute them to the appropriate parties and then to proceed with cross. I haven't distributed them yet because I don't know who I should distribute them to.

JUDGE SCHAER: And these are the documents, Mr. Harris, that you indicated company believed could be distributed to Commission staff, public counsel, Northwest Industrial Gas Users, Industrial Customers of Northwest Utilities and Seattle Steam but to no other parties?

MR. HARRIS: That's correct, and we would ask that they remain designated confidential and that part of the record be sealed, but we're prepared to go forward with the cross-examination.

JUDGE SCHAER: I'm going to ask you at this time, Mr. Cedarbaum, to distribute copies of those exhibits to the bench and to those identified parties so that we have them in front of us and then we will take up the issue of whether any other party objects to not receiving them and if they do we will make some determination of whether or not they should be provided to those parties.

MR. FREDERICKSON: May I inquire, Your Honor, does that include dissemination to the experts, say, of Seattle Steam?

JUDGE SCHAER: What is your position on that, Mr. Harris?

MR. HARRIS: We would ask at this point that it remain just in counsel's hands.

JUDGE SCHAER: If you would like to speak to that restriction you may do so when we get into argument, sir.

I'm marking as Exhibit C-33 for identification a document states at the top Washington Natural Gas Company Statement of Income. States at the bottom federal -- Fiscal Year 1996 Long-Range Strategic Plan. There's numbers at the bottom that go 3-14, 3-13, 2-8, 2-7, 2-5 and 2-6.

MR. MACIVER: Excuse me, Your Honor. Which document were you referring to just then? C-33?

JUDGE SCHAER: This is C-33 for identification. Marking as C-34 for identification a document which states at the top Puget Sound Power and Light Company Income Statement. It states in the bottom corner Rating Agency Presentation and has numbers of F-8, F-12, F-17, F-21 and F-25 and F-26 and F-30 in pages.

And I am marking as Exhibit C-35 for identification a document entitled Response to Staff Data Request Nos. 96. There's two pages of text followed by several pages figures regarding income statement for NewCo.

And would you state now, Mr. Harris, your reasons why you would like to have distribution of this document limited to the parties you have indicated.

(Marked Exhibits TS-33 - TS-35.)

MR. HARRIS: As we discussed this morning, given the nature, the unusual nature of this proceeding, and the somewhat unusual nature of some of the issues in the proceeding, we're presented with a difficult situation of having to reveal some of our most sensitive proprietary and confidential information. We've attempted to limit the designation of that information as much as possible, and we have designated a certain amount of information confidential. Within that class of information, there is an area that is particularly sensitive to us, and it has to do with our plans for the future. Those plans for the future were they to fall into the hands of our competitors could be devastating for us.

Now, we understand that the Commission has the protective order in place and the protective order offers a certain level of protection for us. That is sufficient for most of our confidential information, but for the confidential information that is competitive-sensitive we are concerned about it getting in anybody's hands other than those parties that absolutely have to have it, and we are very concerned that it not end up in parties' hands where it could cause immediate and irreparable harm to us, so our proposal here is that for that type of information we limit it to parties that have a need to know, and that need to know test must have a balancing aspect to it that considers the harm that the companies will suffer, and because of that the ratepayers, too, if that information is distributed.

Now, the question of whether it should even go to counsel for our competitors is an issue that we discussed this morning, and it's our position that the information is so sensitive, so proprietary and so dangerous, that it not be distributed to counsel for our competitors either, and we suggested to the Commission that it might want to look at the recent Ninth Circuit decision in Brown Bag Software vs. Symantec where that very issue is discussed, and the court reaches the conclusion that we're asking the Commission to reach right now, which is when you have that sort of information you do not distribute it to -- even to counsel for the other side even though it may be important for counsel to the other side to receive that information. It's because of the danger of that information being described.

The court makes a couple of key points. One the risk to consider is the risk posed by disclosure to competitors. The court expressly recognizes that. Two, the risk arises whether counsel is inside counsel or outside counsel, it does not make a difference. Three, it's entirely proper to credit counsel's good faith and integrity, and we do not mean to call into question in any way counsel's good faith and integrity in this case. Nevertheless, once counsel obtains that information the risk of it influencing some future decision exists and once that risk exists there's nothing we can do to undo that.

We also have secondary concerns. This information here, C-33, C-34 and C-35 is, under SEC regulations, inside information. Once this information is revealed to somebody were they to go trade on the stock they would be considered in our view a statutory insider. We are required by law to restrict access in every way possible to this information. Were it inadvertently disclosed beyond the bounds of this room, we would be required under exchange regulations and SEC regulations to make an immediate press release and make the information publicly known no matter what the harm to the companies. We can't take that risk. This is our single biggest concern going into this proceeding, how we protect this sort of information but still allow the parties that need to to engage in full cross-examination. We think we've come to an uneasy balance here but a balance nevertheless by restricting access to the documents and trying to keep the questioning at a level that we can keep the record open.

The last point I want to make is the state legislature in Washington has evidenced a clear intent to protect this sort of information. RCW 4.24.601 contains a finding, an express finding by the legislature, that keeping this type of information confidential, quote, promotes business activity and prevents unfair competition. Well, that's exactly what we're trying to do here is prevent unfair competition by giving our most sensitive data to our competitors.

JUDGE SCHAER: Do you have any questions for Mr. Harris?

Is there any party who would like to speak at this time? Mr. Manifold.

MR. MACIVER: Perhaps a clarification. Are you proposing that -- is it okay for me to give this to my experts?

MR. HARRIS: Yes.

MS. PYRON: That's a clarification that I would like to be able to request as well for effective cross-examination and preparation going forward, and our expert is a party to the confidentiality agreement. It's Don Schoenbeck.

MR. MACIVER: I would join in the request as well that I would want to be able to show this information to members of my client who signed the protective order, which is the expert and the executive director of ICN.

MR. HARRIS: We understand that concern and acknowledge it, but given the sensitive nature of this information it would be our position that it would just stay with counsel.

JUDGE SCHAER: So you're requesting that this document be limited to counsel and experts for Commission staff and public counsel and to counsel only for Northwest Industrial Gas Users, Industrial Customers of Northwest Utilities and Seattle Steam and to no one else.

MR. HARRIS: That's correct, Your Honor.

MR. MACIVER: We would then object to that, Your Honor. I don't think there's any reason to distinguish between a customer who intervenes with its own counsel and a customer who participates through public counsel. We're entitled to the same degree of preparation and the same amount of information as public counsel has to represent his customer clients, as well as an individual customer intervening. This information doesn't do ICNU much good unless its experts can review it, which I am not an expert.

MS. PYRON: Your Honor, I would echo the concerns that have been expressed by Mr. MacIver.

MR. VAN NOSTRAND: On that point, Your Honor, there is a distinction which the Commission itself recognized in the fourth supplemental order as to statutory parties versus nonstatutory parties, and that distinction does exist. Although ICNU is a pure customer group of the company it does stand in a slightly different position with respect to it is not a statutory party and that seems to be a distinction which the Commission finds relevant, at least in the fourth supplemental order.

JUDGE SCHAER: Are there other parties that wish to be heard? Mr. Merkel.

MR. MERKEL: Yes. I have to object for the record. I don't know what's in the documents. Maybe I don't need to know it, but I do represent a group that is made up both of customers and potential competitors. I have signed the confidentiality agreement, and I think the confidentiality agreement addresses this very specifically and seems to me is enough. I don't understand why we have the confidentiality agreement if it doesn't cover this kind of information. So I would object. I think there's no need for it.

JUDGE SCHAER: Ms. Richardson.

MS. RICHARDSON: Yes, Your Honor. Thank you. I don't have an objection at this time, but I would like to comment for the record that of the three offered exhibits, that which is identified as C-35, the response to staff's data request 96 is the subject of one of the Public Power Council's data requests to the company. The response to that request, which we saw a copy of, has been denied and we'll be pursuing that outside of this hearing in the motion practice before Your Honor. I would, however, take the opportunity to mention that in denying the request for that information it was identified as in part rejected as being confidential and proprietary, so I think it's appropriate to raise the concern here although I don't object to its being used in a confidential manner here.

Secondly, I would echo Mr. Merkel's concern that having signed the confidentiality agreement for attorneys to this proceeding, I agree to comply with and be bound by the protective order and I did not take that commitment lightly. I appreciate counsel's comment that they don't assume any of us have taken that lightly, but the distinction here is lost on me as to why we have a confidential agreement if that information is to be subsequently withheld.

JUDGE SCHAER: Mr. Ellsworth.

MR. ELLSWORTH: Yes. We're not competitors. We're a labor organization. The type of data that we're talking about here I don't think relates to us in the same fashion that it's been identified relating to other competitors. I feel having signed the agreement and if the information only comes to my attention and it's not shared with my client, the only issue that's been raised is that the information could possibly be used in some speculative collective bargaining purpose, but that information shouldn't be denied to me at this proceeding.

JUDGE SCHAER: Mr. Merkel, you had something else.

MR. MERKEL: Well, only to note that we submitted data requests requesting copies of answers provided to other parties. We submitted no additional data requests independent of that, and the answer we got back was that no answers were provided because everything was either confidential or we had no need to know. If I was absolutely confident that these were the only three or four documents that we would get that kind of an answer on, I might feel less inclined to object right now, but I think it's part of a larger issue that we'll eventually have to address here, and that's to what extent is the confidential label being used to block access to legitimate requests.

MR. VAN NOSTRAND: Your Honor, without

belaboring the point which Mr. Merkel raised this morning, we elected not to pursue, I think it would be helpful if our remarks were factual, and his request was denied on the 17th of July, the day before the cutoff deadline. We received a request for virtually all responses to data requests. There was no effort whatsoever made by the PUD Association to limit its requests to the scope of its intervention. That was the primary basis upon which we denied his request, and we asked him to resubmit a request which properly reflected the scope of his intervention, so it was not denied on the grounds that Mr. Merkel describes now as being the confidential issue. It was primarily that the request did not reflect the scope of their intervention. We asked them to submit a request which did that.

JUDGE SCHAER: Mr. MacIver.

MR. MACIVER: I would like to make one comment. I'm sorry we're discussing two different issues here because there are two different degrees of people who are available to receive this information of which I represent that type of an intervenor and those that aren't, but then I am addressing the issue of once you get the information can you show it to your expert.

JUDGE SCHAER: Yes.

MR. MACIVER: And Mr. Van Nostrand pointed out in the fourth supplemental order it should only be given to parties on a need to know basis. Well, in the fourth supplemental order the Commission stated that with respect to intervenors with specific or limited interests and to those intervenors who are allowed to intervene on a limited basis the Commission will evaluate the request for confidential information on a need to know basis. ICNU was not granted a limited intervention. We are a customer and purely a customer.

Once the information is given to me as counsel, which they don't object to, fourth supplemental order says counsel who receives access to confidential information may not disclose any confidential information to any person who has not signed the confidentiality agreement. I am not requesting to do that. I am simply saying that as a party for the information to be of any use to me as a party, if I'm entitled to have it I'm entitled to show it to my experts. Otherwise it's not much use to me, so I think we're splitting hairs here perhaps, but I very much object to the notion that as an unlimited intervenor and as a pure customer I am not allowed to use this information in the exact same fashion public counsel can use it and that's show it to my expert.

MR. HARRIS: You've persuaded us. I think we are getting off into an area where we're splitting hairs, and I am concerned that we will get sidetracked with this issue. We are very concerned about this information but just so it doesn't become an issue with the customers we would be willing to not try to draw that fine of a line and say the customers get it, the customers' experts that have that have complied with the nondisclosure agreement can have it. But we can't go any further than that.

JUDGE SCHAER: So we then would no longer have concerns from Mr. MacIver, Ms. Pyron or Mr. Frederickson. Mr. Frederickson, did that satisfy your concerns?

MR. FREDERICKSON: Yes, it did, Your Honor.

JUDGE SCHAER: And we do have remaining concerns from Mr. Merkel and Mr. Ellsworth, and I think I would like to try to focus this discussion just a bit more on the nature of this information without going to the specifics and on the issues involved and on the issues that are within the scope of the intervention of Mr. Ellsworth or Mr. Merkel, because I think that's kind of where the need to know idea should be focused to some extent. Without revealing anything that I shouldn't from looking at these, I believe that you have stated that these are sensitive financial projections.

