BEFORE THE WASHINGTON UTILITIES & TRANSPORTATION COMMISSION

IN THE MATTER OF THE JOINT APPLICATION OF

PUGET HOLDINGS LLC AND

PUGET SOUND ENERGY, INC.,

FOR AN ORDER AUTHORIZING PROPOSED

TRANSACTION

DOCKET NO. U-072375

DIRECT TESTIMONY OF BARBARA R. ALEXANDER (BRA-1T)

ON BEHALF OF

PUBLIC COUNSEL AND THE ENERGY PROJECT

June 18, 2008

PUBLIC VERSION

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I. INTRODUCTION / SUMMARY

Q: Please state your name and business address.

A: My name is Barbara R. Alexander. My office is located at 83 Wedgewood Dr., Winthrop, ME 04364.

Q: By whom are you employed and in what capacity?

A: I am a self-employed consultant. I use the title of Consumer Affairs Consultant.

Q: On whose behalf are you testifying?

A: I am testifying on behalf of the Public Counsel Section of the Washington Attorney General's Office (Public Counsel) and the Energy Project.

Q: Please describe your professional qualifications.

A: I opened my consulting practice in March, 1996, after nearly ten years as the Director of the Consumer Assistance Division of the Maine Public Utilities Commission. While there, I managed the resolution of informal customer complaints for electric, gas, telephone, and water utility services, and testified as an expert witness on consumer protection, customer service and low-income issues in rate cases and other investigations before the Commission. My current consulting practice is directed to consumer protection, customer service and low-income issues associated with both regulated utilities and retail competition markets. My recent clients include the Pennsylvania Office of Consumer Advocate, Maryland Office of People's Counsel, New Jersey Rate Counsel, Maine Office of Public Advocate, and various AARP state offices (Montana, New Jersey, Maine, Ohio, Virginia, Maryland, and the District of Columbia). I have prepared testimony on behalf of my clients before state utility regulatory commissions in Pennsylvania, Maine, Vermont, California, New Jersey, Maryland, Illinois, Colorado, West Virginia, Iowa, Kansas, Texas, Wisconsin, Montana, Washington, and the Canadian Radio-Television and Telecommunications Commission.

With respect to my experience in Washington, I appeared on behalf of Public Counsel in the proceeding regarding the merger of Washington Natural Gas Co. and Puget Sound Power and Light Co. in 1996, which created Puget Sound Energy (PSE) (Docket No. UE-960195). It was in that proceeding that PSE's original Service Quality Index (SQI) was developed and approved by the Commission. I have also assisted Public Counsel on matters relating to telecommunications service quality in various proceedings concerning Qwest's retail service quality performance and the structure of its service quality index.

On May 23, 2008, I filed Direct Testimony on behalf of Public Counsel and the Energy Project in the pending GRC proceeding filed by Puget Sound Energy, Docket Nos. UE-072300 and UG-072301.

I am also an attorney, and a graduate of the University of Michigan (1968) and the University Of Maine School Of Law (1976).

My resume and list of publications and testimony are provided in Exhibit No._____ (BRA-2).

Q: What exhibits are you sponsoring in this proceeding?

A: I am sponsoring Exhibit No. ___ (BRA-2), which is my resume and which lists my publications and formal testimony before state regulatory commissions, and

Exhibit No. ___(BRA-3), which is a compilation of PSE's service quality performance under the current SQI from 1997 through 2007.

Q: Please describe the issues you will address in this proceeding.

A: The purpose of my testimony is to respond to the filing by Puget Sound Energy (PSE or Puget) and Puget Holding LLC seeking approval from the WUTC to transfer the control of PSE to a holding company whose majority ownership is controlled by The Macquarie Group (Macquarie), an investment fund based in Australia. My testimony will address those aspects of the acquisition that may affect customer service, reliability and service quality, and low-income programs. I will review PSE's service quality and low income programs and policies and the promises made by the Applicants in this proceeding, and will propose conditions with respect to these issues that should be imposed if the Commission approves this acquisition.

Q: Do you offer an opinion on whether the Commission should approve this Application?

A: Based on my review of the service quality, customer service, and low income commitments made by the Joint Applicants, I support the recommendation of Mr. Stephen Hill on behalf of Public Counsel that this proposed transaction should be not be approved. Based on my review of these commitments, which I discuss in more detail below, the Joint Applicants have not demonstrated that the transaction will be in the public interest. My testimony also proposes specific conditions with respect to service quality, customer service, and low income programs if the Commission chooses to approve this transaction.

Q: In general, what recommendation do you make with respect to the conditions that the Commission should require the Joint Applicants to meet if the Commission decides to approve this transaction?

A: Because this proceeding is on a different track from PSE's pending general rate case (GRC) in Docket Nos. UE-072300 and UG-072301, I recommend that all of the proposals that I have made in the GRC should be adhered to as a condition of this proposed sale of PSE. I discuss the most significant conditions in more detail below in this testimony, but overall, the recommendations with respect to Public Counsel's witnesses in the GRC should be linked and imposed upon the Joint Applicants should this transaction be approved.

Q: What has the Commission stated about the need to evaluate service quality, reliability of service, and impacts on low income customers with respect to similar transactions involving Washington's public utilities?

