**EXHIBIT NO. ___(JHS-10T)**
**DOCKET NO. UG-110723**
**WITNESS: JOHN H. STORY**

**BEFORE THE**
**WASHINGTON UTILITIES AND TRANSPORTATION COMMISSION**

| | |
|---|---|
| **WASHINGTON UTILITIES AND TRANSPORTATION COMMISSION,**<br><br>**Complainant,**<br><br>**v.**<br><br>**PUGET SOUND ENERGY, INC.,**<br><br>**Respondent.** | **Docket No. UG-110723** |

**PREFILED REBUTTAL TESTIMONY (NONCONFIDENTIAL) OF**
**JOHN H. STORY**
**ON BEHALF OF PUGET SOUND ENERGY, INC.**

**NOVEMBER 8, 2011**

**PUGET SOUND ENERGY, INC.**

**PREFILED REBUTTAL TESTIMONY (NONCONFIDENTIAL) OF JOHN H. STORY**

**CONTENTS**

**PUGET SOUND ENERGY, INC.**

**PREFILED REBUTTAL TESTIMONY (NONCONFIDENTIAL) OF JOHN H. STORY**

## I. INTRODUCTION

**Q. Are you the same John H. Story who submitted prefiled direct testimony in this proceeding on September 2, 2011 on behalf of Puget Sound Energy, Inc. ("PSE" or "the Company")?**

A. Yes.

**Q. Please summarize the purpose of your rebuttal testimony.**

A. My testimony will address some of the concerns raised by the Staff of the Washington Utilities and Transportation Commission ("Staff"), the Public Counsel section of the Washington State Attorney General's Office ("Public Counsel") and the Northwest Industrial Gas Users ("NWIGU") witnesses about whether the Pipeline Integrity Program ("PIP") is an appropriate regulatory mechanism.

## II. RESPONSE TO SPECIFIC ISSUES RAISED BY OTHER PARTIES

**Q. On page 14 of Ms. Crane's Direct Testimony, Exhibit No. ACC-1T, she states that customers will be prepaying for plant that is not yet in-service, and**

**Commission Staff witness Mark Vasconi questions whether the PIP violates the used and useful statute. Are these valid concerns?**

A. No. The Company has addressed this issue in its proposal by adding new plant on a monthly basis, based on when the Company plans to replace the old pipe and put the new plant in service. These additions are then averaged using the average of monthly averages to match the rate base additions to the revenues collected during the rate year. The actual amount collected in revenues will be compared to the actual amounts that should have been collected and any differences will be trued up.

The Commission has historically approved future costs and rate base additions that are calculated using the average of the monthly average of rate base during the rate year such as new electric production facilities. For example, on the electric side of the business future production property has been included in rate base at the average of the monthly average for the rate year and conservation expenditures are forecast and trued up for the rate year. For rate base, the purpose of the average of the monthly average calculation is to attempt to match the rate base growth to the revenues collected during the recovery period. One of the stated reasons for doing this is that plant additions are reflected as a point in time when added to the balance sheet; however, revenues needed to recover the investment will be collected over a period of time.

Moreover, the Commission has recently reiterated that it applies a flexible and not overly-strict approach to the determination of when plant is used and useful.[1] The Commission considers whether the plant provides benefits to customers, either directly or indirectly. Under the PIP, customers are paying for plant as it goes into service and the plant provides benefits to customers by enhancing the safety and integrity of the pipeline.

**Q. Is Ms. Crane's testimony regarding the impact of PIP on the Company's budget process correct?**

A. No. Financing and budgeting are related in that budgets will determine how a utility will have to generate cash. Cash can be generated through debt and equity issuance as Ms. Crane presents or through rate increases. The cost of, and the return on, pipeline replaced under the PIP is proposed to be covered by a rate increase. As such these pipeline replacement programs under the PIP will become a part of the fixed portion of the budget, up to $25 million per year, and will not compete for budget funds as described by Mr. Henderson on page 14 of his prefiled direct testimony, Exhibit No. ___(DAH-1T). Obviously, under extreme circumstances even a fixed portion of a budget can be reduced or eliminated. If this were to happen there would be no additions to rate base and there would be no increase in the PIP rate.

---

[1] *Report and Policy Statement Concerning Acquisition of Renewable Resources by Investor Owned Utilities,* Docket UE-100849, (January 3, 2011), ¶¶ 30-31.

Ms. Crane's other concerns regarding the possibility of re-allocating monies budgeted for pipeline replacement to cover executive bonuses are also misdirected. The Company's total budget is approved by the Board of Directors based on need and source of funds. However, the Company's actual expenditures will still need to be reviewed and approved by the Commission prior to the expenditures being included in rates. Thus, if the Company awards executive bonuses that are not reasonable, the Commission will review such expenditures in the next general rate case and take appropriate action.