MR. HARRIS: That's correct, and if I could just add one thing on the need to know test. I agree that half of the test is to what purpose they would put -- to what use they would put this information. I think the other half of it, though, has to be what harm the company could suffer.

JUDGE SCHAER: Well, looking just at the first portion of that on to what purpose this could be put, Mr. Ellsworth, looking at the issues that your client have been allowed to intervene upon, to which of those issues would you believe that the information about the company's financial forecasts would be relevant?

MR. ELLSWORTH: I am not particularly concerned about these three documents. I quite frankly could care less on these three. What I am concerned about is a blanket ruling that will foreclose us arguing about other documents that may come in later in the proceeding that have been marked confidential. As long as we have the right to bring this issue up confidential document by confidential document, I would be satisfied with that.

JUDGE SCHAER: Okay. Then that brings us to you, Mr. Merkel.

MR. MERKEL: I would be -- I think I agree with the prior speaker. I would be willing to at least -- I don't know whether I need to know this information because I don't know what's in it, but I would be willing to put off an issue as to whether I need to have these documents today, as long as it doesn't prejudice my right to ask for them in the future.

JUDGE SCHAER: Thank you. Let's go off the record for just a few moments.

(Discussion off the record.)

JUDGE SCHAER: Let's be back on the record. I want to thank the parties for their cooperation in working together to resolve this. I believe at this point that the parties have agreed that for these particular documents they may be admitted as confidential documents and provided only to the parties previously identified and that will be our ruling. These three documents will be admitted for that purpose. This is not a blanket ruling. As additional confidential documents or confidentiality claims arise during this hearing they will be taken up and parties will be able to speak to them.

In looking at those claims we will be looking at a two-part test, first, to the relevance of those documents to the scope of the intervention granted to the party raising concerns; and secondly, if we find them to be relevant, we will be looking at whether the risk of providing them to the companies would outweigh the benefits to the intervenor or to the Commission through the hearing process of having those provided.

So let's proceed at this time, please. Yes, Mr. Manifold.

MR. MANIFOLD: Your Honor, I just offer for your consideration whether you want to consider some additional designation of the exhibit. The bench -- the Commission started the C designation for confidential exhibits. Seems to me these are getting a new type of confidential designation and it may be useful to have them so designated in the exhibit number as CC or Super C or something.

JUDGE SCHAER: I think that is a good suggestion because it would allow the record center to know that these were to be treated differently even with people who had confidentiality agreements of record. So we'll call these -- these are going to be

TS documents which stands in this setting for top secret.

(Admitted TS-33 - TS-35.)

MS. RICHARDSON: Your Honor?

JUDGE SCHAER: Yes, Ms. Richardson.

MS. RICHARDSON: If I may ask a clarifying question, thank you. With respect to materials that are admitted in this manner as designated TS documents, insofar as those same materials have previously been the subject of discovery requests and that there may be potential disputes with respect to those discovery requests, is it accurate to say that parties making such discovery requests are not precluded from following through, then, with those discovery matters?

JUDGE SCHAER: That would be my intention, that all we have determined now is that these will be admitted into the hearing record and may be questioned upon at this time, but that parties who are seeking information may seek to compel responses to data requests or other discovery and may pursue that outside of the hearing including -- we have not made any final ruling on these documents of that nature. We've told you what the standards would be that we would expect to have addressed.

MS. RICHARDSON: Very good. Thank you, Your Honor.

MR. CEDARBAUM: Is my understanding these documents then are in the record?

JUDGE SCHAER: I did go ahead and admit them, Mr. Cedarbaum.

MR. CEDARBAUM: I will have a witness identify them now.

JUDGE SCHAER: I think you should still go through and have them identified to the extent that you can for the record in addition to what I've done with headings and numbers present.

Q. Mr. Torgerson, referring to Exhibit TS-33, do you recognize this document as six pages from the company's response to staff data request No. 38 which had asked for each merger applicant's financial forecasts under stand alone and merger scenarios for the 1996 to 2001 period?

A. Yes. These are forecast information.

Q. And for your reference, as I ask you questions later about this document, I will be using the page numbers that are handwritten on the upper right-hand corner.

A. Okay.

Q. Do you recognize what's been marked for identification and admitted as Exhibit TS-34, a seven-page document also selected pages from the company's response to staff data request 38 which were documents that were part of the company's rating agency presentation on the merger?

A. Yes. These are part of the Puget Power's portion of the rating agency forecast.

Q. And referring you to Exhibit TS-35, which has also been admitted, do you recognize this document as selected pages of staff data request -- your response to staff data request No. 96 in which we asked you to recast certain portions of staff data request 38, making different assumptions and then also asked you to disaggregate the information between gas and electric operations?

A. Yes. This is, I believe, a partial response to that data request.

Q. And again as we get into these documents I will be referring to the handwritten numbers on the upper right-hand corner of these pages.

A. Okay.

Q. Looking at Exhibit TS-33, is it correct that these pages were part of -- excuse me, just looking at page No. 1 which is entitled Washington Natural Gas Company Statement of Income. This was part of that company's long-range strategic business plan dated October 1995; is that right?

A. Yes. It's part of the long-range strategic plan.

Q. And would you accept that October '95 date subject to your check?

A. Yes, subject to check.

Q. And is it true that this is a comprehensive picture of the revenues, expenses, operating income, net income, rate of return on rate base and equity return on rate base for Washington Natural for the period 1995 through the year 2000 on a stand alone basis?

A. It is an estimate of that, and I need to qualify what's in here a little bit, because you have to realize this was a forecast that was put together, and it was done in part -- it was entirely for our strategic plan. It has very aggressive assumptions on certain aspects of the forecast, particularly savings related to O and M, and it had very low inflation rates. As a matter of fact, we assumed significant productivity in our O and M costs and that's why you see O and M, the utility operating expense only going up slightly over this entire forecast period. So this was relying on our aggressive assumptions and we were going to maintain our costs and keep them very low.

Now, I also have to tell you that we're -- in this year, we view ourselves as probably one of the best companies in the country at keeping our O and M costs down, and if you look at a study that was done by NIGAS/NICOR we're in the top five, or at least we project ourselves to be. We're finding it very difficult to earn close to our rate of return in this instance.

MR. CEDARBAUM: Your Honor, my question was whether this was a forecast for the year 1995 to the year 2000 for Washington Natural on a stand alone basis and I think the answer was yes, and I don't have any problem with Mr. Torgerson explaining why this is an estimate or why it is not but I think he's gone well beyond that type of information.

JUDGE SCHAER: Would you please listen to the question asked, Mr. Torgerson.

THE WITNESS: Certainly.

JUDGE SCHAER: And try to stay within that. Thank you, sir.

THE WITNESS: Certainly.

Q. Now, it was just your testimony that there's certain assumptions made in this document that if changed would impact the results?

A. Pardon me? Can you repeat the question.

Q. You indicated that there was certain assumptions that this document makes that were overly aggressive I think is what your testimony was?

A. I said they were aggressive assumptions, and you have to look at the reason for this.

Q. Again, the answer is yes?

MR. HARRIS: Your Honor, I would object and ask that the witness be allowed to finish his answer before he's interrupted.

JUDGE SCHAER: Mr. Harris, I'm going to ask the witness just to answer the question asked because I think Mr. Cedarbaum is trying to ask some basic foundation to get to a substantive question, and we're getting kind of lost getting there. I would like to proceed if we could. Overruled.

Q. Let me ask you, Mr. Torgerson, as the next record requisition in order to provide us with a list of those aggressive assumptions and the impact they each make on what's been marked as -- what's been admitted as Exhibit TS-33.

(Record Requisition 2.)

A. We can do that. Keep in mind that the forecast that we provided you does have the assumptions that went along with it, and we would be happy to tell you which ones were in our opinion aggressive.

Q. Now, the effects of the factors that contributed to the attrition that you discuss in your testimony and favorable actions from this Commission that you also discuss today would be reflected in the annual income statements in Exhibit TS-33; is that right?

A. The effects of the attrition, the capital spending required that I mention in my testimony, the benefits derived from the investments in technology, which I mention in the testimony, are reflected in here.

Q. And the impact of the Commission's actions with respect to Washington Natural over the last -- favorable actions that you've characterized by the Commission?

A. Yes. The rate increase we received last May and the one previous to that and the line extension policy, those are reflected.

Q. Looking at the last two lines of this page, that data is for rates of return on rate base and equity returns on rate base; is that right?

A. Yes, it is.

Q. Is it true that all the returns except for

1995 exceed Washington Natural's authorized return, the latest authorized returns both on equity and overall?

A. Yes. The numbers here do reflect that. Again, I have to state that some of the assumptions were aggressive.

Q. Is it true that the revenues for the forecast are estimated by applying the rates from Washington Natural's 1995 rate order to projected volumes and that there's no anticipated general rate case for the forecast period?

A. That is correct.

Q. Turning to page 2, as we have numbered them of this exhibit, this net income graph depicts an increasing trend due to profitable growth and costs control; is that right?

A. Yes, it says WNG's income is expected to increase due to profitable growth and cost control.

Q. Also, it indicates that the forecast might be conservative as no income from energy marketing strategies has been included; is that right?

A. Yes, it says that related to that one item.

Q. Where in your testimony, if you did, did you discuss energy marketing strategies?

A. We did not discuss it in my testimony.

Q. Can you describe what those are in general?

A. The one that I recall that we were talking about was -- were sales to perhaps -- the prospect of having city gate sales or sales to industrial customers inside our city gate which we had talked about a number of times and talked to the staff about it, I believe. We have not filed anything to do that at this point.

Q. Do you have any reason why there was no discussion in your testimony of energy marketing strategies?

A. Saw no need to put it in there at this point.

Q. Turning to page 3 of the exhibit, this depicts the consolidated statement of income for Washington Energy Company; is that right?

A. Yes, on a projected basis.

Q. And similar to Washington Natural Gas there's an increasing trend in operating income, net income and earnings per share; is that right?

A. Yes, and I have the same reservations because it is a consolidated basis.

Q. And the information shown on page 3 is graphically depicted on page 4?

A. Yes, it is.

Q. Turning to page 5 of the exhibit, is it true that this page contains information about cost and benefits of re-engineering proposals under a worst case and a best case scenario?

A. Yes. This is a summary of some estimates related to re-engineering relying on investing certain dollars and looking at what could happen related to capital costs and O and M on a worst case and a best case basis.

Q. And re-engineering proposals were also not discussed in your testimony; is that right?

A. Re-engineering specifically relating to Washington Natural Gas was not because when we merge we're looking at the benefits we were going to derive by merging, and re-engineering then really isn't a part of the merger in one sense; in another it is because those are what you would look at as best practices.

Q. Can you just define specifically what is meant by re-engineering benefits or re-engineering?

A. Re-engineering in this context were the activities we were performing at Washington Natural Gas pretty much up until the time of the merger. We had a large team of people that were working on ways to reduce costs, and it's -- re-engineering is the idea of looking at the best way to operate or to perform the activities of a company, with the idea that it's going to improve your service, which is one of our criteria. We wanted to do that and make sure we had improved our service. Washington Natural Gas I think has, and it's also going to be carried forward to the Puget Sound Energy. That is one of our goals is to improve service, so that's how I relate re-engineering to best practices.

Also, what we wanted to do was find ways to reduce our costs, and again, this is something we wanted to make sure happened upon our merger, that through best practices we would be able to reduce our costs and improve our service to our customers.

Q. What we're talking about here is a stand alone forecast; is that correct?

A. Yes. In this case this is stand alone.

Q. And you indicated that the re-engineering actions of Washington Natural Gas were taking place prior to consideration of the merger?

A. We were in the process of it. I said we had teams of people working on it up until about the time of the merger. We did some things. A lot of it was going to occur during fiscal '96 and beyond. We were going to need to make investments in technology.

Many of those we just have not done simply because we are now involved in the merger process, so the benefits we were to be expecting from re-engineering really -- we haven't had a chance to have them occur in total.