A: In its consideration of the PacifiCorp and Scottish Power merger, the Commission identified the relevant issues and scope of inquiry to include the following:

> **Quality of service:** This issue appears to be the heart of the matter from Applicants' perspective. Scottish Power makes commitments to service quality, reliability, and customer service. We agree with several of the parties that this subject requires further consideration. Questions regarding how Scottish Power will improve customer service, the source of funding for improvements, the need for improvements, the effects of the promised efficiencies, the fund allotment for low income assistance, and related issues require more information and analysis.[1]

[1] *In the Matter of the Application of PacifiCorp and Scottish Power*, Docket UE-981627, Third Supplemental Order, p 3 (PacifiCorp/Scottish Power merger).

Q: Please summarize your conclusions and recommendations.

A: My testimony describes the risks associated with this proposed transaction to PSE's customers and the failure of the Joint Applicants to meaningfully address these risks. My testimony proposes specific conditions with respect to service quality, customer service, and low income programs if the Commission chooses to approve this transaction. The following is a summary of my recommended conditions:

- <u>PSE's Service Quality Performance and Structure of the SQI</u>— PSE's annual service quality reports filed with the Commission indicate that several aspects of the Company's service are in need of improvement. Additionally, the manner in which the SQI tracks customer call center performance fails to assure a reasonable level of service throughout the calendar year. My recommendations seek to increase penalties to reflect PSE"s growing revenues, reform the call center performance standard to reflect quarterly performance, respond to PSE's failure to meet the SAIDI standard for two consecutive years, and include additional reporting requirements that reflect emerging service quality performance results.
- <u>PSEs Low Income Bill Payment Assistance Program: Funding and Design</u>—The funding level for PSE's bill payment assistance program is insufficient and enrollment of qualified low income customers reflects a very low penetration rate. I recommend that PSE seek to increase the enrollment of qualified HELP customers over a several year period, beginning with an increase in the next program year of 5,000 additional customers over the number served in 2007. In the course of that effort, PSE should continue to work with the HELP advisory

committee to investigate ways to improve program delivery and effectiveness.

- PSEs Low Income Programs: Energy Efficiency—PSE should increase funding for its low-income energy efficiency programs to compensate for the increased costs for the weatherization measures and to serve more households. Beginning in 2009, I recommend an increase in ratepayer funding of $1,500,000 per year compared to PSE's proposed budget for this program in 2008-2009. Second, I recommend that the Commission require as a reasonable condition for approval of this proposed sale an additional shareholder contribution to the low-income energy efficiency programs in the amount of $7.25 million over five years, similar to the contribution that PSE made to this effort in 1997. In both cases, PSE should work with the provider agencies to develop a plan to implement this increased level of funding over a 12-24 month period.

II. COMMITMENTS OFFERED BY THE APPLICANTS IF THIS APPLICATION FOR SALE IS APPROVED

Q: Please describe your understanding of this transaction and summarize the benefits to PSE's customers promised by the Applicants if the transaction is approved.

A: If this transaction is approved, Puget Sound Energy, an electric and natural gas utility regulated by the Washington Utilities and Transportation Commission, will be owned by Puget Holdings, a Delaware limited liability company, which is owned by six different investing entities. Slightly over 50% of the ownership interest will be held by three members of the Macquarie Group (Macquarie).

Macquarie has its antecedents in Australia and is headquartered in Australia. The other three entities reflect Canadian ownership or investment vehicles.[2]

The Applicants claim that the new investors and owners will be able to provide the significant capital needs of PSE and that the "magnitude" of the external funding needs of PSE "puts PSE and the region at risk."[3] The Applicants state that the provision of the needed capital investment will "sustain a successful, locally managed public utility." These commitments are identified as "substantial benefits for PSE's customers."[4] The Applicants also promise additional "specific commitments that benefit PSE customers and that protect PSE's customers from risk of harm from the Proposed Transaction."[5] I will not discuss all the specific commitments, but will focus on those that relate to Quality of Service, the Capital Investments relating to delivery infrastructure, Low-Income Assistance, and the proposed contribution to Puget Sound Energy Foundation. These commitments include:

- With regard to Quality of Service, the Applicants promise to continue the currently applicable Service Quality Index. [6]
- With regard to Low-Income Assistance, the Applicants promise to maintain existing programs and work with low-income agencies to address issues relating to low-income customers.[7]

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[2] *Joint Application For an Order Authorizing Proposed Transaction* (Joint Application), Appendix B. Public Counsel witness Stephen Hill describes the specifics of the transaction in greater detail.
[3] Joint Application, ¶ 34.
[4] *Id*.
[5] *Id.*
[6] Joint Application, ¶ 37.
[7] Joint Application, ¶¶ 74-75.

- The Applicants promise to provide a one-time contribution of $5 million to the Puget Sound Energy Foundation.[8]
- The Applicants stated that meeting PSE's investment needs for delivery infrastructure will be considered a "high priority" by the Board of Puget Holdings and PSE. A specific credit facility in an amount of not less than $1.4 billion will be made available to PSE to support its October 19, 2007, Business Plan.[9]

Q: Do the Joint Applicants expand on any of these commitments in their testimony filed with the Joint Application?

