BEFORE THE WASHINGTON
UTILITIES AND TRANSPORTATION COMMISSION

WASHINGTON UTILITIES AND TRANSPORTATION COMMISSION, Complainant, vs. PUGET SOUND ENERGY, INC., Respondent.	)	Docket No. UE-060266 Docket No. UG-060267 SEATTLE STEAM COMPANY'S POST-HEARING BRIEF

I. INTRODUCTION AND SUMMARY

1 Seattle Steam Company's primary concern in this matter is whether the rates charged to Puget Sound Energy's ("Puget's") "interruptible" customers, particularly under Schedule 57,[1] but also in all interruptible classes (Schedules 85, 86, 87 and 57), are "just, fair, reasonable and sufficient" when viewed in relationship to the rates charged to other PSE customers and in relationship to the cost of service to interruptible customers. RCW 80.28.010(1).

2 The Commission has been presented with two alternatives with respect to Schedules 85, 86, 87 and 57 – Puget's proposal and the proposal set forth in the Joint Testimony of Ms. Steward, Mr. Lazar and Mr. Schoenbeck ("Joint Testimony") and their accompanying exhibits. Seattle Steam is somewhat conflicted between the two, because the Joint Testimony would result in a slight reduction in its annual bill, while Puget's

[1] Schedule 57 customers are responsible for acquiring their own natural gas on the open market and receive interruptible transportation service for that gas from Puget.

proposal results in an increase. Ultimately, however, Seattle Steam must urge the Commission to accept Puget's proposal. It is founded on sound rate-making principles, while the Joint Testimony does not appear to be. As one of Puget's largest, if not its largest gas customer, it is more important to Seattle Steam that Puget's rates be based on sound rate-making principles than that its bill be slightly reduced in this proceeding.

3 Seattle Steam has three primary concerns about the Joint Testimony.

- First, the Joint Testimony does not purport to be based on its own cost of service study. It claims to be based on a Puget data request response concerning the outcome of a "commission basis" cost of service study, referring to a twelve year old Commission decision.[2] As discussed below, it is not at all clear that the Joint Testimony is based on the "commission basis" cost of service study. In any event, Puget's current cost of service study appears to have appropriately updated the cost of service study to reflect the current cost environment in which Puget now does business. Puget's argument that a Commission decision from more than a decade ago should be updated to reflect its current cost environment is compelling.
- Second, for each interruptible schedule the Joint Testimony asks for a larger increase than Puget sought. It is undisputed that the interruptible classes (with the possible exception of Schedule 87), currently pay significantly more than they cost Puget, and have a parity ratio well above 1. (A parity ratio of 1 means a customer class pays in rates what it costs the company to serve it. A parity ratio greater than 1 means the class pays more than it costs and thereby subsidizes other classes. A parity ratio below 1 means a class is being subsidized.) The Joint Testimony

[2] *In re Washington Natural Gas*, (UG-940814, "WNG") 1995 Wash. UTC LEXIS 19.

would therefore increase the disparity more than Puget's proposal. Arguably a customer class with a parity level significantly greater than 1 should have no rate increase, or a rate decrease. The argument for rate classes that are already subsidizing other rate classes to nonetheless get an increase in this proceeding is apparently that it is politically unacceptable to have some classes get increases while others are exempt from any increase. Assuming merely *arguendo* that is a valid reason to further increase the parity ratios of the interruptible classes, there is no justification for assigning a larger increase to the interruptible classes than Puget has requested.

- Third, the Joint Testimony proposes to fix a dollar amount of increase for the interruptible customers ($576,163 total). It then proposes that only the firm customers benefit from any decision the Commission may make to reduce the total revenue requirement, and resulting total rate increase, from the $39.2 million increase Puget seeks. Seattle Steam expresses no opinion about the total rate increase to which Puget should be entitled. The Joint Testimony offers no reason, however, why a reduction in Puget's revenue requirement should not be shared among all customer classes.

II. PUGET'S COST OF SERVICE STUDY IS APPROPRIATE AND SHOULD BE ADOPTED

4 In a series of decisions, the Commission has recognized that a proper cost of service study is an important step in establishing rate spread and rate design for rates that are "just, fair, reasonable and sufficient." In the 1992 *Washington Water Power* decision (UG-901459), 1992 Wash. UTC LEXIS 27 at 7, the Commission described the use of cost of service studies: "Embedded cost of service continues to provide an important

means for comparing the contributions made by different customer classes to the company's overall revenue requirement. Therefore, any request for rate changes should be accompanied by an embedded cost-of-service study." The Commission has recognized that cost of service for any particular customer class or all classes is not the sole determinant of proper rates. Nonetheless, it is the starting point, and wide disparities between the cost of providing service and the rates charged for the service necessarily cast doubt on whether the rates are just, fair, reasonable or sufficient.