Q. I'm still on page 5 of this exhibit. The description at the top states that most of the costs to achieve re-engineering benefits have been included in the forecast with some modest portion of the anticipated savings. Do you see that?

A. Yes, I do.

Q. When this document discusses modest portion of the anticipated savings, does that mean the level of benefits that would occur under the worst case scenario as shown on this page? In other words, does modest portion indicate worst case or best case?

A. To be honest, I don't recall which one we put in there.

Q. Why don't you provide that then as record requisition No. 3.

(Record Requisition 3.)

MR. MANIFOLD: Your Honor, if I may interrupt, perhaps this would be an appropriate time to take up the matter of who gets record requisitions. It would have to come up sometime. We would like copies to the responses to all the record requisitions including these that relate to the TS exhibits. And I suspect other people may have things to say about that.

MR. HARRIS: I think, Your Honor, it would be our proposal that we formulate the response and then determine at that time whether we can distribute it more broadly or not, depending on what's included in the response.

JUDGE SCHAER: When you say that, are you talking about -- when you say more broadly are you saying that you might have a situation where you would object to giving responses to public counsel or are you thinking of other parties at this point?

MR. HARRIS: Just the distinctions that we drew with respect to these TS exhibits.

JUDGE SCHAER: Okay. I think that what we should do, Mr. Manifold, is that parties who wish to request copies of responses continue to do so off the record in standard practice. Parties who request responses and don't receive them will have the same opportunities they have when they request data requests and don't receive them to pursue what motions to compel they think are appropriate, but I don't think that there's any kind of a blanket ruling that I could make at this point. Just glancing at the three requests that have been made, it appears to me that it might be that some would be in, some would be out, and I think the company's suggested way of proceeding makes sense.

MR. MANIFOLD: It solves my problem.

JUDGE SCHAER: Thank you.

Q. Turning to the last page of the exhibit. One of the key assumptions shown at the bottom is that the forecast does not include any income from incentive ratemaking or wholesale energy services; is that right?

A. Yes, that is correct.

Q. Would those areas be areas which would provide a better opportunity for the company to increase its rate of return?

A. They could, depending on the structure of -- if you have an incentive ratemaking proposal, usually it works in both directions. It can give you an incentive to earn more or if you don't perform you earn a little less, and the same with wholesale energy services. Depending on how it's structured you may make money or you may lose money on it, depending again on how it's structured, so there is a potential for that, certainly.

Q. Looking at the last line of data on this page, it shows that except for 1995 the levels of return on common stockholders' equity for consolidated Washington Energy Company are higher than the equity return on rate base for Washington Natural Gas which appears on page 1 of this exhibit; is that right?
A. Yes, that's true.
Q. Can you explain why?
A. Well, the easy answer is that the equity for Washington Energy Company is considerably less than that for Washington Natural Gas because we took significant write-offs in Washington Energy Company over the last two years and close to a $100 million, so the equity level is a lot less, and when you do a return on equity based on the equity level at the parent company it would obviously improve the return. So we wrote down the investment we had in Cabot Oil and Gas Corporation for our coal and railroad activities, and also a number of other things in the past two years, so that is why the return would be higher. Also we do have some minor income from Washington Energy Services Company and you can see we had forecasted losses in other areas.
Q. Washington Energy Services is the subsidiary of Washington Energy Company?

A. Washington Energy Services is a subsidiary, yes.

Q. Let's switch to Exhibit T-34, and I believe you confirmed before that this is a set of documents from Puget's presentation to rating agencies; is that right?

A. Yes. It was a combined presentation. This is the Puget Power portion.

Q. When was this document prepared?

A. I believe this one would have been prepared in the -- we went to visit the rating agencies at the end of January of '96 so sometime prior to that. Probably in the fall or early winter of this year.

Q. End of '95, beginning of '96?

A. Yes.

Q. Can you tell me -- you said then that you went to the rating -- rating agency presentation was the end of January?

A. Yes.

Q. And where did that occur?

A. In New York. Representatives from both companies, Bill Vititoe, myself, Rich Sonstelie and Bill Weaver and I think one or two others went, and we sat down and visited with the rating agencies, as is normal on an annual basis, and presented this to them.

Q. Which rating agencies was the presentation made to?
A. We visited with Standard and Poor's and with Moody's.
Q. Do you recall who exactly from those two organizations?
A. At Standard and Poor's it was Cheryl Ricker and Michael Call. At Moody's it was Alexandria Parker, Kevin Rose, and I think one or two others which I don't recall their names.
Q. And the presentation was to present to S and P and Moody's information concerning the merger that had been announced prior to that; is that right?
A. Well, we had talked to them before about it. This was a formal, more formal presentation. We provided them the rating agency book in advance. Then we went and sat down with them and reviewed what was in there. Talked about the assumptions that we made. Told them which ones we felt were aggressive, what we felt were conservative, and then we have a very good question and answer session. We talked about the industry. We talked about the merger, what benefits we thought we would derive from the merger, how it was going to be in the best interests of shareholders and customers, our employees, and we usually have a

discussion that goes several hours with each rating agency.

Q. And what was your role?

A. I was one of the presenters along with the other parties. It's really more of a discussion where we go through certain of the pages and talk about key points.

Q. And was the objective of the presentation to present to the rating agencies a favorable financial picture of the merger?

A. We obviously want to make a favorable impression. The objective was to provide them the information we had today, at that point in time, what we thought the impacts at that point in time would be from the merger, and again, laying out the assumptions and what we thought we could do as a merged entity.

Q. In looking at Exhibit TS-34, the first page, is it true that this is a page -- is a multi-year income statement of Puget with actuals from 1992 to 1995 and projections for 1996 to the year 2001; is that right?

A. Not entirely. The actuals were 1992 to 1994. '95 was an estimate because it was taking 12 months ended September 30, '95, so Puget hadn't finalized their calendar year yet and the balance are projects.

Q. And page 1 is a stand alone portrayal of Puget; is that right?

A. Yes, it is.

Q. In the projections columns of page 1, is it correct that in the year 1997 this income statement assumes a general rate increase?

A. Yes, it does. It had I believe about a $74 million rate increase.

Q. Can you state what rate of return on equity that assumes?

A. I believe it was either 11 and a half or 12 percent.

Q. Now, unlike the Washington Natural statement of income that was in Exhibit TS-33, Puget's income statement doesn't include rate of return on rate base and equity return on rate base; is that right?

A. That's correct.

Q. And is it correct that in staff data request 38 we asked that rate base and rate of return be provided and then we followed that up with a data request 96 in which we asked for equity rate of return on rate base as well. Do you recall that?

A. I'm not sure. I've seen data requests, yes.

Q. In your response to data request No. 96 you responded that the data have not been prepared and you're aware of no additional information that would be responsive to the request?

A. That's correct.

Q. Do you know why Washington Natural Gas was able to include rate of return on rate base and equity return on rate base in its information but Puget was not?

A. It's not in here. Washington Natural in our modeling, we have the capability to determine what the rate of return is. I believe in Puget's return -- Puget's forecast -- they targeted a rate of return, so that's what I'm saying. It was targeted at 11 and a half or 12, and I'm sorry, I don't remember which it was, but they targeted a rate of return and backed into what the revenues would have to be in order to reach that targeted rate of return, so Puget has the capability. It wasn't printed up here, and I think in our forecasts that we provided you for the rating agencies it has that assumption in there as to what the rate of return was in the entire rating agency package. I believe it's there.

Q. Turning to page 2 of Exhibit TS-34. This page contains selected financial ratios for Puget derived from the page 1 income statement; is that right?

A. Page 4, did you say?

JUDGE SCHAER: Page 2.

A. Yes, it does.

Q. Before we move on to page 2, let me back up, and just so I'm clear about getting the equity return on rate base and rate of return on rate base for Puget, you indicated that you thought the information was there in the material we've already seen?

A. At least the rate of return. I believe it is there. Equity return.

Q. I want to make as record requisition No. 4 that you provide us -- that you recast or take page 1 of Exhibit TS-34 and add to it rate of return on rate base and equity return on rate base for Puget.

A. I believe it's there.

Q. If it's a matter of just pointing us in the right direction as to where the information is that we already have you can say that but we're having difficulty getting that.

A. Certainly.

(Record Requisition 4.)

Q. Again, turning to page 2. Is it correct that the returns that are shown here are not derived from net operating income relative to rate base but from net income including nonutility income relative to total common equity?

A. Are you referring to the return on average common equity?

Q. Yes.

A. Yes. That is done for the corporation and it's simply -- I believe it's the calculation of average net income or average stockholders' equity, net average divided by average stockholder equity.

Q. Turning to page 3. Is it true that these are Washington Natural Gas Company stand alone income statements as presented to the rating agencies and they differ from Exhibit TS-33 because actual data from '92 to '95 is used and the forecast is extended to the year 2001?

A. Yes. In Exhibit TS-33 that was done earlier for the strategic plan and we updated at the time the rating agency was -- presentation was done.

Q. Turning to page 4, which contains selected financial ratios for Washington Energy Company. It appears from this page that the returns on average common stock from 1996 through 2000 are higher when compared to the return on equity from the Exhibit TS-33. Do you see that?

A. Yes.

Q. Can you explain why that is?

A. Yes. This was what I was talking about before. In the first one, we didn't have the write-offs in fiscal '95 in at that point. We had the write-offs from the previous year in fiscal '94 when we sold or merged our coal operation -- not coal -- merged oil and gas operation. Then in fiscal '95 we took additional write-downs of coal and the oil and gas, which further reduced the equity, so that's why these returns would even be higher. We took expenses I think in the neighborhood of almost $50 million at the end of fiscal '95, so we wouldn't have had it at the time the strategic plan was put together.

Q. Is it true that Washington Energy Company and Puget stand alone financial ratios are expected to improve under the merger as shown on these documents?

A. In these documents?

Q. Yes.

A. Have to look at the one for NewCo, but I believe the ratios for Washington Natural certainly do improve when you're talking about coverage ratios and so forth, and for Puget Power, I believe that they actually are about the same, maybe a little bit better in the out years but we would have to look at the numbers and compare them.

Q. Turning to page 5 of this exhibit, it contains certain general assumptions for NewCo's merged financial forecasts; is that right?

A. Yes, they're general assumptions for NewCo.

Q. And page 6 contains the actual and projected income statement for NewCo; is that right?

A. Yes, this is the -- well, projected, and the actual would actually be sort of a proforma where we combine the two companies.

Q. And I guess for the record, since the testimony was filed NewCo has a real name; is that right?

A. Right. Puget Sound Energy.

Q. For purposes of -- since the testimony is framed as NewCo I will continue to refer to Puget Sound Energy as NewCo.

Turning back to page 5, is it correct that the projected NewCo income statements assume no rate increases or decreases for gas or electric customers as one of the general assumptions?

A. Yes. As you look at the income statement you see where we took out on page 6, we took the projections for the Puget Power increase. Again, keep in mind what I said before about assumptions. This is where it does make a difference because in the forecast for Puget there was an assumption of a certain increase in revenues and it's in the forecast, so you can see that I don't want to start talking about the numbers.

That was probably -- it was somewhat aggressive. It was more than what we were seeing for load growth, so you could say that there was probably assumed in that forecast on a stand alone basis that there was some rate relief over and above what would be stand alone, so you have to dig in some of the details, but there is something there that's in excess of what we would see just on normal load growth.

Q. Another of the general assumptions here is the inclusion of Mr. Flaherty-estimated merger savings; is that right?

A. Yes. Those are the synergy savings that were developed with the Deloitte and Touche and some of our own people who were involved.

Q. That assumption indicates an amount of savings anticipated between 1997 and the year 2001. Do you see that?

A. The line entitled Synergy Savings Net of

Amortization.

Q. Do you know how those savings for the 1997 to 2001 period are taken into account in the income statement?

A. My understanding is that they're simply subtracted from other O and M.

Q. In using Mr. Flaherty's synergy savings, did you check with his -- that his estimating and projection assumptions were consistent with the assumptions you made or that were made in these financial forecasts?

A. No. They were done fairly independently. We didn't necessarily try to make them exactly the same.

Q. The third general assumption included in the forecast are additional savings during the forecasted period for best practices in the operation of NewCo; is that right?

