UG-950326

Dock UG-95_____
Exhibit __ (JTS-Testimony)

BEFORE THE WASHINGTON UTILITIES
AND TRANSPORTATION COMMISSION

PETITION FOR DETERMINING THE RATEMAKING TREATMENT OF CERTAIN SPECIAL CONTRACTS	)))	CASCADE NATURAL GAS CORPORATION DOCKET NO. UG-95____

PREPARED TESTIMONY OF JON T. STOLTZ

Q. Please state your name and address for the record.

A. Jon T. Stoltz, 222 Fairview Avenue North, Seattle Washington

Q. By whom are you employed and what is your title?

A. I am employed by Cascade Natural Gas Corporation ("Cascade" or the "Company") as Senior Vice President of Planning and Rates.

Q. Would you identify your responsibilities with the Company?

A. As Senior Vice President - Planning and Rates, I am responsible for the Special Studies and Rates Departments of Cascade. The Special Studies Department is responsible for the development of the Company's Integrated Least Cost Planning function. Least Cost Planning involves long range market

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forecasts, evaluation of the costs and availabilities of demand side and supply side resources to meet such forecasted markets, as well as the development of written Integrated Resource Plans for submittal before the Washington Utilities and Transportation Commission and the Oregon Public Utility Commission.

The Rate Department is responsible for the preparation of all rate related exhibits in "tracking" and general rate relief filings.

I am also the liaison for the Company with the state utility commissions of Washington and Oregon for all rate related matters. I have the responsibility of maintaining Cascade's tariffs. I also monitor Northwest Pipeline Corporation's ("Northwest" or the "Pipeline") rate applications and the intervening in such applications before the Federal Energy Regulatory Commission ("FERC") where necessary.

Q. Please describe your educational background and previous experience.

A. I am a graduate of the University of Texas at El Paso with a degree in electrical engineering. My post graduate studies include courses in utility economic,

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management and accounting.

Prior to joining Cascade, I was employed by El Paso Electric Company as a Rate Engineer with the title of Special Projects Engineer. My responsibilities while with El Paso Electric were quite similar to those rate analysts have with Cascade. My tenure with El Paso Electric was approximately three years.

Q. Have you previously sponsored testimony?

A. Yes, I have sponsored testimony before the Public Utility Commission of Oregon, before the Washington Utilities and Transportation Commission, before the New Mexico Public Utility Commission, and before FERC.

Q. What is the purpose of the Company's filing and your Testimony?

A. In the process of the Commission's review of Cascade's Petition for approval of its Special Contract with Longview Fibre Company ("Fibre"), in Docket UG-931386, the Company agreed to file a Petition for an Order to determine the ratemaking treatment of the Fibre Special Contract as well as the Special Contracts related to March Point Cogeneration Company ("March

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Point"), Encogen Northwest L.P. ("Encogen"), Tenaska Gas Co. ("Tenaska") and B. P. Exploration & Oil, Inc ("Tosco"). The purpose of this filing is to show the results of the revenues, expenses and the rate base of these five contracts (together the "Special Contracts") and the contribution toward overall cost of service the Special Contracts provide to the rest of the system. Cascade will also attempt to show other benefits Cascade and its other customers are receiving as a result of the Special Contracts.

Q. Do you sponsor any exhibits along with this testimony?

A. Yes. I have prepared or supervised the preparation of the following exhibits: Exhibit ___ (JTS-1), Special Contract's Revenue Requirements, which is a summary of the Statement of Operations and Rate of Return for these Special Contracts; Exhibit ___ (JTS-2), Embedded & Current Deliveries to the Industrial Hosts Customers; Exhibit ___ (JTS-3), Test Period Revenues and Therm Deliveries to the Special Contract Customers; Exhibit __ (JTS-4), Revenue Restatement of Tosco as Required By WUTC Order in Docket No. UG-930511; and Exhibit ___ (JTS-5), Special Contracts'

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Chronology of Events.