5 A great deal of the testimony in this proceeding has related to the investments Puget has been and continues to be forced to make in order to meet the demands of growth in the area and to replace cast iron and bare steel distribution lines. One "given" about Puget's investments, however, is that they are not made to serve its interruptible customers. Puget Gas Rule No. 23 provides:

> PSE's gas distribution system and gas supply resource portfolio are designed to meet the needs of firm [not interruptible] customers. Interruptible service is made available, as long as, in PSE's sole judgment and discretion, any one of the following conditions exists:
>
> a. distribution capacity and/or contracted gas supply resources are not needed to meet the expected demand of firm customers, or
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> b. any excess distribution capacity and/or supply resource may be used by interruptible customers without jeopardizing continuous service to firm customers, or
>
> c. maintenance, repair or operational conditions of PSE's gas distribution system do not prevent or limit service to interruptible customers.

6 In discovery, Seattle Steam asked Puget to list all facilities it anticipates it will be required to build over the next five years in order to be able to continue to provide interruptible service under Schedule 57 (Seattle Steam's current rate schedule). Puget responded in part:

> Pursuant to Rule 23, PSE's facility plan over the next five years is to continue to provide firm service to its firm customers. Rule 23 only allows for continued interruptible service until the firm demand utilizes the capacity of the designed facilities.

7 Exhibit No. 498 (SG-2), p. 1. In short, Puget's policy is to build no facilities to meet the needs of interruptible customers. Exhibit No. 497, p. 4-5.

8 Puget based its proposed rates on a detailed cost of service study. Ex. No. 38, pp. 8-24. The principal difference between Puget's study and the "Commission basis" for a cost of service study as determined in the 1994 *WNG* decision, appears to be that Puget used the "design day" to determine the allocation of distribution main costs among customer classes. Ex. 38, pp. 10-13. The reason for using the design day is that the design day is the driver for the Company's actual investment. In the Commission's 1994 *WNG* decision it proposed using the average peak day from the previous three years. If the Company were to install its distribution mains based on the average peak day of the previous three years, if those three years happened to be warmer than usual, its system would be inadequate to meet its firm demand during a colder than normal year. That would obviously be unacceptable.[3] Thus Puget's cost of service study here reflects its actual investments.

9 The Joint Testimony gives no reason for rejecting Puget's cost of service study other than, "it's not what the Commission said in 1994." The short answer is that in 1994 the company was not facing the need to make the kind of investments to serve growth that

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[3] One test of whether the average peak demand of the previous three years would be an acceptable basis for Puget's costs is whether the Commission would permit Puget to size its distribution system based on the average peak demands of the previous three years, knowing that the result would be that in any colder period, the system would be inadequate to meet firm demand. We assume the Commission would not approve that. If the assumption used in a cost of service study is not an assumption the Commission would permit if it were carried out in fact, then it presumably does not reflect the company's actual costs.

Puget is facing today. Today's cost of service study should be based on today's actual costs.

III. THE JOINT TESTIMONY OFFERS NO JUSTIFICATION FOR IMPOSING A LARGER RATE INCREASE ON EACH OF THE INTERRUPTIBLE CLASSES THAN PUGET ASKED FOR

10 The "parity," or revenue-to-cost ratios of the different customer classes, as determined by Puget's cost of service study, are set forth below:

Rate Class	Parity Ratio	Rate of Return
Residential (Schedules 23, 16, 53)	86%	6.1%
Commercial & Industrial (Schedules 31, 36, 51, 61)	85%	6.1%
Large Volume (Schedule 41)	114%	12.7%
Interruptible (Schedule *85)*	138%	19.3%
Limited Interruptible (Schedule 86)	167%	25.2%
Non-exclusive Interruptible (Schedule 87)	134%	17.8%
Transportation (Schedule 57)	165%	25%
Transportation Special Contracts	101%	9.9%
Compressed Natural Gas (Schedule 50)	2%	-16.2%
Rentals (Schedules 71, 72, 74)	56%	-7.9%

11 Ex. No. 38, p. 23. The parity ratios for the four interruptible classes are 138%, 167%, 134% and 165% respectively – significantly higher than any other class.[4]