A. Yes. The line that says best practices, right.

Q. Just backing up a bit here, in staff data request No. 45 we asked if the companies had attempted to quantify any of the savings that would potentially rise from best practices and the response that we got was that the company had not; is that correct?

A. That is correct.
Q. We also asked on that same data request if the company had considered the potential impacts of technology changes on savings attributed to best practices, and again the response was no; is that right?
A. Yes. That's the correct response.
Q. Now, is it correct that staff data request 45 was submitted to the companies in May of 1996? Would you accept that subject to check?
A. Sure.
Q. Would you also accept subject to check that staff data request 65 we asked for a timetable for the review and quantification of best practice savings and the company's response was that NewCo doesn't have a timetable for review of and quantification of savings from potential best practices. Would you accept that as your response?
A. Subject to check, yes, that is true.
Q. And would you also accept that staff data request 65 was submitted in May of '96?
A. Subject to check, sure.
Q. Now, there's a specific amount shown on page 5 of Exhibit TS-34 for best practices as submitted to the rating agencies. But staff was told

that no estimate had been made. Can you reconcile those two?

A. We have an estimate which is shown in here. I think we interpreted the staff request as to the detail and how it came about, which it really hasn't been developed. I mean, we provided in putting this merger forecast together what we thought we could do without any detail. I mean, the companies looked at their -- few people -- you have to remember the time frame that the best practices were put together it was back when the merger negotiations were going on, back in August, September of '95, and we had very few people working on it at this point in time, and they put together an estimate looking at overall operations what the management thought we could do, and that's where we came up with that number.

So it was very much in the aggregate, and we haven't done anything since then to try to come up with programs or estimates to detail that out. That's one of the things our task forces are working on right now and they're still working on it.

Q. So when we asked you in May of '96 if the companies had attempted to quantify best practices you didn't understand that to mean provide us with the number that's in Exhibit TS-34?

A. Other than I thought we had in this by providing you with a forecast from the rating agencies it's in there.

Q. Are there any work papers or analysis that you know of or that the company has to support the figure for best practices shown in the exhibit?

A. No. I mean, it was developed, as I said, and there really aren't any work papers for that.

Q. Did the rating agencies during your presentation inquire about those savings?

A. Sure. That was one of the things we had a long discussion on was the best practices, power cost, synergy savings, and we told them, those are management's best guess, best estimate, of what we might be able to do.

Q. And you presented that information to them to rely upon in their review of the merger?

A. Well, they're not really reviewing the merger. They will have to come up with a rating for the company once we are merged, and we will go back and talk to them again before they even do that.

Q. You provided that information as to be useful to them?

A. Certainly.

Q. Do you know how that amount for best

practices was reflected in the forecast?

A. Again, it was treated the same way as the synergy savings. It was, I believe, just subtracted from the O and M numbers.

Q. Looking down at the next assumption on page 5 of Exhibit TS-34, it indicates an amount for savings which will result from achieving power cost stretch goals; is that right?

A. Yes.

Q. Can you explain what those -- what power cost stretch goals are as it was explained to the rating agencies?

A. As we explained it to them it was again another area where we thought that savings could be potentially developed.

Q. And are there any work papers underlying that figure?

A. Not that I am aware of.

Q. Are those power cost stretch goals savings amounts that Puget wouldn't have to strive for absent the merger?

A. I think Puget recognizes very well this industry situation and that their power costs, at least on their PURPA contracts, are probably out of the market today and that they need to find ways to reduce that if we're merging or not. So I guess the answer is yes there is -- they would have a goal of achieving some power costs savings as stretch goals regardless of the merger, I would believe, but not being an officer of Puget it's hard to answer for them.

Q. Do you know what type of power contracts those savings are connected with? Are we talking about PURPA contracts, cogen contracts?

A. The idea was that they looked at the PURPA contracts primarily and said they thought there could be some percentage savings there.

Q. Just going back to the best practices figure, is there anything about best practices that either Puget or Washington Natural could not do -- let me say it this way. Can't Puget -- shouldn't Puget and Washington Natural pursue best practices absent the merger?

A. Oh, of course. Both of the companies would pursue best practices. This best practice, though, is mainly related to things we thought we could do beyond the -- after the merger is done and it helps us with developing -- beyond the synergies but things that we could do and probably not necessarily get it all by ourselves.

There are other things. A good example of a best practice might be if you can operate a joint crew. Now, that's definitely not a synergy saving, and it's also something we don't do stand alone, but if we could operate a crew that had line men and a fitter, and maybe one helper as opposed to a helper for each one, that's the idea we're talking about about best practices. Those things we couldn't do stand alone but the merger would certainly allow us to do those things. Those are the type of things. I agree with you we would be pursuing best practices if we were separate companies, and I think our re-engineering was an example of that. Both companies have done re-engineering.

Q. Can you tell me how the power cost stretch savings were accounted for in the forecast? Is that similar to your prior answers on the best practices and --

A. Yes.

MR. CEDARBAUM: Your Honor, as you know, I have a lot of cross for Mr. Torgerson, and I don't know when you want to take a break.

JUDGE SCHAER: Well, I was going to wait until you were done with this exhibit and I was going to ask you to look for a good breaking point. If this is a good breaking point we could also take it right now, Mr. Cedarbaum.

MR. CEDARBAUM: I have more questions on this exhibit than five minutes.

JUDGE SCHAER: Then why don't we take our afternoon recess now and be back at 20 minutes after 3. We're off the record.

(Recess.)

JUDGE SCHAER: Let's be back on the record after our afternoon recess. Would you like to continue, Mr. Cedarbaum.

MR. CEDARBAUM: I think so.

Q. Mr. Torgerson, before I ask some more questions about pages in Exhibit No. TS-34, is it correct that this document which was presented to the rating agency -- in the rating agency presentation was presented to provide information to the rating agencies for them to initially assess the credit quality of NewCo; is that right?

A. That was our intention was to give them an idea where we were, not to necessarily come up with a rating at that point because that wasn't the intention, but it was to give them an update of how things looked and how we perceived it to look.

Q. Looking at page 6 of the TS-34, the yearly figures for each of the assumptions that are shown on page 5 are down at the bottom of page 6; is that right?

A. Yes.

Q. And focusing on the projected years -- this is on the right-hand side of the page -- is it true that the forecast shows a consistent annual increase in operating income in earnings per share from 1996 through the year 2001 without any general rate increase reflected?

A. Yes, but one thing you got to remember on this, and it's fairly important, is that this was not done on a Commission basis. None of these forecasts were. They were done on a financial or GAP basis, so they reflect like 30-year weather rather than the 20 years, so that's one of the things I was talking about when I said the assumptions were somewhat aggressive.

Q. Can the information shown in Exhibit TS-34, and I guess TS-35, be recast on a Commission stated basis?

A. That I'm not certain. I know the estimate we did when I was talking about the forecast, which showed rate relief for the gas side, was an attempt at doing that, and I would be happy to provide it on the electric side. I'm just not sure they have the capability.

MR. CEDARBAUM: Let me make that record requisition 5 for you to recast Exhibits TS-33 and TS-34 on a Commission stated basis, and I understand that there may be difficulties in that, and you can explain what those difficulties are, but if you can make the best stab you can at that.

(Record Requisition 5.)

A. We'll look at it. As I said, I don't know that Puget has the capability to do that, and we would have to estimate it ourselves pretty broadly.

Q. If there are problems just contact us and we can try to work them out.

A. Okay.

Q. And if you could include in that information the return on rate base and return on equity that the Puget pages did not have but that Washington Natural's pages did, I think we talked about that earlier.

A. Again, to the extent we have the capability we'll do that. I'm just not certain that Puget does.

Q. I would like to discuss some items that are not reflected in the forecasted income statements but that have occurred after or pending the time -- after the time that these were prepared and are pending.

And to discuss what impact on operating income and operating return for NewCo's merged data and the first one is with respect to schedule 48 that Puget filed. Are you generally familiar with that filing?

A. Generally, yes.

Q. Is it correct that schedule 48 will negatively affect operating income and equity return during the forecast period assuming that all eligible customers sign up for it?

A. Assuming all eligible customers sign up there would be a reduction in revenues without any mitigation, but yes, there would be a reduction in revenues that should have an impact on the rate of return.

Q. A downward impact?

A. Yes. Again, without any mitigation, yeah.

Q. And the impact of schedule 48 is not included in Exhibit TS-34; is that right?

A. That's correct.

Q. So the rating agencies during the presentation were not made aware of schedule 48?

A. No. We hadn't even completed at that point.

Q. Since schedule 48 was filed, have the companies asked the rating agencies to reassess the credit quality for NewCo with schedule 48 in mind?

A. No. We haven't had any need to really at this point because they haven't come up with any determination on the credit quality or rating for Puget Sound Energy yet and they won't until there's an order.

Q. So the rating agencies have not -- since the presentation in January of '96 there has been no later presentation to update them with respect to schedule 48?

A. Not to my knowledge but we did -- some of the people had a meeting with a couple people from Standard and Poor's about a week ago. I was not in town. I wasn't available for the meeting. I assume they probably discussed it but I can't say that for certain. I wasn't there.

Q. The prospectus in your Exhibit 5, has that been reissued at all or revised to account for schedule 48?

A. No.

Q. Puget also has special contracts that were recently approved by the Commission with Georgia-Pacific and Bellingham Cold Storage; is that right?

A. That's my understanding, yes.

Q. And the impact of those special contracts is also a downward impact on operating income and equity return?
A. That would be my understanding without any mitigation, yes.
Q. And those impacts are not reflected in Exhibit TS-34?
A. That's correct.
Q. With respect to whether or not the rating agencies were updated concerning those two special contracts, and whether the prospectus in your Exhibit 5 was updated with respect to the special contracts, are your answers the same as they were with respect to schedule 48?
A. Yes.
Q. Another special contract that Puget has is with ARCO; is that right?
A. Yes.
Q. And that contract is reflected in Exhibit TS-34?
A. That's my understanding that it is in there.
Q. As record requisition No. 6, could you please provide a rerun of the forecast assuming that ARCO were to stay at its tariff rates as opposed to

the contract rates?
A. I assume we have people who can run through that.
(Record Requistion 6.)
Q. Puget also has pending before the Commission special contract with Intel Corporation; is that right?
A. Yes.
Q. Is it true that that contract would have a positive impact on earnings?
A. That one I don't know. I'm sorry, I can't answer that. I take that back. Since that would be new business I guess it would have to.
Q. And the impact on operating income and equity return under the Intel service would be even enhanced if Intel was served under the applicable tariff rate; is that right?
A. That I don't know. I mean, I haven't done any studies to say that.
Q. If the tariff rate is higher than the contract rate?
A. If the tariff rate is higher than the contract rate it would improve the operating income over what was in the contract, yes.
Q. Is it also correct that the impact of the

one percent rate increases under the rate stability plan would further increase operating income and equity return during the forecasted period from what's shown in the exhibit?

A. Somewhat. I think I mentioned before that there is a -- in the forecast, the way it was done it projected higher -- again, these numbers are in the strategic plan and forecast -- higher revenues on a percentage basis than the load growth would normally indicate, and so I think there is a component that's somewhat over -- overestimating revenues in the base forecast and that the one percent wasn't specifically put in there but there's a component that's probably maybe a half a percent that's more than what a base forecast would indicate, so to some extent that one percent is in there a little bit but not entirely.

Q. And to the extent it is not then if the remaining portion of it was then included that would have a positive impact on the forecast?

A. Yeah. If the one percent is greater than what that over estimation is, yeah.

Q. Is it also correct that activity such as joint meter reading and unity trenching would have a positive impact on forecast?

A. Not necessarily. We had -- Washington

Natural Gas had budgeted those activities, and those were put in Washington Natural Gas's forecast, the joint meter reading, the joint data center, the unity trench, to the extent we do that. We had included some of that in our forecast, or Washington Natural Gas. The Puget side of the forecast, I don't believe those were necessarily -- were budgeted, were put --

Q. And so to the extent they were not budgeted in there, if they were to be included that would have a positive impact on the forecast?

A. Yeah. To the extent they're positive. I mean, we're assuming that those activities would be positive. The joint meter reading, the estimates I saw early would indicate it should be and that's what we budgeted but it's not -- there aren't huge dollars but there are some savings.