A: Mr. Christopher Leslie, on behalf of Puget Holdings LLC, testifies that PSE is a "well run utility that provides excellent service to a growing region."[10] He states that the Service Quality Commitment (to continue the current SQI) "provides assurance to the Commission and PSE's customers that the high quality of service PSE has been providing will continue."[11] With regard to the Capital Requirements Commitment, he states that the transaction is "structured to strengthen PSE's balance sheet at closing" and will "provide a more reliable source of funding for PSE's capital investments needs, including the acquisition of electric generation resources to meet the growing needs PSE's customer base, and replacement of aging energy delivery infrastructure so that PSE can continue providing reliable electric and gas service to its customers."[12] Mr. Leslie

[8] Joint Application, ¶ 55
[9] Joint Application, ¶¶ 38-39
[10] Exhibit No. ___ (CJL-1T), p. 26
[11] Exhibit No. ___ (CJL-1T), p. 29
[12] Exhibit No. ___ (CJL-1T), p. 30

promises that any "net cost savings" as a result of the transaction will be reflected in subsequent rate proceedings and that this is a benefit because it provides a "…mechanism for customers to realize any savings that results from the Proposed Transaction."[13] With regard to the Low-Income Assistance Commitment, Mr. Leslie states that the continuation of the current programs will ensure that "…low income customers will not be exposed to harm as a result of the Proposed Transaction."[14]

Q: Did you conduct discovery to explore these proposed commitments in more detail and, if so, with what result?

A: Yes. A review of the discovery and responses in this proceeding indicates that there are no concrete additional benefits provided to PSE's residential customers if this transaction is approved. The commitments do nothing more than promise to comply with current orders of the Commission or Washington's statutory policies. PSE has stated that it will not fail to make any needed investments if the proposed sale is rejected. Rather, the "promise" is that the sale will result in an "improved access to capital[15] While Mr. Reynolds, on behalf of PSE, references PSE's dedication "to continually improve service quality,"[16] PSE does not propose any additional service quality standards other than those already in place.[17] As I will describe more fully later in my testimony, PSE has not complied with one of the key reliability service quality performance standards for

[13] Exhibit No. ___ (CJL-1T), p. 32.
[14] Exhibit No. ___ (CJL-1T), p. 42.
[15] PSE Response to WUTC Staff Data Request No. 1032.
[16] Exhibit No. ___ (SPR-1T), p. 9.
[17] PSE Response to WUTC Staff Data Request No.1031.

the last two years. In addition, its call center performance is erratic and falls below acceptable standards in several months of each year. Furthermore, PSE is unable to identify any specific investments that will be made with the "improved access to capital" that will result in improved service quality for its customers.[18] According to Mr. Reynolds, PSE will primarily focus on achieving the applicable service quality performance requirements of the SQI in the future in order to meet customer needs.[19] No new standards are proposed. No specific level of improvement in customer service quality is promised.

Q: Please discuss the commitment by Macquarie to a one-time contribution of $5 million to the Puget Sound Energy Foundation.

A: It is not clear whether this proposed commitment will in fact result in an additional $5 million in funds available to the Foundation since it is unknown what criteria governs the current contributions allocated to the Foundation by the current owners of PSE. In any case, this Foundation is not subject to the Commission's regulatory oversight. These contributions will certainly benefit the local community, but they are not contributions that directly impact the regulated services and the ratepayers that the Commission is charged with protecting. The additional funds will be used according to the PSE Foundation funding priorities and guidelines.[20]

[18] PSE Response to Public Counsel Data Request No. 3129
[19] PSE Response to Public Counsel Data Request No. 3130. See also PSE Response to Public Counsel Data Request No.3132.
[20] PSE Response to Public Counsel Data Request No. 3127.

Q: In your opinion, are these specific "commitments" by the Applicants sufficient to demonstrate that the transaction will not result in harm to ratepayers or increase the risk of harm to ratepayers?

A: No. I do not believe it is appropriate for the Commission to rely on the commitments proposed by the Applicants with respect to customer service, reliability of service (investment in the distribution infrastructure), contributions to a PSE-controlled foundation, or low-income programs as sufficient to ensure that customers will not be exposed to harm. Nor do they reflect a fair and balanced allocation of the risks and rewards associated with this transaction. For the most part, these "commitments" do not respond to the heightened risk of deterioration of service or adverse impacts on low income customers should service deteriorate and prices increase as a result of this transaction. The "promises" are nothing more than the continuation of current programs and policies that are in effect and that the Commission has plenary authority to oversee, continue, terminate, or make additional changes as circumstances warrant. I will discuss the potential risks and harms to ratepayers with respect to these issues in more detail below and propose conditions that are meaningful, enforceable, and appropriate in light of risks associated with this transaction and that reflect concerns by other state commissions for transactions of this type in other jurisdictions.

Q: What is your response to the Joint Applicants' assertion that the promised access to capital for investments by PSE in generation and distribution infrastructure will result in benefits to PSE's customers?

A: While Mr. Hill, on behalf of Public Counsel, describes his concern with the Applicants' line of reasoning in his testimony, my additional concern is that the commitments made by the Joint Applicants with respect to access to capital resources is not accompanied by any showing that this capital resource is the "best" option for PSE's ratepayers compared to other options. Nor is this commitment accompanied by any assurance that any of this access to capital will result in adequate or improved service quality performance or reliability of service for PSE's ratepayers.

