

**EXHIBIT NO. ___(MRM-5)
DOCKET NO. UE-072300/UG-072301
2007 PSE GENERAL RATE CASE
WITNESS: MATTHEW R. MARCELIA**

**BEFORE THE
WASHINGTON UTILITIES AND TRANSPORTATION COMMISSION**

**WASHINGTON UTILITIES AND
TRANSPORTATION COMMISSION,**

Complainant,

v.

PUGET SOUND ENERGY, INC.,

Respondent.

**Docket No. UE-072300
Docket No. UG-072301**

**FOURTH EXHIBIT (NONCONFIDENTIAL) TO THE
PREFILED REBUTTAL TESTIMONY OF
MATTHEW R. MARCELIA
ON BEHALF OF PUGET SOUND ENERGY, INC.**

JULY 3, 2008

BEFORE THE WASHINGTON UTILITIES AND TRANSPORTATION COMMISSION

**Docket Nos. UE-072300 and UG-072301
Puget Sound Energy, Inc.'s
2007 General Rate Case**

PUBLIC COUNSEL DATA REQUEST NO. 671

PUBLIC COUNSEL DATA REQUEST NO. 671:

Regarding Exhibit No. ____ (JHS-4), page 1, "Adjusted Results of Operations";
Workpapers of John Story 4.04E; PSE Response to Staff Data Request No. 61; and,
PSE Response to Public Counsel Data Request No. 499:

The following electric results are obtained before the correction noted in Public Counsel
Data Request No. 499 (rounded):

| | |
|---------------------------------|---------------|
| 1. Net operating Income: | \$175,600,500 |
| 2. Interest (WCoD x RB) | \$123,610,700 |
| 3. Income Taxes (net) | \$52,425,300 |
| 4. Taxable income: (1)-(2)+(3) | \$104,415,100 |
| 5. Effective tax rate (3) / (4) | 50.21% |

Considering the normalization principles of ratemaking, please explain in detail and
provide a specific reconciliation of all reasons (including amounts) as to why PSE's
claimed effective Federal Income Tax Rate for ratemaking is in excess of 50% (slightly
less after consideration of correction in Public Counsel Data Request No.499), given the
statutory rate of 35%.

Response:

Attached as Attachment A to Puget Sound Energy, Inc.'s ("PSE") Response to Public
Counsel Data Request No. 671, please find a copy of the summary page of Third
Exhibit to the Prefiled Direct Testimony of John H. Story, Exhibit No. ____ (JHS-4), as
reference.

Attached as Attachment B to PSE's Response to Public Counsel Data Request No. 671,
please find a copy of Mr. Story's workpaper entitled "4.04E Federal Income Tax.xls",
Determination of Tax tab.

In general, PSE's flow-through items are reversing, which causes the effective tax rate
to exceed 35%. PSE has several flow-through items, which can be found in Attachment
B to PSE's Response to Public Counsel Data Request No. 671, in the "Adjustments –

Flowthru" section of the spreadsheet. Please see PSE's Response to Public Counsel Data Request No. 061 for further description of these flow-through items.

It might appear that the effective tax rate from actual operations is relatively close to the statutory rate of 35% as calculated in Attachment B to PSE's Response to Public Counsel Data Request No. 671. However, once non-rate case items are removed (e.g., production tax credits, which are the largest and which are processed in a rider mechanism), the overall effective rate increases. The implied effective tax rate after rate case adjustments is 40.5% as calculated in Attachment B to PSE's Response to Public Counsel Data Request No. 671.

There are also a couple of adjustments that impact the effective tax rate. Please see Adjustment 4.32 (Regulatory Assets and Liabilities - Tenaska Flow Thru) and Adjustment 4.33 (Depreciation Study) for such adjustments.

In addition to flow through tax adjustments, lower earnings further increase the effective tax rate. Applying the effective tax rate calculation to "After Rate Increase" would result in the following (see Attachment A PSE's Response to Public Counsel Data Request No. 671 for more information):

| | |
|-------------------------------|---------------|
| 1. Net Operating Income | \$284,238,477 |
| 2. Interest* | 127,758,075 |
| 3. Income Tax(net) | 110,922,648 |
| 4. Taxable Income (1)-(2)+(3) | 267,403,050 |
| 5. Effective Tax Rate (3)/(4) | 41.48% |

*Interest based on the proforma interest calculation from Adjustment 4.05, line 6.