Q. Are you familiar with the company's bonded conservation issue?

A. Somewhat.

Q. As that revenue requirement declines with respect to bonded conservation, that will also have a positive impact on the forecast?

A. My understanding of the way it's in the forecast is that the tariff rate that the customers pays in, they're in full, and that the conservation --

the money that comes in and is funded to the conservation trust declines, so over time I think there is a little bit more of an income impact, and I think that is in this forecast, at least I thought it was.

Q. You thought but you're not sure?

A. No, I'm not certain because of the way the revenues were developed for the Puget side because that was targeted at a certain rate of return.

Q. We had asked a data request or one of the parties had asked a data request, and I don't have the number off the top of my head, but the answer indicated that the bonded conservation revenue was not reflected in the forecast. Would you accept that subject to your check?

A. Subject to check. I will have to look at that.

Q. And we'll try to get you the data request number.

A. Certainly.

Q. The NewCo financial forecast that's shown in Exhibit TS-34 is a combined picture of gas and electric operations; is that right?

A. Yes. The one on page whatever it is? Page 6, yes.

Q. And so -- and this combined picture of NewCo is better than Puget or Washington Natural stand alone operations on an aggregated basis; is that right?

A. Then either one stand alone, I believe it is, yeah.

Q. Is it correct that the combined --

A. For operating income and revenues?

Q. (Nodding head). Is it correct that the combined picture that's shown on page 6 of Exhibit TS-34 doesn't allow us to gauge the degree to which Washington Natural Gas's operations become better off with the merger as compared to its stand alone operations?

A. Well, they're not -- we didn't do it separately after the merger, I mean, if that's what you're getting to. We don't have gas and electric separate.

Q. And so my question, though, is and now for Puget as well but for both Washington Natural and Puget we can't look at this document and figure out the degree to which Washington Natural's operations or Puget's operations are better or worse off with the merger than on a stand alone basis.

A. Not from this document, no. You would have to look in the aggregate for the two.

Q. So we don't know looking at this document whether or not the merger benefits went to the gas side or the electric side?

A. That's true. This doesn't separate them.

Q. Do you agree in principle that the customers of both gas and electric operations should receive a fair and equitable share of the merger benefits?

A. I think the merger benefits should --

Q. If you could provide me with a yes or no to that question and then explanation after that would be fine.

A. Sure. I think that all the customers should get -- all the customers are going to get a share of the merger benefits, and they're going to both gas and electric.

JUDGE SCHAER: So is that a yes to start with?

THE WITNESS: I think it's a yes.

MR. CEDARBAUM: My question was --

JUDGE SCHAER: And then you wanted to explain.

Q. My question was do you agree with the principle that the merger benefits should be equitably shared between gas and electric and your answer is yes?

A. I said they should be shared and how they're shared becomes the subject that I think we're trying to get to. My position would be that we would share the benefits the same way or allocate the benefits the same way we would allocate the costs.

Q. But you agree with the principles that there should be an equitable sharing of the benefits?

A. I believe there should be a sharing.

Q. That's not equitable?

A. Well, has to be equitable.

Q. But you don't think we need to disaggregate the gas versus the electric operations to determine if that equitable sharing has occurred?

A. We did not do that, and we don't have the forecast to do that right now. We just haven't done it.

Q. And you don't think it's necessary to do that?

A. I think you could probably look at it at some point. It would take an estimating how the benefits would be allocated and, as I said, I would propose we allocate the benefits the same way we allocate costs in the future.

Q. But it's your testimony that even though we can't trace in this exhibit where the benefits go, either to gas or electric, that we can determine that there's been an equitable sharing of those merger benefits?

A. You probably can't from this, I agree. What I said was we haven't done that. We didn't do it.

Q. You don't think that information is important in this proceeding?

A. It may very well be important, yeah. We have not done that.

Q. Turning to Exhibit TS-35, which was part of your response to our staff data request 96, and I believe you anticipated some of these questions, but we asked to have data request 38 recast with some different assumptions, and we also asked for the disaggregated gas and electric operations; is that right?

A. In this one, yes.

Q. And your response is that you don't have a model this time that is capable of showing that disaggregation?

A. That is correct.

Q. You also indicate in the explanation that an allocation of savings to gas and electric is not possible as it is unknown at this time how the savings will translate into the cost allocation?

A. Yes.

Q. When was the merger announced to the public?

A. I believe it was October 18th.

Q. And between October 18th and the presentation to the rating agencies in January a model was constructed that came up with Exhibit TS-34?

A. Not entirely. We took the models that each company had and basically just put them together, and we used a spreadsheet to -- at least to my understanding we used a spreadsheet then to come up with a combined.

Q. Since Exhibit TS-34 was prepared, have either of the companies developed the capability of disaggregating between gas and electric?

A. Not to my knowledge, no.

Q. Let me turn to your testimony at page 5, and by the way I'm done with those exhibits now. In your testimony at page 5 and in your Exhibit JPT-4, which is Exhibit 7, it appears that the reaction of the financial community regarding the proposed merger is negative with respect to Puget and positive with respect to Washington Natural; is that right?

A. No, I wouldn't say that. I think what I said in the testimony is that the rating agencies at that point in time said that the -- they put Puget Power on credit watch with negative implications, Washington Energy with positive implications and the fact that the stock market, what the stock price did was initially it declined a little bit for Puget, then it went up, now it's back down. It's trading pretty much in line with -- actually it's doing a little better than the Dow Jones utility index since then, so I wouldn't characterize it as the market saying it was negative.

Q. Well, on page 5 you say that "S and P -- at the beginning of page 22 -- "on a preliminary basis indicated that the financial profile of NewCo is unlikely to sustain Puget's senior debt rating." You also indicate, as indicated by S and P, that Puget is at the lower end of the A minus category -- excuse me. "S and P has revised its outlook for Puget for '95 as negative." Do you see those as positive reactions to the merger?

A. I think those are reactions not to the merger in itself but to Puget, and what they're doing to the credit ratings of Puget versus what the new company would be.

Q. Well, your question on line 21 is, "What were the rating agencies" initial reactions to the merger announcement"?

A. Correct.

Q. And then from lines 22 on page 5 through the top -- excuse me, through line 6 on page 6 you paint what looks like a negative picture of Puget. And I take that to mean that the rating agencies' -- financial communities' reaction to the merger was not good with respect to Puget and good with respect to Washington Natural?

A. That's fair, but you were saying that it was negative towards the merger, and I wouldn't characterize it that way.

Q. That's what your testimony says.

A. I think the implications were that Puget, at least from -- that the release S and P put out initially -- and they did this the day after, shortly thereafter the announcement of the merger -- that they felt that Puget would end up with a triple B plus rating, or that Puget Sound Energy would, which would be less than the current rating for Puget Power, but in the aggregate for the two companies I felt that it's not necessarily negative for the merger.

Q. So with respect to Puget the financial community's reaction was a possible lowering of the bond rating?

A. The rating agencies said there would be a possible lowering of the bond rating not the financial community. I wouldn't draw the entire financial community into that. And there was one rating agency. That was Standard and Poor's. Moody's did not say that other than they put them on credit watch, the same thing with negative implications, and WNG with positive implications.

Q. Were a lower bond rating to result from the merger for Puget's debt would that mean that Puget's cost of debt would be higher?

A. To the extent you were issuing it as Puget. Keep in mind once you merged you would issue Puget Sound Energy, so you have to look in the total, because Puget Power wouldn't be issuing debt anymore. You would have existing debt, and that's traded. We would issue debt as Puget Sound Energy and it would in the aggregate, at least I feel, that it would be -- you would be better off.

Now, we have one rating agency that said it might be -- that their initial reaction would be it would become a triple B plus. The other ones haven't responded, and that was also before we provided them the forecast. We sat down with them -- and also before we could even talk to them about the benefits of the merger, such things as being able to keep rates stable and all the things that you read -- you read in the exhibit that I put together about what the rating agencies are looking for, which is quality of management. It's looking at expanding customer service, being able to manage costs.

All these things they're going to factor in and the quality of management. So I think you have to look in the aggregate, and I would agree if you were going to say that Puget Power stand alone the rating is lower but it doesn't mean that necessarily Puget's -- Puget Sound Energy's cost of debt would necessarily be higher because you have to factor in the Washington Natural Gas side then.

Q. So on page 5, line 22, the rating agency that you refer to as S and P which anticipated a combined senior debt rating of triple B plus would be a lowering from Puget's stand alone bond rating?

A. Right. At that point in time they were -- as you said they were a very weak A minus, and also if you look at what Moody's was saying they were anticipating in the future that most electric companies were going to be seeing a lowering of their rating over the next two to three years because of the change in the industry. So I think, you know, looking at this merger you could start to look at that as a positive, because we're going to be bringing together two companies that are going to provide a lot of benefits to the customers and to the shareholders, and also then the financial integrity of the company I think is going to get improved.

Q. In your Exhibit No. 5, pages 20 to 21, you indicate that Puget has debt at nine months ended September '95 of $971.4 million. I don't know that you need to actually look at that.

A. Yeah, I have it here.

Q. If Puget on a stand alone basis has a debt rating lower from where it is today, Puget's cost of debt would then increase; is that right?

A. Sure. If Puget stand alone had a decrease in their bond rating then any debt they issue in the future would probably be -- cost them a little bit more, and the difference between, let's say, an A minus and a triple B plus may be in the five to ten basis point range today. That's just a guess right now. Five to ten to fifteen. Somewhere along those lines.

Q. Is it correct that with respect to NewCo Puget's shareholders will own 75 percent of NewCo's shares?

A. I think that's about right, yes.

Q. And if the merger increased the cost of equity of Puget and Puget's 75 percent to the new company, would that mean that the new company would also have a higher cost of equity than Puget did before the merger?

A. If the cost of equity were to go up then, yeah, there would be a little higher. I would contend that because of the things we were doing it would go down.

Q. Mr. Torgerson, the answer to the question was yes. Will Washington Natural Gas's cost of equity decline to offset any increase due Puget so that NewCo's cost of equity is not higher than the average of the two?

A. Can you ask me the question again.

Q. We had agreed, I think before, that if the merger increased the cost of Puget, because Puget owns 75 percent of NewCo's shares, Puget's cost of equity would go up, and my question, would Washington Natural's cost of equity go down to offset Puget's increase?

A. If you assume Puget's cost of equity went up. I'm not sure it does but you're assuming you take one and you're balancing them off against each other and that the cost of equity for one is going up and the other is going down. I think, as we would put together the cost of capital or cost of equity for the Commission, we would do it stand alone, and look at comparables and so forth.

Q. Is the answer to my question -- I'm not sure what the answer to my question is.

A. Well, the answer I think for Puget Sound Energy, at least in my opinion, that the cost of the equity in the aggregate --

Q. That's not my question. My question was if Puget's cost of equity went up would Washington Natural's cost of equity go down to offset the increase of Puget?

A. I'm just not certain that it would. I mean, you're assuming one goes up and they're just going to offset each other.

Q. So the answer to my question is no?

A. I'm saying I don't know without looking at it, but the cost of equity stand alone, it's very hard to take it stand alone and then say you're merging and now it's changing because you're not going to look at it stand alone necessarily afterwards. Things have changed with the company. The shareholder base changes. The dividend the Washington Energy people would be getting is changing dramatically, so you're looking at trying to calculate something that before was stand alone and now is combined and saying they're changing and the changes are offsetting each other.

Q. Did Mr. Flaherty's analysis assume any changes to the cost of capital for NewCo?

A. I do not believe it did.

Q. If the merged company had a higher cost of capital than the two companies did on a stand alone basis, is that something that would be important from a public interest perspective?

A. If they did I would assume it is, yes.

Q. Is it correct that the shares of Washington Energy Company will represent .86 of old company shares when they become new company shares?

A. The exchange ratio that would exchange Washington Energy shares into Puget Sound Energy is .86, so a person owning one share of Washington Energy would get .86 going forward.