The proposed commitment relating to new investment refers to making funds available to PSE to carry out PSEs 2007 Updated Business Plan. A confidential copy was provided in PSE's Response to Public Counsel Data Request No. 3069. While the Business Plan is confidential, it is fair to state that this plan focuses on earnings and the impact of the proposed business plan on the corporate balance sheet and does not reflect commitments for specific or measureable service quality results for ratepayers. I understand that the current SQI measures some of the key variables related to customer service quality and reliability of service and that the Joint Applicants have committed to continue to comply with the current SQI. However, PSE has failed to meet one of the critical reliability performance standards for the past two years. PSE barely meets the customer calling performance standard. Furthermore, the current SQI does not even measure PSE"s performance in assuring timely delivery of service to customers for which new construction is required.

The combination of the new owners' reasonable expectations of profit earned on this investment in purchasing PSE and the lack of any specific or enforceable promise relating to the results of providing new capital resources to PSE suggests that my concern about who bears the risks associated with this proposed transaction are reasonable and valid.

III. RISKS TO CUSTOMERS POSED BY THIS TRANSACTION

Q: Please describe the risks and potential harms to residential customers that may result from this transaction.

A: The lack of specificity with respect to the impact of this transaction on customer service, service quality, and low-income programs and the failure to identify any specific goals and objectives that will guide the operations of PSE by its new owners increases the risk of a degradation of service quality and reliability of service. It also threatens the ability of vulnerable lower income customers to maintain and retain affordable service. There are a number of reasons why this proposed acquisition does not adequately respond to the needs of residential customers or respond to the risk of harm associated with such a dramatic change in ownership of Washington's largest investor-owned public utility.

Q: Do the "commitments" proposed by Mr. Leslie and the Joint Applicants adequately respond to the risks associated with this transaction?

A: No. First, the proposed commitments by Mr. Leslie on behalf of Puget Holdings, LLC are vague and without substance. In most cases, he promises only items which already in effect and which the new owners have no authority to change without the Commission's approval in any event. A promise not to seek to eliminate the SQI, for example has no value since, in 2002, PSE already agreed not to seek to terminate the SQI. Mr. Leslie's promise to continue the current low-income programs is a similar "non-promise" and the notion that PSE has to promise to consult with low income advocates concerning the needs of low income customers is similarly without meaning or value.

With regard to new infrastructure investments, the Applicants have not really promised a specific level of investment. Nor have they demonstrated that the costs for these capital investments would somehow be lower or more beneficial to PSE's customers in the form of lower rates compared to the traditional access to capital available to PSE. No specific investments are promised. There are no performance measures or other indicia proposed to ensure that such investments will result in an adequate level of facilities to respond to local growth and development. These promises reflect a complete lack of risk assumed by PSE's new owners. On the contrary, all the risks associated with the failure to meet these commitments remain with PSE's customers.

Second, customers will bear significant risks associated with the transfer of ownership from a Washington-based utility with publicly traded stock and shareholders responsive to Washington's regulatory policies to a private equity investment consortium. The new owners will naturally seek a return on this investment. The operations of the many companies and investments made by the Macquarie Group and the urge to generate the return on the substantial investment made to acquire PSE may result in pressure to cut costs and reduce expenses, thus adversely impacting customer service and service reliability. I am not suggesting that adverse results are necessarily inevitable as a result of this transaction. However, it is only appropriate to point out the potential for such actions that have occurred when utilities have been acquired by new owners in the past and that could occur when management is striving to demonstrate lower costs and savings to its investors. Of course, it may be possible to reduce costs, increase efficiency, increase profits, and improve customer service and service quality performance. My recommendations are designed to make it more likely that these "win-win" results do occur and that the risk of their non-occurrence is shifted from Puget's customers to Macquarie's investors.

Finally, the risks I have described above can have particularly adverse consequences for low-income and other payment troubled customers. These customers rely heavily on the ability to reach customer service representatives in a timely manner, respond to threats of discontinuance of service, negotiate reasonable payment arrangements, and make use of their rights under the Commission's credit and collection and consumer protection rules. More so than other residential customers, low-income, vulnerable, and payment troubled customers rely on access to customer call centers to negotiate payment arrangements, respond to disconnection notices, and enroll in various low-income programs. Low-income customers are typically disconnected more frequently than non low-income customers and experience a higher rate of nonpayment.[21]

[21] According to the U.S. Department of Energy-Energy Information Administration 1997 Residential Energy Consumption Survey, over 5 percent of low-income households experienced an electric shutoff in 1997 compare to less than 2 percent of those over 150 percent of poverty. Those with very low-income (less than $5,000 annual household income) experience disconnection at an even higher rate, about 8 percent.

The receipt of timely and accurate bills and disconnection notices with a well-understood and efficient collection routine is crucial to such customers' ability to manage their monthly payments and seek financial assistance. These activities are at risk, even if a utility has historically had good service quality, when a company is subjected to pressures to assure adequate profits to new investors.

Q: Have other state regulatory commissions shared your concerns and imposed meaningful conditions for transactions of this type?

A: Yes. In fact, the Macquarie Group purchase of Duquesne Light Co. in Pennsylvania was approved pursuant to a settlement that included specific service quality performance measurements and new performance standards. The fact that these were agreed to was significant because of the lack of previously established service quality performance standards applicable to Duquesne.[22] Finally, specific consultations were set forth with low income and other public interest advocates for low income programs and the settlement reflected additional funding for specified low income programs, including the expansion of eligibility for the low income weatherization program and commitments to expend the budgeted funds in future years. In the case of the latter programs, the settlement of the sale transaction specifically linked an increase in certain funding levels of a recently concluded base rate case.