Q. Please describe Exhibits ___ (JTS-1).

A. Exhibit ___ (JTS-1) summarizes the Special Contracts' impact on the Statement of Operations for Cascade's State of Washington service area for the calendar year of 1994, on a per books, restated and pro forma basis. The analysis was performed in a similar manner to the approach Cascade would use in a typical general rate case application. This Exhibit consists of four pages. Page One lists the per books portion of the Statement of Operations in Column (b) for the Special Contracts. The summation of the restating adjustments that are developed on Page 2 is shown in Column (c) on Page 1, with the restated results shown in column (d). Column (e) shows the summation of the pro forma adjustments to these Special Contracts which were developed on Page 3. Column (f) shows the total pro forma results and indicates that the Special Contracts earn an overall 12.07% return on a proforma 1994 basis. Column (g) shows the amount of change in revenue that would be needed to make these Special Contracts earn a certain overall rate of return. I

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will discuss the significance of these numbers later in the testimony.

Page 2 shows the individual restating adjustments in columns (b) through (f) with the sum of the adjustments shown in column (g). It is this Column (g) which is brought forth to Page 1, Column (c).

Page 3 shows the individual pro forma adjustments in columns (b) through (d) with the sum of the adjustments shown in column (e). It is this Column (e) which is brought forward to Page 1, Column (e).

Page 4 has been included to show the pro forma results of each individual Special Contract.

Q. Please describe Exhibit ___ (JTS-2).

A. Exhibit ___ (JTS-2) shows the monthly sales and revenue levels of each of the industrial hosts to the cogeneration customers as such sales and revenues were reflected in Cascade's last general rate case which was based upon the test period of calendar 1988 and the sales and revenues for the same customers in calendar 1994. This schedule also shows the restated

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and pro forma revenues for these customers.

Q. What is shown on Exhibit ___ (JTS-3)?

A. Exhibit ___ (JTS-3) shows the monthly sales and revenue levels of each of the cogeneration customers for calendar 1994, as well as any required restating and pro forma adjustments to volumes delivered and the revenues for that period.

Q. Please explain the purpose of Exhibit ___ (JTS-4).

A. In the Commission's Fourth Supplemental Order in Docket No. 930511, Cascade was directed to file its case showing Tosco's revenues at tariff rates and the Commission would consider an adjustment to contract rates if justified by cost information and evidence that the contract rate was the best obtainable. This Exhibit shows the adjustment to the test period that is required to restate the revenue at Rate Schedule 663 rates on line 4. Line 6 shows the pro forma adjustment that would be required to reflect contract rates. These restating and proforma adjustments are reflected in Exhibit ___ (JTS-1), on page 2, Column (c) and page 3, Column (b), respectively.

Q. What is the purpose of Exhibit ___ (JTS-5)?

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A. Exhibit ___ (JTS-5) attempts to show the chronology of events that took place in the development of the Special Contracts as well as the construction of facilities to serve these customers. Many of the Commission's comments concerning these Special Contracts address Cascade's estimated costs of the constructing these projects compared to the actual construction costs. It is hoped that Exhibit ___ (JTS-5) will assist the parties in evaluating what facts were reasonably known by Cascade at the time each Special Contract was negotiated.

Q. What is the significance of the overall results for these Special Contracts.

A. As I indicated earlier, based on proforma results for calendar 1994, these five Special Contracts have a combined 1994 overall rate of return of 12.07%. Cascade's last authorized overall rate of return, as approved on December 1, 1989, was 11.95%. It is anticipated that if Cascade were to seek general rate relief under today's financial situation, it likely would experience a lower authorized rate of return. If, as an example, the overall return were in the

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11.00% range, the contribution of these Special Contracts toward the revenue requirements of other ratepayers would be about $530,000 annually.

Additionally, in the Order approving Cascade's Special Contract with Tosco in WUTC Docket No. UG-930511, the Commission indicated that the Company is required to demonstrate that the Special Contract does not draw improper contributions from ratepayers. The proforma 1994 results indicate that these Special Contracts do not draw contributions from other ratepayers and, in fact, provide contributions toward lowering the rates of the other ratepayers.

Q. Please describe each of the Special Contracts and the customers that are served with the Special Contracts.

A.