Q. And Puget shareholders receive a one for one exchange for shares of NewCo?

A. Well, it really isn't an exchange because we're being merged into Puget so theirs stays the same.

Q. One Puget shares equals one?

A. Puget Sound Energy, yes.

Q. Was the .86 figure for Washington Energy Company and the one for one for Puget negotiated by investment bankers or was it set by the market in some manner?

A. It was negotiated by the CEOs with assistance from investment bankers.

Q. Can you explain in more detail your answer, just what happened?

A. Sure. The investment bankers, we had board meetings going on simultaneously with the two companies. Puget had one and we had one. And the investment bankers presented to each board what they believed a fair exchange would be within ranges, and then -- and I'm talking more from Washington Energy's side because that was the board meeting I was in.

Then the two CEOs contacted each other and started talking about what kind of exchange ratio there could be, and they negotiated it throughout several different phone calls where they would talk, then go back and talk to their boards, and then go back and talk again. There were several phone calls that went back and forth and finally they both agreed that the .86 exchange ratio would be appropriate and the investment banker said that it was fair for each company. Our investment banker Goldman Sachs said it was fair for us and Morgan Stanley gave the Puget board the same opinion at that time at the board meeting and then they substantiated that exchange or fairness opinion at the time the proxy was sent out.

Q.   During what period of time did these events take place, do you recall?

A.   The negotiations?

Q.   Right.

A.   Well, keep in mind we were working with Puget and investment bankers and all sorts of people -- and it's all laid out in the proxy -- for a number of months. The actual negotiations on the exchange ratio probably occurred during those board meetings, I mean, that day. I mean, we knew where we needed to be. At meetings I had with the Puget people and their investment bankers I had told them where I thought the price needed to be and given them an indication. And -- because we told them there would have to be some sort of premium and we had communicated that. So the negotiations culminated on the day of the board meeting with the CEOs discussing and negotiating actually that exchange ratio with the investment bankers helping us.

Q. We've asked in a recent data request for board meeting minutes. Would those minutes reflect some of this discussion?

A. They may. I don't know how much detail those board minutes have.

Q. Are there any other documents that would document these negotiations and discussions?

A. No. There really aren't. I thought we provided everything I have.

Q. Looking at page 26 of Exhibit 5, is it correct that for the last quarter prior to the merger announcement that the market price for Washington Energy Company's stock averaged $17.81 per share and the market price for Puget stock during the same quarter averaged $23.125 per share?

A. Can you point to me which line you're looking at there?

Q. If we were to average -- I'm looking at page 26 of Exhibit 5. If we average for Puget the high and low for the fourth quarter '95 we would get the 23 and an eighth dollar figure and if we were to average Washington Energy Company's high and low for the same quarter we would get the $17.81 figure.

Would you accept those subject to check?

A. I think the averaging is probably right. The only thing I need to check here is which quarter are we talking about, because we're on a fiscal year, that our fourth quarter would have ended -- I have to see what we said here. Our fourth quarter would have ended September 30 of '95 whereas Puget's would have ended December 31, and I am not certain which is which here.

Q. Why don't I ask you then as record requisition No. 7 --

JUDGE SCHAER: You may want to look at the left-hand labeling.

A. That's calendar year. So that's the calendar year for '95 so that would have been October through December, so if those averages are right, I mean, I don't -- subject to check I can average those two.

Q. And the ratio between those two subject to your check is .77?

A. That may very well be. As you're well aware the markets are discounting our stock at this point because of a couple of things. One, the dividend that we pay is less than the Puget dividend.

Q. Mr. Torgerson, you really need to think

about answering my question and stop there. You've got your own lawyers that can follow up.
A. Okay.
Q. Staying on page 26 of Exhibit 5, will you accept subject to check that the ratio of the closing high prices for Washington Energy Company versus Puget for all quarters from the third quarter of 1993 through the first quarter of 1996 have never been as high as .86?
A. Subject to check, certainly.
Q. And this same page indicates that if the merger took place on January 30, 1996 Washington Energy shares would have been converted into NewCo shares at $21 and a half which was one dollar per share higher than WECO existing price on January 30, 1996?
A. Subject to check, sure.
Q. In your testimony at page 13, line 21, you refer to the ratio of February 13, 1996 stock prices as $25 and an eighth for Puget and $20 for Washington Natural. Would you accept subject to your check that this would be a ratio of less than .80?
A. Yes, subject to check.
Q. You also say on the bottom of 13 and on to 14 that the extent to which the ratio was less than

.86 represents Washington Energy Company's discounted -- price discounted for the difference in annual dividends and uncertainty as to the time and the likelihood that the merger will be completed; is that right?

A. That's right.

Q. So is it correct that when the merger is completed WECO shareholders will expect a dollar per share gain because the uncertainty of the merger would be over?

A. At that point in time the exchange -- the differential in the price should move to where it should be trading at .86, so whatever the price is, it will go to that exchange ratio, based on Puget's price versus our price at that point in time. I can't say that it would be a dollar because I don't know what the price would be at that point in time. But it will move to the exchange ratio.

Q. And so completion of the merger from the Washington Energy Company shareholder's perspective is a good thing because Washington Energy Company stock price is less than .86 of Puget's stock price; is that right?

A. I think it's good for both, but yes. I think that shareholders -- Washington Energy shareholders will see an increase over the current price based on the exchange ratio.

Q. In making the statement about the discount for Washington Energy Company, you're making reference to that company as being below the .86 ratio; is that right?

A. Yes. Today, as you pointed out, the exchange rate -- the ratio of the Washington Energy price to the Puget price is less than .86.

Q. Now, if we were to look at the transaction from Puget's perspective using the February 13th, '96 stock price of $25 and an eighth, it would appear that Puget's stock is 25 percent above WECO stock; is that right?

A. Yes, it's about that, that's right.

Q. And that could be a bad event for Puget stockholders because if the merger were consummated it would be possible for Puget's shares to fall below the $23 and an eighth under the same theory that you say WECO shares are selling at a discount relative to the .86 ratio; is that right?

A. I wouldn't agree with that. I think the Puget stock price -- the Washington Energy stock price, as I said, reflects the Puget stock price today and the exchange ratio and then discounted for the dividend and the timing. The Puget stock price is going to trade on its own and most of the investors have already factored in the merger into their stock price and the Washington Energy price is just trading at a discount because of, as I said, the dividend and the uncertainty, so I believe that the Puget price already reflects at least to some extent the merger, and I couldn't see necessarily that it would pull it down.

Q. I would like to discuss book value for a few minutes. Is it correct that on page 24 of your Exhibit 5 the merged company book value is $16.13 for the nine months ended September of '95?

A. Yes. Under this proforma it shows $16.13.

Q. And that results from a combination of 18.29 per share from Puget, which is shown on page 20 of your exhibit, with $8.17 from WECO which is shown on page 21?

A. Yes, and reflecting the exchange ratio.

Q. So that means that WECO stockholders will experience an increase in book value from -- excuse me -- 8.17 to 16.13 on a post-merger basis; is that right?

A. It says that the company, yes, will have a higher book value of Puget Sound Energy than

Washington Energy Company book value today on a proforma basis when you add the two companies together.

Q. But the numbers I gave you are correct that with the merger a Washington Energy Company stockholder will have a share of stock worth $16.13 whereas before there was a book value of $8.17 for that share?

A. The book value -- yeah. The book value of the new company is considerably higher.

Q. So the answer to my question is yes?

A. Yes.

Q. And Puget will experience a reduction in book value per share pre-merger to post-merger from $18.29 for a Puget shareholder to $16.13 for a Puget shareholder; is that right?

A. Yes. Again, the Puget Sound Energy book value will be that on a proformed basis.

Q. And we can refer to that decrease in the book value per share of a Puget shareholder as dilution?

A. It's a decrease, so I guess you could say it is somewhat dilutive on the book value basis.

Q. And if Puget's book value per share falls, wouldn't you expect its stock price to fall?

A. No, not necessarily.
Q. Why is that?
A. I think you have to look at the overall benefits of the merger. I mean, we're assuming that the book value equates directly to stock price, and some people say that it does. A lot of people look at book value in relationship to stock price. It's one of the things our investment bankers looked at, but it doesn't mean that just because the book value of the company dropped that the shareholders are going to see a decline in their market price.
I think you have to look at the benefits of the merger in the aggregate, which are all the things we've talked about in our testimony about being able to provide customers a stable rate environment, being able to generate the synergy, best practice, power cost savings. All those things are going to enter into what happens to the stock price, and I don't think it's just looking at a change in book value.
Q. Is it correct that the business we're talking about is a regulated business that's regulated on the basis of book value?
A. It is, yes. It is regulated and the book value does have -- does play into how the returns are calculated in some calculations.

Q. Turning to your testimony at page 6. I believe you testified on this page that the rate stability plan would alleviate some of the concerns of the rating agencies, and this is on line 10 and 11.

A. Yes, that's here.

Q. Since the rate stability plan calls for the company to essentially retain the benefits of the annual merger savings and best practices savings with no rate increase until the year 2001 for gas and then one percent annual increases through 2001 for electric, it would be your assumption that NewCo's earnings would rise; is that right?

A. We said publicly after the merger was announced that providing we got the synergy, best practices, all those savings, that we would be -- the merger could be accretive to the earnings of Puget, Puget Sound Energy.

Q. Referring once again to your Exhibit 5, page 24, you show the merged company's financial results by combining Puget and Washington Energy Company operations from 1990 through September 30, 1995; is that right?

A. Yes.

Q. Let me ask you if you would accept the following: Combined returns on equity and fixed charge coverages since 1991 for NewCo, and for the year 1991 the return on equity is 13.01 percent with a fixed charge of 2.41. For 1992 a return on equity of 10.77 percent with a fixed charge coverage of 2.49. For 1993 a return on equity of 10.05 percent for a fixed charge coverage of 2.23. 1994, a return on equity of 6.27 percent for a fixed charge of 2.40, and finally 1996 a return on equity of 5.37 percent with a fixed charge of 1.75.

That was a lot of numbers but would you accept them all subject to your check?

A. Yes. If you got them all off this proforma we can check that.

Q. Just so you can check how we got these numbers, we took the earnings per share and divided by the average back value per share off of page 24.

A. Okay. Just straight up? I mean, it's not a Commission basis or anything?

Q. Straight off this document.

A. Okay.

Q. Has there been prepared the -- similar document to page 24 of Exhibit 5 for the 12 months ended calendar year 1995?

A. I would have to check. I would have to look. I think we have and it's probably in one of the

10Ks or the 10Qs because I believe we have to report a proforma since we announced the merger but let me look.

Q. Let me ask as the next record requisition that you provide us with the comparable page 24 of Exhibit 5 for the 12 months ended calendar year 1995 and then if you have it -- also if you have it available the first quarter 1996 and the second quarter 1996.

A. The first quarter we can do that. Second quarter we haven't provided a 10Q yet.

Q. You respond to the record requisition as best you can and as additional quarters in 1996 become available if you would supplement the response with them.

A. Okay.

(Record Requisition 7).

JUDGE SCHAER: That will be record requisition No. 7.

Q. On page 9 of your testimony, at the bottom you state that you believe NewCo's bond rating should be in the A minus category. Do you see that testimony?

A. Yes.

Q. Can you describe any projection that you have available which forecasts the increased return on equity in coverages to the point where an A minus rating would be justified, if you have such projections?

A. Well, they were in the rating agency forecast which you have which gives the -- there's a page in there for Puget Sound Energy that show what our projections would be for all of those ratios, and that is what led me to the conclusion that if you look at those ratios -- and again it assumes a lot of things, that we get all of these best practices savings and so forth -- that the ratios would be at least consistent with what Puget Power had in the past and pretty much in the range of an A minus company.

Q. On page 12 of your testimony you indicate that Puget has a $74 million revenue requirement deficiency that would only be partially offset by the synergy savings. Do you see that testimony?

A. Yes, I do.

Q. And so is it your testimony that absent the merger Puget would file a rate case to produce increased revenues of $74 million?

A. Puget has the need for $74 million in revenue. Absent the merger I would assume they would probably have to file some type of rate increase.