[22] Pennsylvania PUC, Application of Duquesne Light Company for a Certificate of Public Convenience Under Section 1102(a)(3) of the Public Utility Code Approving the Acquisition of Duquesne Light Holdings, Inc., by Merger, Docket No. A-110150F0035, Initial Decision (March 20, 2007), provided in PSE's Response to Public Counsel Data Request No. 3116, Attachment C. (includes settlement agreement).

There are a number of examples of state regulatory commission action in response to mergers or sale transactions on the issues of customer service and service quality.

The Massachusetts regulatory commission has routinely required that proposals for merger or acquisition include specific provisions to track, report, and establish enforceable performance standards to prevent the potential for service quality deterioration. For example, in 1999, Massachusetts Electric Co. and New England Power Co. and Eastern Edison Co. petitioned for approval of Eastern Edison Company's merger into Massachusetts Electric Company and for other related approvals.[23] In its Order, the Massachusetts Commission stated:

> The Department has recognized the importance of maintaining service quality, particularly when mergers, and the resultant efforts to achieve cost savings or "synergies," can potentially lead to service quality degradation. Boston Edison Merger at 15; Mergers and Acquisitions at 8-10. Acknowledgment of the importance of service quality led the Department to direct all companies that file for approval of mergers or acquisitions to include a service quality plan in their filings. Eastern-Essex Acquisition at 33.

The New Jersey Board of Public Utilities has routinely noted the potential for service quality deterioration as a result of a merger or acquisition and approved specific conditions for the merger in recent electric and natural gas proceedings. With regard to the merger proposal by Atlantic City Electric (Conectiv) with Pepco, the Board stated in its Order:

> In terms of customer service, Staff also recommended that ACE retain the existing New Jersey customer payment centers, maintain existing call center operation located in New Jersey for at least five years post-merger; and commit that any new call center operations will be staffed by

[23] D.T.E. No. 99-47 (2000) Available at: http://www.mass.gov/dte/electric/99-47/finalorder31400.htm .

> trained in ACE's service territory issues, New Jersey regulations, Board policy, ACE's tariffs and the New Jersey Customer Choice Program. Staff requested that ACE also be required to submit to the Board and the RPA a customer information program designed to inform customers of the merger, continuing BPU oversight and continuity of ACE's customer service procedures. While supporting the Joint Petitioners plan to establish performance goals and penalties under a new "Customer Service guarantee" program, Staff noted that ACE should be barred from recovering any penalty payment costs from ratepayers.[24]

Additionally, with respect to assuring compliance with New Jersey customer service regulations, the Board stated:

> ACE, Pepco and Delmarva combined their call center statistics for purposes of the proposed guarantees, and the statistics were based on historical performance of the merged companies. Such an approach could be expected to facilitate assurances that performance did not deteriorate as a result of the merger. Pepco, ACE and Delmarva agreed on a common approach to be utilized for purposes of the proposed voluntary service level guarantees subsequent to the merger (ID at 30.) ACE, in further discussions with Division of Customer Relations Staff, agreed to adopt the additional customer service initiatives. ACE agreed to strive for an annual target of no more than 1500 customer complaints per year to the Board. If the number of customer complaints exceeds 1500 in any year, ACE shall meet with the Division of Customer Relations to discuss the issue and, if necessary, develop a remediation plan. ACE also agreed to maintain regular, ongoing communications with the Board's Division of Customer Relations, and schedule monthly meetings in person or by telephone, or as the parties otherwise agree regarding the customer service issues contained herein. Additionally, ACE agreed to retain its existing New Jersey Customer Payment Centers, i.e., Atlantic's walk-in offices where company personnel accepts bill payments, for a period of at least four (4) years following the completion of the merger and to provide Board staff with a copy or description of the collection policies to be used after the merger to the extent they differ from ACE's current practices. For at least four

[24] Order at 15.

> (4) years after the closing of the merger, ACE agreed to maintain its existing call center operations in New Jersey. Additionally, any new call center operations established to serve New Jersey customers, regardless of the centers' location, will be staffed by personnel trained and familiar with ACE's tariffs and rules and other customer safeguards.[25]

Other states that have approved service quality performance plans as a condition of mergers include Colorado (Colorado Public Service Co. merger with Xcel, based in Minnesota), Washington (Puget/Washington Natural Gas, as noted above), and Washington, Oregon, Utah and Idaho (PacifiCorp/Scottish Power merger).

In addition to the Duquesne Light proceeding described above, the Pennsylvania Commission has recognized the importance of assuring service quality improvement and implementation of promised "best practices" as a result of a merger. In its Order approving the merger of GPU, Inc. with FirstEnergy in 2001, the Commission approved a Service Quality Index plan proposed by the OCA, stating, "Furthermore, without the SQI or some other customer service and reliability measurement and enforcement mechanism, the Applicants' claimed public benefit of improved customer service would be illusory."[26]

Q: Are there examples of mergers or sales of public utilities that have resulted in degradation of service quality and harm to low income customers?

A: Unfortunately, yes. In 2002, the Maine Commission opened an investigation into the service quality performance of Northern Utilities after its parent company,

[25] Order at 32.
[26] Docket A-110300F0095, Opinion and Order, May 24, 2001 at 31-32.