March Point

The first Special Contract is with March Point. The cogeneration facility is located at the Texaco Refinery in Anacortes, Washington. The Texaco Refinery is a long time customer of Cascade and is now receiving excess steam from March Point to augment

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some of the refinery's energy requirements, as the industrial host for the cogeneration facilities. The Agreement For Natural Gas Service Firm Transportation ("March Point Agreement") was entered into on February 28, 1991. On May 21, 1991, Cascade filed its request for approval under WAC 480-80-335. On July 31, 1991 the Commission approved the Special Contract under Docket No. UG-910571. The Contract provides for the firm delivery of 400,000 therms per day through Cascade's Anacortes-Sedro Woolley distribution system. In the development of its feasibility study, Cascade estimated that March Point would consume 55,000,000 therms per year.

Cascade first learned of the potential cogeneration project at Texaco on March 2, 1988. At that time Cascade first developed its estimate of the cost to construct new facilities to serve the load. It was almost three years to the day before the March Point Agreement was executed. The required new facilities were constructed in early 1992 and were put into service in May, 1992.

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Encogen

The second Special Contract, with Encogen, is for a cogeneration facility located at the Georgia Pacific facilities in Bellingham, Washington. Georgia Pacific is a long time customer of Cascade and is now receiving excess steam from Encogen to augment some of the mill's energy requirements, as the industrial host for the cogeneration facilities. The Agreement For Natural Gas Service Firm Transportation ("Encogen Agreement") was entered into on November 14, 1991. On November 29, 1991, Cascade filed its request for approval of the Special Contract under WAC 480-80-335. In its filing, Cascade demonstrated that the rates negotiated under the Encogen Agreement were required to avoid the customer bypassing Cascade's distribution system. On April 30, 1992, the Commission approved the Special Contract under Docket No. UG-911345. The Encogen Agreement provides for the firm delivery of 370,000 therms per day through Cascade's Bellingham distribution system. In the development of its feasibility study, Cascade estimated that Encogen

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would consume 115,705,000 therms per year.

Cascade first learned of the potential cogeneration project at Georgia Pacific in mid-1990. It was at that time Cascade first developed its estimate of the cost to construct new facilities to serve the load. Negotiations continued for over a year before the Encogen Agreement was executed. The required new facilities were constructed in late 1992 and early 1993 and were put into service in February, 1993.

Tenaska

The third Special Contract, with Tenaska, is to serve a cogeneration facility located at the site of the former B P Oil refinery, now owned and operated by Tosco, in Ferndale, Washington. This refinery in Ferndale is a long time customer of Cascade. It has been owned by Mobil Oil, then by B P Oil, and now by Tosco. Like the other industrial hosts, Tosco is now receiving excess steam from Tenaska to augment some of the refinery's energy requirements. The Agreement For

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Natural Gas Service Firm Transportation ("Tenaska Agreement") was entered into on January 15, 1991. On November 1, 1991, Cascade filed its request for approval of the Special Contract under WAC 480-80-335. In its filing, Cascade demonstrated that the rates negotiated under the Tenaska Agreement were required to avoid the customer bypassing Cascade's distribution system. On March 18, 1992, the Commission approved the Special Contract under Docket No. UG-911247. The Tenaska Agreement provides for the firm delivery of 520,000 therms per day through Cascade's Northern Bellingham and Ferndale distribution system. In the development of its feasibility study, Cascade estimated that Tenaska would consume 150,000,000 therms per year.

Cascade first learned of the potential cogeneration project at B P Oil in mid-1990. It was at that time Cascade first developed its estimate of the cost to construct new facilities to serve the load. Negotiations continued for about six months before the Tenaska Agreement was executed. The required new facilities were constructed in 1993 and

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were put into service in November, 1993.

Tosco

The fourth Special Contract was initially with B P Oil, which has since been acquired by Tosco. As indicated above, the B P Oil refinery is the industrial host for the Tenaska cogeneration facilities. The Agreement For Natural Gas Service Firm Transportation ("Tosco Agreement") was entered into on March 25, 1993. On May 4, 1993, Cascade filed its request for approval of the Special Contract under WAC 480-80-335. In its filing, and through subsequent hearings, Cascade demonstrated that the rates negotiated under the Tosco Agreement were required to avoid the customer forcing Tenaska to cancel the Tenaska Agreement with Cascade, which would have resulted in B P and Tenaska jointly bypassing Cascade's distribution system. On April 29, 1994, the Commission approved the Tosco Agreement in its Fourth Supplemental Order in Docket No. UG-930511. The Tosco Agreement provides for the firm delivery of

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100,000 therms per day through essentially the same distribution facilities that are used to serve Tenaska.

