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September 26, 2006

Carole J. Washburn, Secretary
Washington Utilities and Transportation Commission
1300 S. Evergreen Park Dr. SW
P. O. Box 47250
Olympia, Washington 98504-7250

Re: *Puget Sound Energy General Rate Case*
Docket Nos. UE-060266 and UG-060267 Consolidated

Dear Ms. Washburn:

Enclosed for filing in the above-referenced docket are the original and 16 copies Commission Staff's response to Bench Request No. 1.

Sincerely,

ROBERT D. CEDARBAUM
Senior Counsel

Enclosures
RDC:klg
cc: Parties



WASHINGTON UTILITIES AND TRANSPORTATION COMMISSION STAFF
RESPONSE TO BENCH REQUEST

DATE PREPARED: September 20, 2006
DOCKET: UE-060266 & UG-060267
REQUESTER: Bench

WITNESS: James M. Russell
RESPONDER: Staff

BENCH REQUEST NO 1:

Please explain the differences in the calculation of Mr. Valdman's "actual ROE of approximately 8%" (Exhibit No. 457 at 26:9) and Mr. Russell's "achieved rate of return" of 10.14% on equity (Exhibit No. 521 at 22:15).

RESPONSE:

The primary reason for the difference in ROEs is that Mr. Russell addresses the Company's regulated operations as reflected in Commission Basis reports, while Mr. Valdman includes unregulated operations as reflected in the Company's financial statements.

Mr. Valdman's "actual ROE of approximately 8%" is a 4-year average for the calendar years 2002 through 2005. It is derived from Puget Energy's annual reports to shareholders, adjusted for the Tenaska disallowance. The specific pages from the annual reports are contained in Exhibit 465 and show Puget Sound Energy's consolidated (regulated and non-regulated) income statements and capital structures. The calculation of Mr. Valdman's 8% ROE is shown in Exhibit No. 465 and is reproduced on page 1, lines 1-7 of the Attachment.

In contrast, Mr. Russell's test period "achieved rate of return" of 10.14% on equity supporting rate base is derived from Puget Sound Energy's Electric and Gas regulated net operating income and rate base (investments) shown in Exhibit Nos. 522 and 524, and Puget Sound Energy's average capital structure for the indicated years. Page 1 of the Attachment, lines 14-22 calculate the "Commission Basis" implied ROE for the same 4-year period covered by Mr. Valdman and calculated in the same manner as the test period 10.14% reflected in Mr. Russell's testimony. Mr. Russell's ROE figures do not reflect removal of the Tenaska disallowance. Page 2 of the Attachment is page 2 of Exhibit No. 525 supporting Staff's ROE calculations for the calendar years 2002 through 2005. Page 3 of the Attachment includes the capital structure and cost rates used to determine the actual "Test Period" ROE of 10.14%. Page 4 of the Attachment comes from the Company's response to Staff Data Request No. 49 and is the source for the test period capital structure shown on page 3. The amount of equity supporting regulated operations is reflected in the calculation of the Investor Supplied Working Capital (Working Capital) adjustment to rate base and is shown in Exhibit Nos. (KRK-G3) and (JHS-E3)

After reviewing the Company's response to Bench Request No. 1 it is appropriate to reflect in Staff's ROE figures both an interest synchronization adjustment and the Tenaska disallowance (March Point disallowance is not reflected). These adjustments are reflected on lines 23 and 24

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of page 1 of the Attachment. The interest synchronization adjustments come directly from the Commission Basis reports for the indicated years. The interest synchronization adjustments reduce the Test Period ROE from 10.14% to 10.03%, as shown on line 26.

ATTACHMENT

Staff Response to Commission Bench Request No. 001

PSE Calculation of Return on Equity
(PSE Consolidated)

(\$000)

	12/31/01	12/31/02	12/31/03	12/31/04	12/31/05	4 Yr-Avg
1 PSE Equity	\$1,267,654	\$1,426,121	\$1,535,469	\$1,592,433	\$1,986,621	\$1,550,290
2 Avg Equity		\$1,346,888	\$1,490,795	\$1,573,951	\$1,789,527	
3 Net Income	\$101,117	\$114,735	\$114,735	\$126,192	\$146,769	\$122,203
4 Tenaska after tax impact	\$0	\$0	\$0	(\$28,210)	(\$2,665)	\$129,922
5 Income excluding Tenaska Disallowances	\$101,117	\$114,735	\$114,735	\$154,402	\$149,434	
6 Actual ROE	7.5%	7.7%	7.7%	8.0%	8.2%	7.9%
7 ROE with Tenaska adjusted out	7.5%	7.7%	7.7%	9.8%	8.4%	8.4%
8 Allowed ROE	11.0%	11.0%	11.0%	11.0%	10.4%	10.8%
9 Through 2/17/05						
10 Beginning 2/17/05						
11 Blended ROE						
12 Under Earning	-3.5%	-3.3%	-3.3%	-3.0%	-2.2%	-3.0%
13 Under Earning excluding Tenaska	-3.5%	-3.3%	-3.3%	-1.2%	-2.0%	-2.5%