Bay State Gas, merged with NIPSCO Industries (later renamed NiSource). In opening this investigation, the Commission stated:

> In approving the merger, we noted that customer service quality can suffer when utility funds are short or when management's interest in this aspect of a utility subsidiary is diluted after a merger and that in other reorganizations we had implemented service standards and related penalties to ensure that customer service quality would be maintained. The service quality indicia on which Northern is required to report do not carry any formal requirements or penalties for particular performance results. Northern's rates are currently set using traditional rate setting methodologies that do not impose any direct penalties for poor service quality problems, relying instead on rate of return allowances to discipline utilities.
>
> The short time frame of the NiSource/Columbia merger case did not allow development of service standards and penalties. Consequently, we left open the question whether, at a later date, we would open an investigation to review the adequacy of Northern's service quality, its reporting criteria, and to determine whether we should adopt any mechanisms, programs, standards, or penalties to ensure that Northern provides adequate service quality to its customers. Consistent with our general authority, in the event that Northern's service quality is inadequate, we will order an appropriate remedy, one that could include financial directives or instituting a performance based regulatory mechanism.[27]

Subsequent to this investigation, the PUC approved a Service Quality Plan for Northern Utilities, Inc. which imposed a maximum penalty of $300,000 if it fails to meet 11 performance targets. The Commission's press release approving this plan noted that it had received many complaints over the past three years from customers who could not reach the company over the phone or who could

[27] See the Maine PUC's Order Initiating Management Audit and Investigation of Service Quality Incentive Plan (May 16, 2002) at http://www.state.me.us/mpuc/orders/2002/2002-140o.htm.

not understand their bills and directly linked these service quality failures with numerous reorganizations and substantial cuts in personnel subsequent to the merger.[28]

In 2003, the Colorado PUC initiated an investigation into Colorado Public Service Company's reliability of service in the wake of numerous outages for which the company incurred a penalty of $5 million in 2003. A Colorado Staff report to the PUC found that the utility's new owner (Xcel) had reduced capital investment in new distribution facilities and reduced its amount of capital available to the subsidiary in Colorado.[29] Subsequent to this report, the Company entered into a Stipulation with the PUC Staff and the Office of Consumer Counsel that included additional investments in the distribution system, contributions to the low-income program, and revisions to its Quality of Service Plan for the post-2006 period.[30]

IV. PSE'S SERVICE QUALITY AND CUSTOMER SERVICE PERFORMANCE: PROPOSED CONDITIONS

Q: Please describe PSE's current Service Quality Index and the recent performance of PSE pursuant to these performance standards.

A: The SQI was originally created in the stipulated settlement of the 1996 merger between Puget Sound Power & Light Co. and Washington Natural Gas Co. in Docket Nos. UE-951270 and UE-960195. The SQI was reviewed and modified in

[28] See PUC Orders Service Quality Plan for Northern Utilities, Inc. (March 29, 2004) at http://www.state.me.us/mpuc/staying_informed/news/news_releases/prNUIMgtAudit.htm.
[29] See http://www.dora.state.co.us/puc/energy/InitialRpt01-14-04ReliabilityPSCoElectric.pdf.
[30] Public Service's Quality of Service Plan can be accessed at its website in the Colorado electric tariff, pages 124-133: http://www.xcelenergy.com/docs/corpcomm/psco_elec_entire_tariff.pdf

PSE's General Rate Case in 2002 in Docket Nos. UE-011570 and UG-011571. As a result of the 2002 rate case, the SQI was continued indefinitely beyond its original five-year term, some of the metrics were modified, and the total potential penalty amount was increased.

The current SQI contains 11 service quality performance metrics. There is a maximum penalty of $10 million that is applied in a predetermined formula when PSE fails to meet one or more standards. Exhibit No. ____ (BRA-3) sets forth the current performance areas and performance standards that PSE must meet on an annual basis. Also included in this exhibit are PSE's actual performance results between 1997 and 2007.

As Exhibit No. ____ (BRA-3) demonstrates, PSE has failed to meet the System Average Interruption Duration Index (SAIDI) standard of 136 minutes per customer per year in 2006 (214) and 2007 (167). This level of performance shows a significant deterioration from the performance baseline requirement equal to 57 percent in 2006 and 23 percent in 2007.[31] PSE's failure to meet the SAIDI benchmark has resulted in a penalty of $1 million in 2006 and $513,000 in 2007. Additionally, PSE has routinely failed to meet the Overall Customer Satisfaction benchmark of 90 percent since 2000, but there is no penalty attached to this performance measure. PSE's annual service quality reports filed with the Commission also indicate that the company has met the annual average call center performance standard of answering 75 percent of the calls that seek to speak with

[31] The 2006 percentage deterioration was calculated as (214-136) ÷ 136 = .573. The 2007 percentage deterioration was calculated as (167-136) ÷ 136 = .228.

a customer representative within 30 seconds. PSE has reported their annual performance results for 2005, 2006 and 2007 at exactly 75 percent, the minimum performance standard.

Q: As a result of this recent performance, do you think that the commitment to continue the current SQI is sufficient?

A: No. While I do not recommend any structural change to the SQI design, I do recommend that the total dollar amount of penalties be increased to reflect the revenue growth that PSE has experienced since the penalty was increased from $7.5 million to $10 million in 2002. PSE's retail jurisdictional revenues grew from $1.9 billion in 2002 to over $3 billion in 2007.[32] I recommend an increased total penalty amount of $15 million be applicable to the SQI metrics. This represents approximately 0.5 percent of these retail gas and electric revenues and continues the historical approach to establishing a penalty level that reflects PSE's revenues. After all, if the penalty dollars do not increase to reflect the growth in revenues there is a risk that PSE could consider penalty dollars as "worth" the cost of failing to deliver reasonable service quality and reliability to its customers. This $15 million should be allocated equally to the 10 SQI metrics ($1.5 million per metric) that carry the risk of penalties for the failure to meet the annual standard. The penalty dollars should be calculated in the same manner as in the past, but the dollars per point of deterioration should be increased by 50 percent to reflect the increased total penalty dollars at risk.