**Q. Ms. Crane states that the PIP will cause an additional $10 to $15 million of additional rate increases through 2016. Is this an accurate statement?**

A. No. Without the PIP, some of these cost increases would still be recovered in general rate cases. However, as discussed by Mr. DeBoer and Mr. Henderson, this traditional ratemaking approach does not provide the customer benefits that can be achieved under the PIP.

**Q. Ms. Crane criticizes Mr. Henderson's statement that there is no new revenue associated with the pipe replacement that would take place under the PIP. Is her criticism valid?**

A. No. Mr. Henderson's prefiled direct testimony addressed the fact that the pipe being replaced under the PIP proposal is not pipe that would otherwise generate additional revenues from customers at the time it is replaced, absent the PIP tariff. Customers would continue to pay the embedded cost of plant in their rates until those rates are adjusted, and because there are no new customers being added to the system, there are no new customer revenues. Under historical ratemaking, customer rates might not be adjusted until up to 27 months after the plant replacement.

**Q. Do you agree with other parties' assertions that there are operations and maintenance expense savings that should be offset against the PIP costs?**

A. No. Mr. Henderson explains in his prefiled direct testimony that operations and maintenance costs will not be reduced materially with this type of pipe replacement as the new pipe will still require ongoing testing and maintenance programs that are standard business operations. Any other savings due to a decrease in leak repairs would be offset with increased operations and maintenance costs related to increased construction.

Moreover, while any savings might be a concern if PSE was currently earning its authorized rate of return and the savings in operations and maintenance expense caused PSE to over earn its authorized rate of return, that is not the situation in which the Company finds itself. As can be seen in the table below, the Company's actual adjusted rate of return, as determined by the Commission in recent general rate case proceedings, is well below the rate of return authorized by the Commission. The adjusted rate of return and the allowed rate of return in this table are taken from the Company's compliance filing in each of the indicated general rate case dockets. This difference in the rate of return earned versus allowed amounts to millions of dollars. This underearning should outweigh Ms. Crane's concerns regarding the 28 basis point increase in PSE's actual earning on new plant that is in service and benefiting customers, and her concerns regarding cost savings that might occur from the PIP process.

| **Docket Number** | **Adjusted Results of Operation** | **Allowed Rate of Return** |
|---|---|---|
| UG-040640 | 6.93% | 8.40% |
| UG-060267 | 6.85% | 8.40% |
| UG-072301 | 5.98% | 8.25% |
| UG-090705 | 7.67% | 8.10% |

**Q. Mr. Schoenbeck states that the application of the PIP charges to special contract customers is erroneous. Do you agree with this assertion?**

A. No. Whether a new rate schedule applies to special contract customers depends on the terms and conditions of the customer contracts. PSE reviewed its contract language prior to proposing the PIP, and concluded that supplemental schedules do apply; therefore including special contract customers in the PIP was appropriate. For example, another tracker schedule that was implemented in recent years, the merger credit (Schedule 132), also applies to special contract customers. NWIGU did not object to applying this supplemental schedule to special contract customers. In fact, the merger rate credit allocated to special contract customers exceeds the amounts allocated to them in the current PIP proposal.

**Q. Mr. Schoenbeck also indicates that the PIP proposal fails to reflect the cost of service among PSE's customers, because PSE applies its own cost of service study without consideration of other allocation methodologies advocated by other parties. How do you respond?**

A. The cost of service approach used by PSE to allocate PIP costs is the same one proposed in the Company's gas tariff increase filing, Docket No. UG-101644, and 2009 general rate case, Docket No. UG-090705. WUTC Staff,[2] Public Counsel[3] and Nucor Steel Seattle, Inc.[4] are all on record as generally supporting the proposed rate spread resulting from the Company's gas cost of service methodology. In fact, the only party to object to PSE's proposed gas cost of service methodology in its 2009 general rate case was NWIGU. Therefore, PSE concluded that a majority of parties to this case would also find PSE's cost of service methodology acceptable for allocating PIP costs.

---

[2] Testimony of Thomas E. Schooley, Exhibit No. TES-1T, page 15, lines 11-16 and page 16, lines 10-12.

[3] Direct Testimony of Glenn A. Watkins, Exhibit No. GAW-1T, page 26, lines 1-6 and page 29, lines 1-2.

[4] Prefiled Response Testimony of Kevin C. Higgins, Exhibit No. KCH-1T, page 5, lines 3-14.

## III. CONCLUSION

**Q. Does this conclude your testimony?**

A. Yes, it does.