Fibre

The fifth and last Special Contract reflected in this filing, with Fibre, is to serve a generation facility located at the site of Fibre's cardboard mill, in Longview, Washington. This cardboard mill is a long time customer of Cascade. Unlike the other industrial hosts, Fibre's natural gas consumption at the mill will not decrease as a result of receiving excess steam from generation facilities, as this natural gas turbine generator is replacing an existing hog fuel boiler/generator Fibre has operated for many years. The Agreement For Natural Gas Service Firm Transportation ("Fibre Agreement") was entered into on September 1, 1993. On November 15, 1993, Cascade filed its request for approval of the Special Contract under WAC 480-80-335. In its filing, Cascade demonstrated that the rates negotiated under the Fibre

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Agreement were required to avoid the customer bypassing Cascade's distribution system. On September 26, 1994, the Commission approved the Fibre Agreement under Docket No. UG-931386. The Fibre Agreement provides for the firm delivery of up to 360,000 therms per day through Cascade's a new 12 inch pipeline in the Company's Longview distribution area. In the development of its feasibility study, Cascade estimated that Fibre would initially consume 55,845,000 therms per year with Fibre's first turbine, and will eventually consume 111,690,000 therms per year.

Cascade first learned of the potential new generation project at Fibre in mid-1991. It was at that time Cascade first developed its estimate of the cost to construct new facilities to serve the load. Negotiations continued for more than two years before the Fibre Agreement was executed. The required new facilities are currently being constructed and the Company expects to put this pipeline into service in the second quarter of 1995.

Q. In addition to the $1,790,000 contribution toward

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March 15, 1995

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Mr. Steve McLellan
Secretary
Washington Utilities and
Transportation Commission
Post Office Box 47250
1300 So. Evergreen Park Dr. S.W.
Olympia, Washington 98504-7250

Subject: Cascade Natural Gas Corporation/Petition for Determining Ratemaking Treatment of Certain Special Contracts

Dear Mr. McLellan:

Enclosed for filing are the original and 19 copies of a Petition for Determining the Ratemaking Treatment of Certain Special Contracts of Cascade Natural Gas Corporation ("Cascade") in accordance with the Washington Utilities and Transportation Commission's ("Commission") order in matter UG-931386. Cascade asks the Commission for an Order determining the ratemaking treatment with respect to the special contracts with Longview Fibre Company, March Point Cogeneration Company, Encogen Northwest L.P., Tenaska Gas Co. and B.P. Exploration & Oil, Inc. (the "Special Contracts"). By testimony filed as part of this petition, Cascade expects to demonstrate the benefits of the Special Contracts for ratepayers generally, that the business terms of the Special Contracts had a reasonable basis and do not force inappropriate costs onto captive ratepayers, that the cost bases for Cascade's decisions were appropriate, that the Special Contracts do not result in improper subsidization; and, based on the foregoing, that the Special Contracts were prudently entered into by Cascade.

Certain information contained in this filing has been deleted due to its confidential nature. One copy of this filing containing the confidential information is enclosed as well. It is contained in the sealed envelope marked "Confidential." At the pre-hearing conference, Cascade will request a protective order to be entered in this docket in the standard form used at the Commission.

Exhibit C-2

other ratepayers' revenue requirements, do these projects provide other benefits to Cascade's other ratepayers?

A. Yes. These Special Contracts not only enabled the Company to attach these new loads, Cascade was also able to avoid the loss of the industrial host customers to bypass. With the exception of Fibre, with whom Cascade has a long term contractual commitment at Fibre's mill, all of the industrial hosts had short term contracts and could have ceased taking service from Cascade if the cogeneration customer had bypassed Cascade's distribution system. During 1994, Tosco, Georgia Pacific and Texaco consumed [redacted] therms and generated $[redacted] of margin, all of which would have been lost with very little corresponding decrease in expense and dedicated rate base, if bypass had occurred. In addition, the Longview Fibre mill consumed [redacted] therms in 1994 and generated $[redacted] of margin. Cascade's Peaking Gas Supply (PGS) Contract obligates Fibre not to bypass Cascade at the mill as long as the PGS is in effect. If Cascade had not negotiated the PGS

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Contract, Fibre's bypass opportunity would have included [redacted] million therms at the mill as well as the new generating facilities.