As stated in the PSE's Response to Public Counsel Data Request No. 499, PSE's original filing in this proceeding used an incorrect number from Attachment B to PSE's Response to Public Counsel Data Request No. 671 for the Federal Income Tax Adjustment, line 9, page 4.04 of the Third Exhibit to Mr. Story's Prefiled Direct Testimony, Exhibit No.__(JHS-4). The total tax should have been \$72,349,599 instead of \$74,688,396, resulting in \$2,338,797 reduction to federal income tax. Please see page 2 of Attachment B to PSE's Response to Public Counsel Data Request No. 671 for details. Applying the \$2,338,797 reduction to federal income tax to the "After Rate Increase" from the original filing would result in 40.6% effective tax rate. This correction was included in PSE's supplemental filing on April 14, 2008.

**ATTACHMENT A to PSE's Response to
Public Counsel Data Request No. 671**

**PUGET SOUND ENERGY-ELECTRIC
 RESULTS OF OPERATIONS
 FOR THE TWELVE MONTHS ENDED SEPTEMBER 30, 2007
 GENERAL RATE INCREASE**

| LINE NO. | ACTUAL RESULTS OF OPERATION | TOTAL ADJUSTMENTS | ADJUSTED RESULTS OF OPERATIONS | REVENUE REQUIREMENT DEFICIENCY | AFTER RATE INCREASE |
|----------|--------------------------------------|-------------------|--------------------------------|--------------------------------|---------------------|
| 1 | <u>OPERATING REVENUES:</u> | | | | |
| 2 | \$ 1,785,744,016 | \$ 51,122,909 | \$ 1,836,866,925 | \$ 174,482,512 | \$ 2,011,349,437 |
| 3 | 374,331 | (18,627) | 355,704 | 336,605 | 692,309 |
| 4 | 268,574,887 | (262,488,315) | 6,086,573 | | 6,086,573 |
| 5 | 43,280,356 | (5,100,752) | 38,179,604 | - | 38,179,604 |
| 6 | 2,097,973,590 | (216,484,784) | 1,881,488,806 | 174,819,117 | 2,056,307,923 |
| 7 | | | | | |
| 8 | <u>OPERATING REVENUE DEDUCTIONS:</u> | | | | |
| 9 | | | | | |
| 10 | <u>POWER COSTS:</u> | | | | |
| 11 | \$ 118,473,661 | \$ 68,709,004 | \$ 187,182,664 | \$ - | \$ 187,182,664 |
| 12 | 1,017,118,800 | (272,340,941) | 744,777,859 | | 744,777,859 |
| 13 | 65,628,548 | 4,137,061 | 69,765,609 | | 69,765,609 |
| 14 | (84,819,852) | 84,819,852 | (0) | | (0) |
| 15 | 1,116,401,157 | (114,675,024) | 1,001,726,133 | - | 1,001,726,133 |
| 16 | | | | | |
| 17 | \$ 79,069,006 | \$ 18,344,169 | \$ 97,413,175 | \$ - | \$ 97,413,175 |
| 18 | 6,532,375 | 3,815,356 | 10,347,731 | | 10,347,731 |
| 19 | 67,507,444 | 103,297 | 67,610,741 | | 67,610,741 |
| 20 | 37,171,867 | 2,163,664 | 39,335,530 | 586,070 | 39,921,600 |
| 21 | 9,736,024 | (7,655,879) | 2,080,145 | | 2,080,145 |
| 22 | 32,494,479 | (32,489,368) | 5,111 | | 5,111 |
| 23 | 76,980,894 | 4,863,912 | 81,844,807 | 349,638 | 82,194,445 |
| 24 | 160,277,383 | 15,231,526 | 175,508,910 | | 175,508,910 |
| 25 | 30,986,683 | 2,084,547 | 33,071,230 | | 33,071,230 |
| 26 | 5,380,486 | 19,546,385 | 24,926,871 | | 24,926,871 |
| 27 | (11,616,918) | 15,280,435 | 3,663,517 | | 3,663,517 |
| 28 | 887,595 | (887,595) | - | | - |
| 29 | 171,491,627 | (55,562,491) | 115,929,136 | 6,748,053 | 122,677,189 |
| 30 | (5,105,994) | (32,062,089) | (37,168,083) | 58,497,379 | 21,329,295 (a) |
| 31 | 67,629,351 | 21,964,002 | 89,593,353 | | 89,593,353 |
| 32 | \$ 1,845,823,459 | \$ (139,935,153) | \$ 1,705,888,306 | \$ 66,181,139 | \$ 1,772,069,446 |
| 33 | | | | | |
| 34 | \$ 252,150,131 | (76,549,631) | 175,600,500 | 108,637,978 | 284,238,477 (b) |
| 35 | | | | | |
| 36 | \$ 3,189,416,474 | \$ 115,682,173 | \$ 3,305,098,647 | \$ - | \$ 3,305,098,647 |
| 37 | | | | | |
| 38 | 7.91% | | 5.31% | | 8.60% |
| 39 | | | | | |
| 40 | <u>RATE BASE:</u> | | | | |
| 41 | \$ 5,564,169,427 | \$ 335,818,634 | \$ 5,899,988,061 | 1. Oper Inc (b) | 284,238,477 |
| 42 | (2,277,237,104) | (147,484,215) | (2,424,721,319) | 2. Int Adj: 4.05 | 127,758,075 |
| 43 | 313,382,560 | (61,810,849) | 251,571,711 | | |
| 44 | (432,609,629) | (10,841,397) | (443,451,026) | | |
| 45 | 95,493,209 | - | 95,493,209 | 3. Tax (c) = | 110,922,648 |
| 46 | (73,781,988) | - | (73,781,988) | | |
| 47 | \$ 3,189,416,474 | \$ 115,682,173 | \$ 3,305,098,647 | 4. Taxable Inc | 267,403,040 |
| 48 | | | | | |
| 49 | | | | | |