[32] As reflected in PSE's 2004 SEC Form 10-K Filing on March 1, 2005 and PSE's 2007 SEC Form 10-K f iling on February 29, 2008.

Q. How does PSE explain its recent failure to meet the SAIDI standard?

A: PSE has not undertaken a formal analysis of the "root causes" of the performance standard failures. The company has typically blamed weather-related events that do not qualify as "major events" as the cause of this failure. PSE's 2006 System Performance Annual Review[33] describes the abnormal number of weather events in 2006, stating that the same number of localized non-major weather related events occurred in 2006 compared to 2003-2005 combined. The System Performance report then states that "[o]nce we've reviewed our response to these weather events and evaluated what can be done to modify sections of our electric system to improve performance, we will be considering infrastructure additions and modifications."[34] The 2007 Service Quality Annual Report points to the wind storms in January 2007 that did not meet the "major event" exclusion criteria and so adversely impacted the annual SAIDI results.[35]

Despite this statement in the 2006 System Performance Programs Report, there is no evidence that such analysis or targeted additions and modifications were actually identified or implemented. Furthermore, this same report documents that the vegetation management program (tree trimming, etc.) targeted fewer distribution and transmission miles in each of the recent years (reduced from 2,198 miles in 2004 to 1,656 miles in 2006).[36] It is certainly possibly that a

[33] PSE Response to Public Counsel Data Request No. 81, Attachment C is the 2006 report. See also PSE Responses to Public Counsel Data Requests Nos. 97, 98, 103 [No "additional analysis" in recent years]; and PSE Response to Public Counsel Data Request No. 136.
[34] PSE Response to Public Counsel Data Request No. 81, Attachment C, p. 6.
[35] The 2007 Service Quality Report was provided in PSE response to Public Counsel Data Request No. 84, Attachment A (First Supplemental Response), p.8.
[36] PSE Response to Public Counsel Data Request No. 81, Attachment C, p. 8.

formal root cause analysis could conclude that the reductions in the vegetation management program contributed to the SAIDI performance failures.

Q: Has PSE prepared a compliance plan to assure that it will meet the SAIDI standard in the future?

A: No. PSE has not prepared a formal compliance plan to achieve compliance with the SAIDI benchmark outside of preparing some graphs about various outage types and noting that "non-storm tree-related outages" may have contributed to failures. This is not an acceptable response in my opinion, particularly since PSE has now missed the applicable performance standard for two years in a row by a significant margin.

Q: What change in the SQI penalty structure do you recommend be implemented to respond to PSE's failure to meet the SAIDI standard for two consecutive years and the risk that the proposed sale of PSE may continue this trend in deterioration in service?

A: I recommend that any failure to meet the annual performance standard for any metric should require PSE to submit an enforceable compliance plan that demonstrates how the Company will meet the standard the following year. This compliance plan should have specific milestones and reporting requirements to demonstrate progress in meeting the standard.

Second, the penalty structure should reflect a higher level of penalty when the performance standard is not met for two consecutive years. I recommend that the otherwise applicable penalty dollars be doubled for the second consecutive failure. Any such penalty that is incurred pursuant to this proposal would be in addition to the maximum $15 million penalty at risk. If this additional penalty had been in place for 2007, PSE would have incurred an additional penalty of approximately $500,000. I recommend that PSE be penalized at least this amount either through a disallowance from PSE's revenue requirement in the GRC proceeding or as a separate one-time penalty payment to customers. This recommendation reflects PSE's failure to meet SAIDI for two consecutive years and because PSE's response to the 2006 and 2007 failure has been inadequate. This penalty or disallowance is appropriate due to PSE's failure to take the continuing failure to meet the SAIDI standard seriously and develop and implement a formal compliance plan.

Q: Do you have any recommendation for an additional Customer Guarantee Payment that addresses the need for an incentive to restore power during major storms?

A: Yes. The current SQI does not provide any incentive to PSE to restore power promptly during major storms because any significant storm results in those events and outage minutes are excluded from the SAIDI and SAIFI calculations. I acknowledge the purpose of these exclusions, but the failure to meet SAIDI in the last two years and my testimony in the GRC proceeding concerning PSE's lack of investment in certain "best practices" for emergency storm preparedness and restoration processes suggest that an additional approach be considered to create an incentive for prompt restoration of service after storm outages. In other words, there is no performance standard in effect by which customers can be assured that service will be restored promptly when there is a "major" storm or other outage event excluded from the measurement of SAIFI and SAIDI. From the customer's perspective, an outage is an outage whether due to a local transformer failure, common thunderstorm, or a "major" storm.

I recommend that the Commission add another provision to the existing Customer Guarantee Program[37] that is based on a requirement in effect in Michigan.[38] PSE should be required to provide an individual customer with a credit of $50 when power is not restored within 120 hours (five days) after an interruption of service that occurs due to a major storm. Any payments for customers pursuant to this policy should not be recovered from ratepayers. Any exception to this policy should only occur when PSE has sought and obtained a specific waiver from the Commission due to an extraordinary event that prevented compliance with this policy.