Q. So this Commission can expect a tariff filing?
A. You may want to ask Mr. Sonstelie but not being an officer of Puget I couldn't respond to that, but they certainly had the need for the $74 million rate increase.
Q. And earlier you had indicated with respect to Washington Natural an additional revenue requirement of three or four percent I think?
A. Yes.
Q. Is it your testimony that after the current rate case moratorium for Washington Natural that a filing would be made?
A. We would make a filing -- if we were not to merge, we would be stand alone, we would be making a filing for a two or three percent increase sometime in 1997 after the moratorium is over.
Q. If the actual savings exceeded the savings that Mr. Flaherty has forecasted, is it correct that NewCo would experience excess earnings?
A. If the actual savings related to the synergies --
Q. Yeah.
A. -- specifically? I wouldn't say we have excess earnings. We would have savings above the

synergy amount. Keep in mind that we also assumed for Puget Sound Energy best practices and power cost savings, so you have to look at all of those before you could make that statement.

Q. Let's say that all the savings exceeded what was forecasted, best practices, power costs, Mr. Flaherty's number. Is it correct then that NewCo's earnings would increase?

A. If all those things -- we got all those plus more then, yeah, the earnings would be somewhat higher than what we had forecasted.

Q. Would Puget forego the one percent annual increase in electric rates for '97 through the year 2000 under that circumstance?

A. I think you're trying to jump a little bit far here. To assume that we're going to get all these savings and they come over time and to say that we don't need that one percent, the one percent was part of an entire package, and I think the whole thing is needed. I mean, we were looking at the entire program of what we presented to this Commission.

Q. And so in a particular year during the period 1997 through 2000 if all of the savings from all sources exceeded the projections Puget would still come in with tariff filings for the one percent increase?

A. Yes, that's our plan right now. And I think it would be -- actually I think it would be great if we could do better because then the customers are all going to get that in the future. I mean, all the savings go to the customers, and I think if we could do a whole lot better I think it would be great not only for our company but for customers in the future, and I think we will be striving to do as best we can maintaining and keeping our costs down.

Q. The one percent annual increase is proposed -- so it's your testimony that if the savings from all sources exceed the forecast Puget will still file for one percent increases and that that's a benefit to customers?

A. I think over time it will be, sure. If we can have a very healthy company and knowing that all savings ultimately go to customers, then I think that's a good outcome. And yes, you know, the program we have now says there would be a one percent tariff increase annually, and if you start -- a lot of these savings are generated over time. You're not going to get them all day one, so to look at maybe we get a host of them early on and then nothing later. I mean, it's timing at that point.

Q. You may have already indicated this, but is it correct that the merger will help NewCo's shareholders by increasing their earnings per share?

A. As I stated before, that after we announced the merger we said that we felt assuming that we attained all the savings we outlined that would be accretive to Puget Energy's earnings.

Q. If the return on equity were to rise from 9 to 12 percent under the merger and the rate stability plan as proposed is instituted, is it correct that NewCo's stock price would also rise?

A. If the stock market assumes that 9 percent is the rate of return we're getting and we actually realize something higher than that and it looks like that can be maintained and sustained for some period of time then I think the stock price would reflect that. I mean, you're talking about a three percent differential on earned return, and as long as it was durable and it was going to be earned over time versus saying that 9 percent was all that the company was ever going to earn then I think the stock market would reflect that with an upward movement in the stock price.

Q. Looking at page 87 of Exhibit 5. At the top under the heading dividends it contains the stated intent of NewCo to maintain the current $1.84 dividend per share of Puget; is that right?

A. Yes. The words are subject to the foregoing but initially will adopt the dividend policy followed by Puget which currently is $1.84.

Q. And currently Washington Energy Company pays a dividend of a dollar per share?

A. Yes. Currently that's our dividend rate annualized.

Q. And so since WECO is currently paying a dollar per share, doesn't that mean that the larger amount of merger savings would have to go to pay the higher dividends on former WECO shares?

A. Well, you have a merged company now.

Q. This is all part of the pooling?

A. The shareholders of Washington Energy would receive a higher dividend, the former shareholders will become Puget Sound Energy shareholders. Their dividend, yes, will go up.

Q. It will go up because a larger amount of the merger savings will be used to pay that higher dividend?

A. I mean, the earnings have to come from the company and they're paying all shareholders the same amount, $1.84, at least initially.

Q. So to the extent that there are savings those savings must be used to pay the higher dividend of the combined company?

A. I think the earnings of the company --

Q. Can you answer yes or no and then you can explain. That's fine.

A. You're going to have to have more cash flow to pay the higher dividend. The earnings of Puget Sound Energy are going to be whatever they are.

Q. As the source of that higher cash flow, a source, the savings --

A. One source of the savings and the earnings are the -- rather the earnings and the cash flow are the savings, all the savings.

Q. Can you tell me what payout ratio the $1.84 dividend for NewCo implies?

A. I think you're getting into an area that --

Q. If you need to do that by record requisition that would be fine.

A. That is confidential if you're asking me to say what a payout ratio would be and you can translate that into an earnings number on a projected basis, which I don't think I ought to be doing.

Q. You ought not to be doing that if I were to ask you to provide that to the staff?

A. We can do it on a confidential basis. This would have to be one of those confidential requests.
MR. HARRIS: Let's do it as a record requisition.
MR. CEDARBAUM: Well, that's what I was going -- I thought we would just treat this as Mr. Harris proposed back at the beginning of all this. I will make the record requisition and then you can decide, you can decide, who gets it. As long as I get it.
Q. Would your response to that record requisition --
MR. CEDARBAUM: Did we have a number for that?
JUDGE SCHAER: No. 8.
(Record Requisition 8.)
Q. -- would that include a cash flow forecast?
A. Well, Puget Sound Energy already has all that, the forecast, on a combined basis, and I think in the information that was provided the rating agency, it's all in there.
Q. So that information would provide us with a cash flow forecast indicating how NewCo can support the $1.84 dividend?
A. Yes. That's in the rating agency forecast,

the payout ratio. If it's not there it's a very simple calculation.

Q. If the Commission were to disallow some of the proposals in the merger and the rate stability plan, could that reduce the $1.84 dividend per share target?

A. If the Commission were to disallow the proposals the company made then the boards would have to determine whether we wanted to merge in the first place, and that's a determination only the boards could make. So --

Q. What about a situation where the merger is approved -- the merger goes forward but with certain conditions that are different from the merger as proposed in the testimony and the application? And the Commission also with respect to rate stability plan revises that somehow or rejects it. Would that -- and again I'm assuming the merger still happens. Would that have an impact on the $1.84 dividend per share target?

A. To assume that all those things and then say the merger is going to happen is kind of a stretch. I mean, I think the boards would have to look at exactly what is proposed. I mean, we had a plan that we put forth that the boards approved. Any deviation from that the boards would then have to review it and decide if the merger should go forward.

Q. Or if the $1.84 dividend per share target should be lowered?

A. The boards have discretion to determine what the dividend is going to be, certainly.

Q. If the Commission allowed the merger to go forward but required savings from all sources to be shared with ratepayers in some way, would that jeopardize NewCo's financial viability?

A. Well, in my mind the savings are all going to the ratepayers today, so if you're talking about having -- causing some type of rate decrease or whatever, I mean, in my mind the savings are all going to the customers. So perhaps you can ask me the question differently.

Q. I guess that's my question then. That if the Commission permitted the merger to go forth but rejected the rate stability plan what is your opinion about NewCo's financial viability?

A. I think first we would have to get over whether the merger -- the boards would approve it, and I think only the boards are going to decide if that's appropriate to even have the merger consummated without the rate stability plan.

Q. So the impact on the financial viability of NewCo might be such that the merger would not go forward?

A. Could very well be. It would be a negative impact on the projected financials.

Q. And the same would be true for the $1.84 dividend target?

A. Again, the boards would determine what kind of dividend to pay. With the merger, without, that would have to be determined based on the earnings of the company going forward. Either stand alone or as a merged entity.

Q. I would like to shift gears a little bit and discuss Washington Energy Company's nonregulated operations. And my question is, what is NewCo's plan with respect to the nonutility subs of Washington Energy Company?

A. Well, we can take them one at a time. Washington Energy -- and basically we haven't made very many decisions regarding the subsidiaries. Especially Washington Energy Services Company, we have not decided yet what is going to happen with that subsidiary. I mean, it could be that we retain it as the company it is or expand it. We just haven't made that decision. We've been focusing more on the utilities. The coal and the railroad I would expect those would be -- we're looking at whether or not we want to continue with those right now, and we're pursuing whether we should even have those into the future, but we haven't made any final decisions on that yet either.

Those are the two major subsidiaries. The other holding we have is the Washington Energy has an equity interest and preferred stock in Cabot Oil and Gas Corporation, and I think ultimately that investment will probably be disposed of at some point in time but I don't see it in the near future. And the reason being is -- well, one is the impact it would have on the pooling of interest by disposing of a large block of assets. Could negate the pooling of interests.

Q. With respect to the subsidiaries that NewCo will keep, it may be eventually that they'll sell them off but at least for the foreseeable future -- let me back up and ask you this question first. Is it correct that Washington Energy Company's nonregulated subsidiaries have operated at losses?

A. Some of them have. Today Washington Energy Services Company earned a small profit year-to-date. Thermal Energy and ThermaRail, which are the coal and rail subsidiaries, have losses but it's mainly allocated interest expense and operating expenses. So those -- since we never had an operation those have always been in a loss position. Going back a few years, the oil and gas subsidiary actually did make money but when we merged it we ended up with a significant write-off, so it made operating income but then the merger resulted in a large loss.

Q. What about Cabot?

A. Cabot this year, if I remember right, it's earning about -- so far this year I think it's earned about four, five, six million net income and we report 9.4 percent of that on an equity basis and we also get preferred dividends which are -- obviously add to our income.

Q. If we look at pages 20 and 21 of your Exhibit 5 -- excuse me, 21 and 22 --

A. I have those.

Q. -- it shows for Washington Energy Company, beginning in 1994 through the nine months ended September 30, '95, losses in the range of 41 to 54 million for income available for common stock; is that right?

A. Right.

Q. And then if we were to look at Washington

Natural on page 22, at least for 1995 it's an income gain -- income available for common stock with positive 10.7 million?

A.   Yes, that's correct.

Q.   So is it correct that the losses that Washington Energy Company have shown are caused predominantly by the nonregulated subsidiaries?

A.   Well, this is what I mentioned before. These are the write-offs and write-downs of those nonregulated assets that we took.

Q.   Will the nonregulated subsidiaries contribute to the $1.84 payment?

A.   Based on this year, if you look at Washington Energy Services, which is profitable, and the Cabot investment, the answer is yes, because both have generated income for the parent company.

Q.   You indicated that some of the subs were operating at a profit now, which I'm having a little trouble reconciling with Exhibit TS-33 page 6. If you look at the top part of that page under the estimated 1995 and budgeted '96, at least the estimated 1995 Washington Energy Service, Thermal and Thermal show losses in '96 budget. Thermal shows a loss, Washington Energy Services a gain and then Washington Energy Company, which I assume would include the Cabot holding, shows losses throughout the period shown on this page 1995 through 2000. So I guess I'm confused about your testimony that just occurred that the nonregulated subs are profitable and would support the $1.84 dividend.

A. What I said was Washington Energy Services year-to-date was making a small amount of money. I agree in '95 they had losses. Going forward the projection shows them being profitable. I also said Thermal Energy was losing money mainly because of interest allocations. In Washington Energy Company you have interest that's at the holding company level. You have allocated expenses that come in through -- for holding company activities. You also do have the Cabot investment, which is, as I told you this year, they have public information which shows that they are profitable this year. Last year Cabot had a loss and they took a significant write-off which was part of the write-down we also had to take. So, yes, that's in '95.

Q. So if I were to add a column to page 6 of Exhibit TS-33 for Cabot you're saying I would be showing positive numbers across the page?

A. I can't project Cabot's earnings going forward. We have for a forecast, and I don't know anything more than anybody else who is a public shareholder. We do get a preferred dividend from Cabot, which is about 3.4 million annually, and then we also report, as I said, 9.4 percent of equity earnings they generate. This year Cabot is profitable so far, and going forward you have to look at what the analyst estimates are. I know we will get money out of the preferred dividend but I can't really get into projections on Cabot's earnings.