5. Effective Tax Rate (3/4) 41.48%

\$ - NOI Check

**ATTACHMENT B to PSE's Response to
Public Counsel Data Request No. 671**

**Puget Sound Energy
Federal Income Taxes
For Test Year Ended 09/30/2007**

Increase/(Decrease) Taxable Income

Operating Income

FIT in Operating Income

Interest Expense

Taxable Income

ADJUSTMENTS - Flowthru

Book Depreciation

Sec. 263A Costs - Capitalized Prop Tax

Cabot Gas Contract - Book Amortization

WNP 3 - Book Amortization

Electric Plant Acq. Adj. - Book Amort

Amortization of WUTC AFUDC

Colstrip Common Amort

ADR Dismantling Costs

Common Dismantling Costs

Tenaska - Tax Amortization

Tenaska - Book Amortization

Tax Depreciation Less Clearing

Tax Depreciation Less Liberalized

Tax Depreciation Less Normalized

Payroll Taxes Charged to Retirements

Bad Debt Excess Tax Expense

Reserve for Injuries and Damages-Elec

Depr on Post Surcharge CIAC

Total Adjustments - Flowthru

ADJUSTMENTS - Permanent

Meals - 50% Disallowed

§162(m) limitation

Total Adjustments - Permanent

ADJUSTMENTS - Normalized

Tenaska AFUDC (Net of Amortization)

Liberalized Depreciation

Normalized Depreciation

Loss on ACRS Property

Environmental Costs

Non-Qualified SERPs

Pension

Storm Damage Amort

CIAC Receipts (253-08)