Additionally, the 1994 proforma results of these Special Contracts are conservative since the attached Exhibit ___ (JTS-1) has assigned all of the rate base to these cogeneration projects, although other ratepayers actually are provided service through the use of this rate base. The distribution facilities that serve March Point also provides augmented service to the Texaco and Shell refineries, and to the residential and commercial customers in Anacortes. The new distribution pipeline serving Encogen could provide backup service to the Georgia Pacific facilities and to many of the residential and commercial customers in Bellingham. The distribution facilities Exhibit ___ (JTS-1) assigned to Tenaska also provides service to Puget Power's Whitehorn gas turbines, the Tosco refinery and the residential and commercial customers in the towns of Lynden, Sumas and Blaine, Washington.

Furthermore, through the Company's Peak Gas

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Supply Service (PGSS) Agreement with Tenaska, the facilities that serve Tenaska can currently be used to service up to 200,000 therms per day of the requirements of the firm core customers Cascade serves in Bellingham on the coldest days of the heating season. Cascade's Ferndale distribution facilities also connect directly with the Canadian pipeline of Westcoast Transmission, LTD, which enables Cascade to avoid the reservation of Northwest Pipeline's Firm Transportation capacity for the service the Company provides to its core market, as described above. The new 12 inch pipeline Cascade is building to serve Fibre's new generators will provide a complete backup to Cascade's Longview core market at a very low incremental cost.

Q. Other than the margin associated with avoiding bypass at the industrial host plants, has Cascade attempted to quantify those other benefits in this filing?

A. No. The Company believes that the "Stand Alone" Proforma Results of Operations shown in Exhibit __ (JTS-1) clearly demonstrates that the Special Contracts do not draw improper contributions from the

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Company's other ratepayers. If these Special Contracts remain as part of the Company's overall cost of service, as pointed out earlier, they will provide a higher overall return which would lower the revenue requirements of all other customers.

Q. Were the actual construction costs higher than the first budget estimates submitted to the WUTC on the March Point, Encogen and Tenaska distribution system projects?

A. Yes, actual construction costs and, as a result, the actual rate base were higher than first anticipated for those projects. The actual costs were higher than the initial estimates included in the information the Company supplied in its requests for Special Contract approval by this Commission. However, these Special Contracts earn more than an adequate rate of return, even with the higher than anticipated rate base.

Q. Did the Company intentionally understate the estimates for any reason?

A. No, it did not. The Company receives no benefit from understating its estimates. To the contrary, the Company's incentive is to make estimates as accurate

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as possible. In developing its initial estimates for these projects, the Company used what it believed was a reasonable approach and the best information it had available at that time. In March of 1988, when the Company first estimated the cost of providing incremental service to March Point, and as late as 1991, when thefirst three Special Contracts had been signed, but facilities not yet constructed, many of the environmental, permitting and right-of-way acquisition problems that the Company ultimately encountered were unforeseeable by Cascade and the industry, generally. Due to the rapid succession of the first three projects (March Point, Encogen and Tenaska) coming to Cascade's attention, the lessons to be learned from the first project as to increasing costs of pipeline construction were not available in time to significantly aid the Company in estimating the second or third projects. The graphic representation of the time line, as shown on Exhibit ___ (JTS-5), shows that the Special Contracts with March Point, Encogen and Tenaska were signed prior to the construction of any of the three. As a result,

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Cascade significantly underestimated the cost of the March Point, Encogen and Tenaska construction projects. However, since the rates for these projects were all set on a bypass avoidance basis, and due to certain competitive advantages Cascade held due to the structure of its existing facilities, and due to the relative risk of these projects, the Company negotiated rates which it anticipated would provide fairly high rates of return. As a result, the Company's actual earnings from these projects still provide higher than authorized rates of return, even with the actual costs exceeding estimated costs.

Q. Please elaborate on the actual costs of construction compared to the pre-construction estimates.

A. One general factor that was not anticipated at the time estimates were submitted was the high overall level of pipeline construction activity in the Pacific Northwest in 1992 and 1993. Other major pipeline projects were going on concurrently, creating a great demand for pipeline construction equipment and experienced installation crews, resulting in higher costs to reflect the higher demand.