Source:

Annual Rpt (2005: pg 88; 2003: pg 81; 2001 pg 71)

Annual Report (2005: pg 85; 2003: pg 79)
Annual Report (2005: pg 115)

Comments:

Avg: Around 8%

Avg: Approximately 250 basis points

Staff Calculation Return on Equity
(Regulated Electric and Gas Operations)

(\$)

	12/31/02	12/31/03	12/31/04	12/31/05	2002-2005 Sources:	Test Period	Test Period Source:
14 Equity Supporting Electric and Gas Rate Base:							
15 Rate Base (AMA)	\$3,657,685,402	\$3,533,438,185	\$3,560,830,848	\$3,691,943,579	JMR-5, page 2, lines 2, 12's and 22	\$3,692,823,186	JMR-2
16 Equity Ratio (AMA)	33.02%	37.46%	39.81%	40.06%	JMR-5, page 2, lines 9 and 19's	40.55%	
17 Equity Supporting Rate Base	\$1,207,932,369	\$1,323,452,036	\$1,417,595,138	\$1,478,942,954		\$1,497,437,740	
18 "Commission Basis" Electric and Gas Net Income:							
19 Net Operating Income	\$290,986,270	\$295,659,351	\$285,258,405	\$299,525,242	JMR-5, page 2, lines 1, 11's and 21	\$303,778,102	
20 Implied Interest Expense	172,416,526	155,480,208	149,177,217	154,604,086	Line 30 below	151,777,647	
21 Preferred Dividends	7,303,020	4,971,208	196,203	133,210	Line 34 below	138,910	
22 Net Income Available for Common	\$111,266,724	\$135,207,935	\$135,884,986	\$144,787,946		\$151,861,544	
23 "Commission Basis" Implied ROE	9.21%	10.22%	9.59%	9.79%		10.14%	
24 Interest Synchronization (Per Commission Basis Reports)							
25 Add Back - Tennessee Dissallowance	-\$7,270,111	-\$7,609,468	-\$6,664,298	-\$4,002,028		-\$4,667,596	Prorated 2004 & 2005
26 Adjusted NOI	\$103,996,613	\$127,598,467	\$157,430,688	\$143,450,918		\$150,193,949	
27 Adjusted "Commission Basis" Implied ROE	8.61%	9.64%	11.11%	9.70%		10.03%	
28 Implied Interest Expense:							
29 Rate Base (AMA)	3,657,685,402	3,533,438,185	3,560,830,848	3,691,943,579	Line 15 above	3,692,823,186	
30 Weighted Cost of Debt (LT, ST, Trust Preferred)	4.71%	4.40%	4.19%	4.19%	JMR-5 sum of lines 5,6&7 (eg. 2002)	4.11%	
31 Interest Expense	172,416,526	155,480,208	149,177,217	154,604,086		151,777,647	
32 Preferred Dividends:							
33 Rate Base (AMA)	3,657,685,402	3,533,438,185	3,560,830,848	3,691,943,579	Line 15 above	3,692,823,186	
34 Weighted Cost of Preferred	0.20%	0.14%	0.01%	0.00%	JMR-5 lines 8 and 18's	0.00%	
35 Preferred Dividends	7,303,020	4,971,208	196,203	133,210		138,910	

2002 Utility Operations: (3.1% Colder than normal)

Actual Results of Operations (Per Exhibit 56, Docket 040640)		Electric	Gas	Total
1	Net Operating Income	212,276,159	78,710,111	290,986,270
2	Rate Base	2,588,830,450	1,068,854,952	3,657,685,402
3	Overall Rate of Return	8.20%	7.36%	7.96%
4	Implied Utility Operations ROE	9.95%	7.42%	9.21%

PSE "Utility" Capital Structure (Per Exhibit 57, Docket 040640)		Structure (%)	Rate (%)	Weighted Cost	
	AMA Amount				
5	Short Term Debt	131,839,500	3.25%	2.77%	0.09%
6	Long Term Debt	2,180,798,445	53.76%	7.42%	3.99%
7	Trust Preferred	300,000,000	7.40%	8.58%	0.63%
8	Preferred Stock	104,099,400	2.57%	7.78%	0.20%
9	Common Stock	1,339,577,881	33.02%	9.21%	3.04%
10	Total	\$4,056,315,226	100.00%		7.96%