Q. On Exhibit TS-33, page 6, doesn't the exhibit show that except for Washington Energy Service Company, beginning in 1996, all of the unregulated subsidiaries in the aggregate, at least, operated at a loss?

A. If you add up those numbers, it would show a loss, and just keep in mind what is in Washington Energy Company in total, and the other thing that's in there, which I forgot initially, is the preferred dividends of Washington Natural, which because of the way the preferred dividend gets reported, because it's a preferred stock holding of a subsidiary when we consolidate has to be shown as expense or minority interest in the holding company, so that's $7 million a year of preferred dividends are included in that one number as a loss for Washington Energy Company.

That's another piece of it you have to remember.

Q. Turning to page 44, and now actually I'm -- you have the attachments that were included with the application with you? They're not exhibits in the case.

A. The attachments to the application?

Q. I'm looking at included in the attachment were Washington Energy Company's 1995 10K, so that's what I would like you to have in front of you.

A. I have a copy of the 10K here.

Q. And it's attachment B, in attachment B of the application. Do you have it?

A. I have Washington Energy's 10K for fiscal year ending '95.

Q. Looking at page 44 it shows that Washington Energy Company's 1995 common shareholder's interest was $196.7 million; is that right?

A. Yes.

Q. And on page 55 of the same document, it shows Washington Natural Gas's '95 common stockholder's interest to be $251.5 million; is that right?

A. Yes.

Q. Can you explain why Washington Energy Company '95 stockholder's interest was $55 million less than Washington Natural Gas's?

A. Sure. I think I mentioned this before. We had write-offs at the holding company related to Cabot primarily and the coal and the railroad which eroded the equity.

Q. Since you've indicated that some of the investment in the unregulated subsidiaries was written off, I assume that means that that investment was financially a big problem?

A. They were written down under FASB -- Financial Accounting Standard Board -- 121 on Cabot investment, and on the coal investment. This is a new accounting pronouncement, actually came out about a year or so ago, that required a valuation of long life assets and we revalued our assets under those provisions and it required a write-down.

Now, the coal and railroad we had considerable amounts invested and the prospects of earning on that over time, I think, is -- well, I just don't see it happening in the near term so that was what entered into the write-down there, and Cabot wrote down -- took a write-down of their own under FASB 121. We took an additional write-down to reflect the stock price being below -- take it even further down to the current market price at that point in time.

Q. Would you accept subject to check that in fiscal year 1990 Washington Energy Company's gross assets in its oil, gas and coal subs totaled $173.9 million?

A. Subject to check, I will look at that, yes.

Q. Is it correct that in fiscal year '95 Washington Energy Company's gross assets in its oil, gas and coal subs fell to 15.6 million and if we were to include its investment in Cabot the total would be 85.9 million. Would you accept those figures subject to your check?

A. Subject to my check, yes.

Q. So Washington Energy Company's gross assets in those same properties fell by $88 million over the 1990 to 1995 period; is that right?

A. Based on that calculation, subtracting the two and subject to check, yes.

Q. Is it correct that Washington Energy Company's capital expenditures for those properties totaled about $106 million -- 106.7 million over the 1990 to '95 period, subject to check?

A. Subject to check, yes.

Q. In 1994 Washington Energy Company merged its oil and gas exploration and production subsidiary

with Cabot; is that right? We've had some discussion about that already.
A. Yes. I think it was May of '94.
Q. Do you know what's happened to the value of Washington Energy Company's investment in Cabot between '94 and 1995?
A. Yes. As I said, we took some write-downs of that.
Q. Would you accept subject to check that it fell from $97.8 million to $70 million?
A. Subject to check, yes. That sounds about right.
Q. Do you expect any more decline in Washington Energy Company's investment value in Cabot?
A. I wouldn't expect any further decline. As a matter of fact, Cabot's stock price is actually up somewhat since we took those write-downs.
Q. Do you know what the current value Washington Energy Company is now carrying for Cabot on its books?
A. It's probably in the same neighborhood of that $70 million. I would have to check.
Q. Why don't I make that the next record requisition in order.
JUDGE SCHAER: No. 9.

(Record Requisition 9.)

Q. Can you tell me what Washington Energy Company's earnings per share from continuing operations were for the 12 months ended June '96?

A. 12 months ended June '96? We just did a press release on it and I don't have it off the top of my head, but the nine months I believe were like $1.17. The twelve months would probably have been a loss because we would have picked up the fourth quarter of the calendar year -- or fiscal year '95.

Q. Would it then be less than a dollar, do you think?

A. Oh, yes.

Q. We previously discussed Washington Energy Company's current annual dividend per share of a dollar. Can you tell me how it finances that dividend?

A. Currently we are not -- over the last 12 months we're not earning the dividend so --

Q. So it's not financing?

A. The earnings have not, no, over the last 12 months.

Q. Do you know what Puget's earnings per share for the 12 months ended June 30, 1996?

A. I believe theirs was right around $1.84.

Q. And its current annual dividend per share again is $1.84?
A. Yes.
Q. So its dividend payout ratio is 100 percent?
A. Yes.
Q. And Washington Energy's then would exceed 100 percent?
A. Since we had a loss, yes, for the 12-month period.
Q. Mr. Torgerson, do you know if Washington Energy Company has made any studies of its return -- of its return on investment in Cabot that would likely be produced over the next five years?
A. No, we have not.
Q. You haven't?
A. We have not.
Q. Do you know what the 1997 capital expenditure requirements of NewCo will be other than its expenditures for electric and gas operations?
A. Well, I know for at least the Washington Energy subsidiaries it will be virtually zero. There won't be much in the way of capital expenditures going forward, I mean, once the companies are merged. '96, I think the projection for capital is fairly

minimal. I mean, less than -- it's probably in the one million range. I mean, it's just not much. We're expensing everything for the coal and railroad at this point. Washington Energy Services has almost none so I think it's less than a million.

Q. Do you expect any capital expenditures for Cabot?

A. No. We have an investment. We just hold the stock. We do not have to make any investments.

Q. And so which of the unregulated subs do you expect capital expenditures for?

A. Like I said, the only one would be Washington Energy Services and it's very small. I don't know if it's even $100,000. We just don't have any capital needs there. Thermal Energy and ThermaRail, as I said, we're expensing everything.

JUDGE SCHAER: Mr. Cedarbaum, about how much more do you have?

MR. CEDARBAUM: I think I can probably be done in about 15 minutes.

JUDGE SCHAER: Let's proceed. Thank you.

Q. Washington Natural's current authorized rate of return on equity is about 11 to 11 and a quarter percent; is that right?

A. Yes.

Q. Is it correct that Washington Natural Gas in 1995 didn't earn that return?

A. That's correct.

Q. Why didn't it?

A. Well, first off, we did not have the benefit of -- for '95 you're talking about?

Q. Yes.

A. We didn't have the benefit of the rate increase which we got in May of '95. We had very adverse weather during fiscal '95. It was -- if I remember right it was considerably warmer than normal. So those were probably two of the factors. Also, the other things that we have are we didn't have the benefit of the Commission's line extension policy, which is going to help us going forward, so we had expenses going up. We did have some re-engineering costs and we hadn't gotten the benefit of the re-engineering, that's a timing issue, but so there are a lot of factors why we didn't earn it.

Q. Assuming normal weather and the implementation of all of these factors that you've just been discussing, would that allow Washington Natural Gas to earn its authorized return?

A. For right now?

Q. Yeah.

A. I would say we probably would not. One of the things we saw -- we've seen this year there have been significant schedule switching among commercial customers where they've gone to a lower rate tariff, which has had an impact on our earnings. We're still seeing our costs going up even though we're doing everything we can to keep them down, so I would not expect us to earn our allowed rate of return right now. It will be a lot closer than it was in the past but I don't think we earn it.

Q. Is it correct that this Commission doesn't have any control over Washington Energy Company's nonregulated -- excuse me -- over the earnings of Washington Energy Company's nonregulated operations?

A. I believe that it's true, yes.

Q. Would you accept subject to check that in order for Washington Natural Gas in fiscal year '95 to earn its authorized return on equity that it would need about $17 million more revenue?

A. For '95?

Q. Yes.

A. Well, I would have to look at it. Yeah, I mean, subject to check.

Q. And just to specify the subject to check, the $17 million was not revenue but earnings. Would you accept that subject to check?

A. Subject to check, sure. On a Commission basis, right?

JUDGE SCHAER: Mr. Cedarbaum, was that on a Commission basis?

MR. CEDARBAUM: Yes.

Q. It would be how much more they would actually have to earn to reach their authorized return. I think whether it's on a Commission stated basis wouldn't matter.

A. We can give you the calculations. We do provide that report to the Commission semi-annually.

Q. Well, let's leave it subject to check and you can check it.

Would you also accept subject to check that at fiscal year end 1995 Washington Energy Company had 24 million shares of common stock outstanding?

A. Washington Energy Company?

Q. Yes.

A. They had approximately 24 million, yes.

Q. And at one dollar per share current dividend -- and after current one dollar per share dividend requirement it would then have to earn $24 million at least in order to meet its dividend requirement; is that right?

A. On an earnings basis. Keep in mind we have a dividend reinvestment plan so it's not all cash that has to go back out but on an earnings basis, yes.

Q. And we previously discussed out of your exhibit that Washington Energy Company lost $41 million in fiscal year '95; is that right?

A. Yes.

Q. Just a few more questions for you. On page 43 of your testimony --

A. Of the exhibit?

Q. I'm sorry, of the exhibit. I don't want to get to the specifics about it, but generally speaking, there's a discussion entitled "discounted cash flow analysis" and a description of how Morgan Stanley applied a discounted cash flow analysis for fiscal '95 through 2004 to calculate per share values for Washington Energy Company and Puget; is that right?

A. Yes.

Q. And at the bottom of this page and the top of the next page Morgan Stanley applied a similar procedure for discounting dividend payment; is that right?

A. Yes. They did a discounted dividend analysis.

Q. And in your opinion was that an appropriate analysis for them to do in terms of preparing this prospectus?

A. They did not do this for the prospectus. They did it for their fairness opinion they were going to give to Puget Power's board.

Q. And that was an appropriate thing for them to do for that purpose?

A. It was one of many analyses they did and it's one way to look at it, certainly. They did a lot of analysis and these were only two of the things they looked at.

Q. On page 47, there's a similar type of discussion with regard to Goldman Sachs. Do you see that?

A. Yes. There's a dividend discount analysis. Number of different analyses on that page.

Q. And you felt in terms of giving their fairness opinion that this was also one analysis of whatever analysis they did that was appropriate for them to do?

A. They have to do their analysis for their fairness opinion. They determined what they need for their fairness opinion, and it is appropriate for them to do that, certainly, along with all the other analysis they did.

Q. And finally on page 3 of your testimony, you reference the applicable waiting period under the Hart-Scott-Rodino Antitrust Improvements Act. Do you know when that waiting period ends?

A. We filed -- we made the Hart-Scott-Rodino filing July 15 so it would be 30 days from that point in time.

Q. What was the date?

A. July 15. That would assume there's no second request or other information we would have to provide.

JUDGE SCHAER: Is that of this year?

THE WITNESS: Yes. I'm sorry. July 15, '96.

Q. I'm not sure if that filing has been requested in a data request or not yet, but let me ask as the next record requisition for you to provide us with a copy of your filing under the Hart-Scott-Rodino Act.

A. We can do that but that would also have to be confidential.

Q. Okay. And then on a continuing basis for you to provide us with copies of information that you requested from the FTC.

A. It's actually the Department of Justice that I believe has it, but --

MR. CEDARBAUM: Thank you. Those are all my questions.

JUDGE SCHAER: That would be record request No. 10.

(Record Requisition 10.)

JUDGE SCHAER: Our plan going forward is to reconvene this hearing at 9:00 tomorrow morning. The first order of business will be to take the testimony of Richard R. Sonstelie and we will then proceed to take the testimony of William P. Vititoe. After those two witnesses are concluded we will then continue with Mr. Torgerson. Please be prepared first thing in the morning to distribute any exhibit that you may have for Mr. Sonstelie.

Is there anything else that needs to come before us this afternoon? Hearing nothing we are off the record.

(Hearing adjourned at 5:12 p.m.)