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1. March Point.

In generating the original cost estimate, Cascade used what it believed to be a reasonable standard of $20,000 to $25,000 per inch mile for installing a pipeline. (Eg. a 10"pipeline would cost $200,000 to $250,000 per mile, a 20" pipeline would cost $400,000 to $500,000 per mile.)

The preliminary system design and construction estimates for March Point (a 16" inch pipeline project of about 8 miles) began in 1988. The construction cost estimate of $2,800,000 that was originally submitted to the WUTC was developed in April 1991. Construction did not begin until early 1992. The original basis for estimating this project was the construction contract for the 16" Fredonia pipeline that ran from the Sedro Woolley gate station to the Puget Power Fredonia generating station in Burlington. The Fredonia line was constructed in 1983. This appeared reasonable at the time since the March Point construction project was essentially a further extension of the Fredonia construction project.

In fact, the use of the $20,000 to $25,000 per

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inch mile estimating rule of thumb was confirmed in 1991 on a construction job in Whatcom county. This was a 4.8 mile project using 2" and 6" pipe completed at an average cost of $16,533 per inch mile. The project was considered to be recent evidence of the reliability of the appropriate cost estimating method. This project was considered more difficult than average construction at that time, due to limited working area, traffic control requirements and blacktop restoration costs.

One unanticipated increase in costs on the March Point project was in the cost of acquiring right-of-way. Cascade estimated right-of-way on the March Point project would be similar to the cost of right-of-way on the Fredonia project. The actual costs of securing rights-of-way and the related crop damage payments were several times the figure used in the April 1991 estimate.

Other unanticipated items not covered in the original estimate included environmental consulting requirements and extended permitting time, due to changes in the requirements by the U. S. Army Corp of

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Engineers and the State of Washington.

The single largest cost item that increased on the March Point Project was contractor installation costs. The April 1991 estimate included $1,502,000 for contractor installation (including $102,000 for 8" pipe that was later changed to 16" pipe). The actual contractor installation cost turned out to be $5,423,000. The Fredonia project was installed for $20,790 per inch mile and the March Point project cost $56,000 per inch mile to be installed. Due to delays in receiving the required permits and rights-of-way, the construction of the project began in January 1992. The effect of winter construction can not be precisely determined but Cascade believes winter construction contributed to the higher cost. The contractor bids were higher than anticipated and the final construction cost were higher than the bid estimates.

2. Encogen.

The original construction estimate of $1,440,000 for the entire Encogen project was prepared from the same inch-mile rule of thumb that was used for the March Point project. By the time the extensive cost

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increases on the March Point project were identified, the Special Contract with Encogen had been negotiated and signed, the project design was underway and the Contract, along with the underlying cost estimate had already been submitted to the WUTC. During 1992, the Encogen project was re-estimated based upon the contractor's preliminary estimates and the lessons learned on the March Point project. This revised estimate assumed a $57,500 per inch mile cost. Even this revised estimate, however, failed to accurately predict the total cost of the project. The final costs resulted in a $67,300 per inch mile rate. Among the still unanticipated costs suffered in the Encogen project were right-of-way costs which were increased due to Cascade's lack of alternate routes once permits were in place. Some local government permits required lengthening the pipeline route in some locations. The City of Bellingham imposed some unexpected restrictions concerning the installation of the pipeline near wetlands and waterways which resulted in increased costs.

3. Tenaska.

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As was the case with Encogen, many of the original cost estimates for the 20" Tenaska pipeline project were done in advance of the construction of the March Point project. The $20,000-$25,000 /inch-mile basis was used for the early estimates.

The 20" project was the first of these projects to be installed in Summer/Fall weather. This fact was relied on to predict the quantities of select material and material haul-off that would be required. Once again, the estimate was low but for a different reason. The use of several miles of public road right-of-way was necessitated by Intalco Aluminum Company's unwillingness to grant an easement to Cascade and the Whatcom County Public Works required a large amount of select material in the roads. (Intalco had bypassed Cascade and became involved in litigation with Cascade over a claimed refund after the project was estimated).