[4] In Exhibit 586 the Joint Testimony says that the parity ratio for the four interruptible classes under Puget's cost of service study is 1.56, 1.89, 1.52 and 1.87 respectively, or significantly higher than Puget says it is. Although the joint witnesses do not explain the difference between Puget's testimony, and the Joint Testimony's characterization of Puget's testimony regarding parity ratios, the difference appears to be that Puget's cost of

12 Exhibit 586, p. 1 shows Puget's proposed increase and the Joint Testimony's proposed increase for the various classes. Their respective proposals for the interruptible classes is as follows:

	Margin Increase		Total Percent Increase	
	Puget proposal	Joint Testimony proposal	Puget proposal	Joint Testimony proposal
Interruptible (85)	$49,731	$108,572	0.36%	0.78%
Limited Interruptible (86)	$54,779	$104,536	0.30%	0.57%
Non exclusive Interruptible (87)	$57,744	$186,423	0.17%	0.61%
Transportation (57)[5]	$158,995	$176,632	1.43%	1.51%

Ex. 586, p. 1.

13 In each instance the Joint Testimony would assign a larger rate increase to the interruptible class than Puget asked for. Clearly if the revenue-to-cost ratio is already too high for these classes, increasing the amount of their margin increase will exacerbate the situation. Nor do the equities change, except perhaps for Schedule 87, if one relies on the Joint Parties characterization of the "commission basis" cost of service study. It also

service study presumed it needed increased revenue, while the parity ratios shown in Exhibit 586 assume current rates are adequate.

[5] As stated in the Introduction, Seattle Steam is conflicted about objecting to the Joint Testimony proposal because it would actually lower Seattle Steam's bill in the short term. It does that by assigning most of the increase to the first two blocks of monthly usage, while lowering the rates for the subsequent blocks. That means that the percentage increase for the smaller Schedule 57 users is higher and larger schedule 57 customers get a rate decrease. Exhibit No. 586, p. 11. For all we know, that may be "just, fair and reasonable" but it is not based on any cost of service study or other factual foundation that has been presented. As a result, it appears to be merely a way of keeping the peace with larger users. The difficulty with that approach for Seattle Steam is that long-term it will pay far more than it should if rates are not based on real costs, but rather are set at the highest level that it or other large customers will tolerate.

shows the parity ratio of Schedules 85, 86 and 57 as being higher than for any other class besides large volume (4) customers.[6] *Id.*

14 It is the opposite of just, fair, reasonable and sufficient to assign a greater rate increase to the interruptible classes than Puget requested. Those customer classes that already pay more than the cost of providing them with service. There is no justification for increasing the disparity between them and the other classes.

IV. THERE IS NO BASIS TO FIX THE RATE INCREASE FOR THE INTERRUPTIBLE CLASSES AND THEN SHARE THE "SAVINGS" FROM ANY REDUCTION IN REVENUE REQUIREMENT THE COMMISSION MAY ORDER SOLELY AMONG THE FIRM CUSTOMER CLASSES

15 The final and most inexplicable area in which Seattle Steam objects to the Joint Testimony is that the Joint Testimony allocates a fixed $576,000 to the interruptible classes, and then proposes that any "savings" that are derived from the Commission's decision about the total Puget revenue requirement should be shared exclusively among the firm customers.

16 Seattle Steam expresses no opinion as to the total revenue requirement that the Commission should establish for Puget. Much of the testimony in this proceeding has related to what capital structure and what return on equity are needed to attract the capital Puget needs in order to make the investments it is facing. Like every other company or individual, Seattle Steam wants the rates set as low as possible. Perhaps unlike some, however, it also wants Puget to be financially strong enough so that it can make favorable long-term contracts. Seattle Steam trusts this Commission will establish the capital

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[6] Again the Joint Testimony's characterization of the parity ratio of the interruptible classes under the "commission basis" cost of service study does not match what Puget says the parity ratio of the interruptible classes is under the commission basis. Again, the Joint Testimony does not explain the differences. *Compare*, Ex. 586, p. 1 with Ex. 581, p. 1, line 18.

structure and return on equity for Puget wisely. Wherever the Commission sets those numbers, however, the rates for all classes should be adjusted accordingly. Exhibit 586 is premised on the total increase to Puget's margin being $39.2 million. Ex. No. 586, p. 1. If the total increase is less, then all classes should share in the reduction.

V. CONCLUSION

17 There may be a basis for the Joint Testimony's proposal for gas rate design and rate spread, but if so, they have not provided it. The Commission's decision needs to be based on a factual foundation. Puget has provided such a foundation for their proposed gas rate design and rate spread, and as such it is the only proposal that can be adopted.

DATED this 31st day of October, 2006.

GRAHAM & DUNN PC

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