Depr on Post Surcharge CIAC

White River Water Right

Horizon Payment

Colstrip Reclamation

Liability Reserve - Colstrip 1 & 2

Deferred Revenue - Connex

SAP Software Amortization

Canwest Gas Supply

Amortization of Reaquired Debt Expense

Costs Ded. to Bonds Redeemed in 2006

Cost of Removal - Normalized Portion

| ELECTRIC | | | |
|--------------------|-----------------|---------------------|---------------|
| Current | Deferred Debits | Deferred Credits | Pro Forma Tax |
| 252,150,131 | | | 252,150,131 |
| 62,523,357 | | | 62,523,357 |
| (136,226,387) | | | (136,226,387) |
| <i>178,447,101</i> | | <i>(b) = 35.03%</i> | |
| 150,278,207 | | | 150,278,207 |
| 1,991,934 | | | 1,991,934 |
| 2,962,000 | | | 2,962,000 |
| 3,526,905 | | | 3,526,905 |
| 37,000 | | | 37,000 |
| 1,409,678 | | | 1,409,678 |
| 706,995 | | | 706,995 |
| (4,767,933) | | | (4,767,933) |
| 141,196 | | | 141,196 |
| (14,333,083) | | | (14,333,083) |
| 19,434,500 | | | 19,434,500 |
| (275,087,254) | | | (275,087,254) |
| (153,011) | | | (153,011) |
| 149,308,249 | | | 149,308,249 |
| (463,958) | | | (463,958) |
| (416,071) | | | (416,071) |
| (343,750) | | | (343,750) |
| (15,887) | | | (15,887) |
| 34,215,716 | | | 34,215,716 |
| 401,064 | | | 401,064 |
| 331,535 | | | 331,535 |
| 732,599 | | | 732,599 |
| 3,977,251 | | (3,977,251) | - |
| 152,261 | (152,261) | | - |
| (149,308,249) | 149,308,249 | | - |
| (5,027,537) | 5,027,537 | | - |
| 632,771 | | (632,771) | - |
| 2,621,421 | | (2,621,421) | - |
| 150,426 | | (150,426) | - |
| (98,998,041) | 98,998,041 | | - |
| 43,083,133 | | (43,083,133) | - |
| (15,563,742) | 15,563,742 | | - |
| 745,076 | | (745,076) | - |
| 1,484,328 | | (1,484,328) | - |
| 370,522 | | (370,522) | - |
| (28,100) | 28,100 | | - |
| (1,140,122) | 1,140,122 | | - |
| 3,081,393 | | (3,081,393) | - |
| (3,797,508) | 3,797,508 | | - |
| 741,712 | | (741,712) | - |
| (2,205,003) | 2,205,003 | | - |
| (7,197,872) | 7,197,872 | | - |

Puget Sound Energy
Federal Income Taxes
For Test Year Ended 09/30/2007

Increase/(Decrease) Taxable Income
Vacation Pay
Cabot Gas Contract (IRS audit)
FAS 106 Ret. Med. & Life (ATL)
Virtual Right of Way
CLX Software Amortization
Fredonia Turbine Lease
Repair Allowance
Encogen Tax Depreciation
Encogen Book Depreciation & Amortization
Schedule 94 - BPA Residential Ex
Deductible Costs §263A
Total Adjustments - Normalized
Total Tax Differences

| ELECTRIC | | | |
|---------------|-----------------|------------------|---------------|
| Current | Deferred Debits | Deferred Credits | Pro Forma Tax |
| (570,582) | 570,582 | | - |
| (1,411,764) | 1,411,764 | | - |
| (1,292,262) | 1,292,262 | | - |
| 4,430,333 | | (4,430,333) | - |
| 10,383,581 | | (10,383,581) | - |
| (797,983) | 797,983 | | - |
| (12,271,010) | 12,271,010 | | - |
| (8,488,572) | 8,488,572 | | - |
| 6,897,579 | | (6,897,579) | - |
| (33,640,040) | | 33,640,040 | - |
| (750) | 750 | | - |
| (262,987,353) | 307,946,837 | (44,959,484) | 0 |
| (228,039,037) | 307,946,837 | (44,959,484) | 34,948,316 |
| | | | |
| (49,591,937) | 307,946,837 | (44,959,484) | 213,395,416 |
| (17,357,178) | 107,781,393 | (15,735,819) | 74,688,396 |
| | | | |
| | | (1,060,555) | (1,060,555) |
| | 1,036 | | 1,036 |
| | | (69,500) | (69,500) |
| | | (50,500) | (50,500) |
| | | (50,500) | (50,500) |
| | | (65,250) | (65,250) |
| | | | - |
| | | | - |
| | | (630,000) | (630,000) |
| | | (413,528) | (413,528) |
| 0 | 1,036 | (2,339,833) | (2,338,797) |
| | | | |
| (17,357,178) | 107,782,429 | (18,075,652) | 72,349,599 |
| (17,357,178) | 107,782,429 | (18,075,652) | 72,349,599 |

Taxable Income
Tax at 35%

WNP 3 Regulatory Tax Benefit
CIAC Post Surcharge Amortization
BEP Amortization
Fredonia Amortization
Colstrip 3 Amortization
Colstrip 4 Amortization
PTC Hopkins
PTC Wild Horse
Cabot Gas Contract
Excess Credits - Electric Depreciation
Subtotal

Total Tax

Total Tax 72,349,599 *Supplemental*
Tax at 35% 74,688,396 *Original*
Tax Adjustment 2,338,797