Right-of-way compensation was fairly reasonable on the West end of the project near Ferndale. On the East end of the project, the demands of the land owners presented unique problems. In the years just

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preceding Cascade's construction of the Tenaska project, two other pipeline projects had purchased right-of-way in that area and had bid up the "going rate" for compensation to property owners. The property owners demanded a higher price than paid by previous pipelines (Arco/Intalco and Sumas Energy).

The actual bids received from the contractors for the installation of the pipeline were higher than the pre-bid informal estimates that were received the previous year (1992), even though those pre-bid informal estimated were made with the knowledge of the cost of the March Point project. The actual installation cost was higher than the contractors' estimates, particularly due to the extensive work required in the public road rights-of-way.

Q. If Cascade had known during negotiations that the actual construction costs were going to exceed the estimated construction costs, would Cascade have attempted to negotiate higher rates in the Special Contracts?

A. If the Company had known the estimates were too low, Cascade would have attempted to negotiated rates for

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the Special Contracts based upon higher estimated construction costs. However, that does not mean that the rates that were negotiated were not the best rates the Company could obtain under the circumstances. All three of these projects, March Point, Encogen and Tenaska, involved negotiations with parties that were experienced in the cost of the constructing new pipelines to serve cogeneration facilities and each of the parties had estimated their bypass construction costs. March Point Cogeneration Company is a partnership involving San Juan Energy Company. San Juan is a wholly owned subsidiary of Mission Energy Company. Mission Energy Company had recently built several cogeneration facilities in California and they were knowledgeable in the cost of constructing pipelines to serve those facilities. March Point had estimated the cost of constructing new pipeline facilities to serve the Texaco site and had reviewed possible pipeline routes to the site. Based upon the tough negotiations between Cascade and March Point in setting the Special Contract rate, Cascade believes March Point's estimated cost were similar to Cascade's

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initial estimate. If Cascade had insisted on higher Special Contract rates, March Point would have likely bypassed Cascade and built their own pipeline facilities.

Encogen is associated with Enserch Development Corporation which has developed several cogeneration projects elsewhere in the country and has first hand knowledge of the potential cost of pipeline facilities required to serve a new cogeneration facility. Enserch is wholly owned by Lone Star gas Company, which also has pipeline construction cost knowledge. Like March Point, Encogen had estimated the cost of bypassing Cascade and negotiated the Special Contract rate with Cascade with that knowledge. Cascade believes Encogen's estimated construction costs were also similar to Cascade's estimated costs and, if Cascade had insisted on higher Special Contract rates, Encogen would have likely bypassed Cascade and built their own pipeline facilities.

Tenaska Gas Company also was experienced in the construction of pipeline facilities necessary to serve a new cogeneration facility. Tenaska had recently

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built a bypass pipeline in Texas to serve a cogeneration facility Tenaska built there. Many of the people representing Tenaska during Cascade's negotiations had worked for interstate pipelines before forming Tenaska Gas Company. Tenaska had estimated the cost of constructing a new pipeline to serve the proposed cogeneration facilities at Tosco (B P Oil). Cascade believes that Tenaska's estimated cost of bypassing Cascade was lower than Cascade's estimate and that if Cascade had insisted upon higher Special Contract rates, Tenaska would have bypassed Cascade.

Cascade did not have to build any new facilities to serve Tosco. The Commission, in its Fourth Supplemental Order in Docket No. UG-930511, found that Tosco, by joining Tenaska in a joint bypass, had a credible bypass threat, even though Cascade was not informed by Tenaska or Tosco of that joint bypass opportunity until after it had negotiated its rates with Tenaska. The Special Contract rate for Tosco had all but been decided before Cascade was informed of the potential joint bypass. Tenaska had

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early on promised Tosco the same rate that Tenaska would pay for distribution transportation service. Cascade's negotiation choices were simple; either give Tosco the same rate as Tenaska or lose both customers to bypass. Although Cascade was not pleased with the position it found itself in, the business opportunity of serving the new Tenaska load appeared to be too good to allow the joint bypass.

Cascade believes that the rates negotiated for all of the Special Contracts were the highest rates Cascade could obtained, based upon what was known by Cascade and the other parties' negotiation teams at the time the Contracts were entered into.