2003 Utility Operations: (5.6% Warmer than normal)

Actual Results of Operations (Per Exhibit 56, Docket 040640)		Electric	Gas	Total
11	Net Operating Income	213,474,475	82,184,876	295,659,351
12	Rate Base	2,492,964,158	1,040,474,027	3,533,438,185
13	Overall Rate of Return	8.56%	7.90%	8.37%
14	Implied Utility Operations ROE	10.74%	8.97%	10.22%

PSE "Utility" Capital Structure (Per Exhibit 57, Docket 040640)		Structure (%)	Rate (%)	Weighted Cost	
	AMA Amount				
15	Short Term Debt	52,290,500	1.31%	8.80%	0.12%
16	Long Term Debt	2,092,562,193	52.37%	7.02%	3.68%
17	Trust Preferred	282,718,750	7.08%	8.60%	0.61%
18	Preferred Stock	71,427,213	1.79%	7.87%	0.14%
19	Common Stock	1,496,527,416	37.46%	10.22%	3.83%
20	Total	\$3,995,526,072	100.00%		8.37%

2004 Utility Operations: (7.8% Warmer than normal)

Actual Results of Operations (Per Comm. Basis Report)		Electric	Gas	Total
11	Net Operating Income	211,309,050	73,949,355	285,258,405
12	Rate Base	2,490,635,488	1,070,195,360	3,560,830,848
13	Overall Rate of Return	8.48%	6.91%	8.01%
14	Implied Utility Operations ROE	10.77%	6.82%	9.59%

PSE "Utility" Capital Structure (Per Comm. Basis Report)		Structure (%)	Rate (%)	Weighted Cost	
	AMA Amount				
15	Short Term Debt	88,715,833	2.18%	5.46%	0.12%
16	Long Term Debt	2,083,124,804	51.09%	6.81%	3.48%
17	Trust Preferred	280,250,000	6.87%	8.60%	0.59%
18	Preferred Stock	1,889,400	0.05%	11.89%	0.01%
19	Common Stock	1,623,129,995	39.81%	9.59%	3.82%
20	Total	\$4,077,110,032	100.00%		8.01%

2005 Utility Operations: (6.4% Warmer than normal)

Actual Results of Operations (Per Comm. Basis Report)		Electric	Gas	Total
21	Net Operating Income	221,820,052	77,705,190	299,525,242
22	Rate Base	2,511,214,961	1,180,728,618	3,691,943,579
23	Overall Rate of Return	8.83%	6.58%	8.11%
24	Implied Utility Operations ROE	11.59%	5.97%	9.79%

PSE "Utility" Capital Structure (Per Comm. Basis Report)		Structure (%)	Rate (%)	Weighted Cost	
	AMA Amount				
15	Short Term Debt	134,520,584	3.17%	5.88%	0.19%
16	Long Term Debt	2,148,818,333	50.66%	6.86%	3.48%
17	Trust Preferred	257,229,167	6.06%	8.67%	0.53%
18	Preferred Stock	1,889,400	0.04%	8.10%	0.00%
19	Common Stock	1,699,118,174	40.06%	9.79%	3.92%
20	Total	\$4,241,575,658	100.00%		8.11%

Staff Response to Commission Bench Request No. 001

Docket No. 060266 & 060267

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REVISED 8/8/06

Results of Operations - Actual (Per Comm. Basis Report)

	Electric	Gas	Total
21 Net Operating Income	231,281,640	72,496,462	303,778,102
22 Rate Base	2,513,582,619	1,179,240,567	3,692,823,186
23 Overall Rate of Return	9.20%	6.15%	8.23%
24 Implied Utility Operations ROE	12.55%	5.02%	10.14%

Source:

JMR-2, page 1, line 34 and JMR-4, page 1, line 33
 JMR-2, page 1, line 36 and JMR-4, page 1, line 35

PSE "Utility" Capital Structure (AMA 9/05)

	AMA Amount	Structure (%)	Rate (%)	Weighted Cost
15 Short Term Debt	121,272,125	2.87%	5.72%	0.16%
16 Long Term Debt	2,123,253,188	50.20%	6.77%	3.40%
17 Trust Preferred	267,854,167	6.33%	8.64%	0.55%
18 Preferred Stock	1,889,400	0.04%	8.42%	0.00%
19 Common Stock	1,714,943,095	40.55%	10.14%	4.11%
20 Total	\$4,229,211,975	100.00%		8.23%

PSE Response To Staff Data Request No. 49, page entitled:

"Utility Capital Structure
 Cost of Capital and Rate of Return
 As of September 30, 2005"