Q. Were the lessons learned on the first three projects helpful in estimating the Fibre Special Contract rates?

A. The Company is hopeful that its construction estimate for the Fibre project will more accurately reflect the ultimate actual construction costs. At the time of preparing this testimony, the new distribution facilities required to serve Fibre are still being installed and not all actual cost are known. The

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reports thus far indicate that the Fibre construction project is within budget.

Q. What is the future outlook for these Special Contracts?

A. All of the Special Contracts are in the very early stages of their terms. March Point is in its third year, Encogen is just completing its second year and Tenaska had not been on a full year in the 1994 test period used in Exhibit ___ (JTS-1). The Fibre service is expected to be completed and the Fibre Agreement is expected to become effective in the second quarter of 1995.

As is the case with normal Utility rate making, as accumulated deprecation reduces rate base over time, the overall rate of return earned from these Special Contracts will increase, given the same level of volumes delivered.

Q. Are there any risks associated with these Special contracts?

A. Certainly, there are still risks associated with these Contracts. The Companies that currently operate these facilities could go out of business before Cascade has

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recovered its investment. However, all of these facilities have substantial dollars invested in the generation equipment and facilities. Cascade believes that it is highly likely that the banks, which financed the cogeneration plant, or some new entity could continue to operate the facilities if a current operator would falter.

Cascade is currently depreciating its new distribution systems over the useful life of those facilities, generally 37.5 years, while its Agreements with the customers range between 15 and 25 years. It is possible that, at the end of the primary term, the customer may not want to continue receiving service from Cascade, leaving the undepreciated plant stranded unless Cascade can find other customers to use the distribution facilities. Again, with the large capital investment in the generating equipment, it seems likely that the facilities would want to continue to receive natural gas service beyond the primary term, even if the cogenerator had to find another purchaser for the power.

Other risks which might be imagined include the

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risk of plant obsolescence, the risk of reduced demand for electricity from these plants, mechanical failure or other force majeure occurrences which disrupts the operation or destroys one or more plants.

Q. Is it appropriate for other ratepayers to take on those risks?

A. If the Commission believes that the current and future benefits of these contracts should flow through to the ratepayers, then the ratepayers should also incur the risks associated with these Contracts. Part of the reason these Contracts are currently earning a 12.07% overall return is because the Company is using standard deprecation based upon useful life rather than a depreciation rate based upon contract life. If today's ratepayers have lower rates because of the depreciation rate, then the future ratepayers should be at risk for the undepreciated plant that will remain at the end of the Special Contracts' primary term.

Q. Would the Company and its shareholders be willing to take on the risk of the Special Contracts?

A. The Company believes these projects represent good

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business. It foresees these Special Contracts generating higher than allowed rates of return over the primary terms and beyond. Cascade does not believe the risks associated with the longevity of these projects is unreasonable. However, if the Commission feels the risks are too great for Cascade's other ratepayers and the Commission would allow Cascade to take earnings benefits, along with the investment risk, below the line, Cascade would accept that alternative treatment.

Q. What is the Company's recommendation to the Commission in this Petition to Determine Future Ratemaking Treatment of the Special Contracts?

A. Cascade recommends that the Commission find the following:

(1). The volumes of gas delivered to Tosco should be priced at the Special Contract rates for ratemaking purposes.

(2). The Special Contracts do not draw improper contributions from other ratepayers.

(3). The Company acted responsibly and in the best interest of all of its customers as well as

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its shareholders in negotiating the Special Contracts.

(4). Based upon what was reasonably known at the time, the Company obtained reasonable rates under the Special Contracts.

(5). The Special Contracts do not force inappropriate costs onto Cascade's captive ratepayers.

(6). The Special Contracts which contain an automatic rate adjustment clause are to be excluded from any overall general rate increase or decrease the Company may seek and obtain for its other rates schedules for customers generally, and

(7). The revenues, expenses and rate base, along with the resulting net operating income generated from the Special Contracts shall be combined with the revenues, expenses and rate base of all other Washington ratepayers to determine an overall net operating income and rate of return. Any surplus net operating income from the Special Contracts above the allowed rate of return will be used to lower the rates of all other rates schedules and

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ratepayers generally and any deficit net operating income below the allowed rate of return will be used to raise the rates of all other rate schedules and ratepayers generally in all future general rate proceedings.

Q. Does this complete your direct testimony?

A. Yes, it does.

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