Q: Does PSE track Momentary Outages or MAIFI (Momentary Average Interruption Frequency Index)?

A: No. PSE does not track the momentary outages.[39] Momentary outages impact power quality and are often a source of customer complaints about reliability of service because these types of outages cause home electronics to flicker or reset. MAIFI is a recognized metric for reliability of service and a recognized standard for defining and tracking this metric has been recommended by IEEE.[40]

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[37] PSE's existing Customer Guarantee Program provides a $50 credit to customers when PSE fails to keep an appointment. However, even this obligation is waived during major outage events.
[38] 2004 MR 3, R 460.744 (eff. 2004). Available http://www.state.mi.us/orr/emi/admincode.asp?AdminCode=Department&Dpt=LG&Level_1=Public+Service+Commission.
[39] PSE Response to Public Counsel Data Request No. 94.
[40] IEEE was previously an acronym for Institute for Electronics and Electronic Engineers, but now uses IEEE as its formal name. IEEE develops standards through a consensus process through its members

Q: Do you recommend that PSE track and report MAIFI results?

A: Yes. I recommend that PSE track and report MAIFI where SCADA[41] systems enable this data to be obtained, although I do not recommend that any penalty dollars be attached to a specific performance level at this time.

Q: Please discuss PSE's call answering performance.

A: For 2005, 2006, and 2007, PSE reports that it has met the annual average call answering standard of answering 75 percent of the calls that seek to speak with a customer representative within 30 seconds. That is, in each of those years, PSE has reported their performance results at exactly 75 percent. PSE has a high rate of calls handled by the automated Voice Response system: 48 percent in 2006 and 42 percent in 2007 of all incoming calls were handled through the automated menu and did not require an "answer" by a representative.[42] This should allow PSE to answer more calls at a faster rate, but the range of monthly call answering performance is very wide—and is particularly poor in the early months of the year (winter) and much better in the summer. For example, in early 2007 PSE only answered 39 percent (January), 48 percent (February), and 50 percent (March) of the calls within 30 seconds. The same pattern of very poor performance in these months is evident in 2006.[43]

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which are then voluntarily referenced or adopted by states and other entities on a wide range of matters. See www.ieee.org. Unfortunately, most of IEEE publications and standards are only available to its members.

[41] The term "SCADA" refers to Supervisory Control and Data Acquisition technology that is installed at substations so that the operational state of the substation can be remotely determined. According to PSE's Response to Public Counsel Data Request No. 132, only 137,000 customers are served by substations without SCADA.

[42] PSE Response to Public Counsel Data Request No. 82, Attachment A. See also PSE Response to Public Counsel Data Request No. 138.

[43] PSE Response to Public Counsel Data Request No. 652, Attachment A.

PSE staffs its call center with a mixture of "on-site" representatives and those that work from their homes. A monthly average of 165 representatives was physically present at the call center in 2007. A monthly average of 19 worked from home. However, the number of those who worked at home increased each month in 2007, reaching 27 per month for the period August through December 2007.[44]

PSE also tracks additional call answering performance metrics, but these metrics are not part of the SQI, nor are they included in PSE's annual service quality reports to the Commission. PSE records the Average Speed of Answer for customer calls, e.g., the average number of seconds or minutes to answer each call. In 2006 this was 50 seconds and in 2007 this was 63 seconds, indicating a deteriorating level of service quality that is not reflected in the annual average of calls answered over 30 seconds. Finally, PSE has a fairly high "abandonment rate," the percentage of callers who abandon their call after joining the queue: 5.65 percent in 2006 and lower at 3.8 percent in 2007. PSE does not track or know the "busy out rate," the rate at which callers encounters a busy signal and thus are unable to even get into the queue.[45] This is important because it is possible that during busy hours, such as during widespread outages, customers cannot get through to PSE at all and even join the queue. These calls are not being captured in the call answering performance areas that are measured in the SQI.

[44] PSE Response to Public Counsel Data Requests Nos. 106, 492, and 624.
[45] PSE Response to Public Counsel Data Request No. 82, Attachment A. See also PSE Response to Public Counsel Data Request No. 83.

PSE can obtain this information from the phone service provider and it is a metric that is included in some service quality performance plans elsewhere.

Q: What recommendation do you make to change the current SQI to respond to the erratic performance of the call center and the risk that customer service will deteriorate even further under this proposed transaction?

A: With respect to metrics that measure call answering performance, I recommend that the current metric be changed from an annual standard to a quarterly standard. This would require PSE to answer 75 percent of customer calls within 30 seconds for each quarter. Each quarter's performance should carry a maximum penalty equal to one-fourth of the annual penalty at risk for this performance area. It is clear that PSE's performance reflects significant swings in performance level and that the Company is allowing poor performance in early months to be offset by better performance later in the year when the monthly performance indicates that the annual standard will not be met. Customers deserve a more acceptable level of performance throughout the year. Finally, I recommend that PSE be required to report on its monthly and annual call abandonment rate and busy out rate as part of its annual SQI report, although I do not recommend any penalty dollars associated with these reporting metrics at this time.

Q: How does PSE return the penalty dollars incurred when the company fails to meet one of more of the SQI performance standards?

A: Pursuant to previous approval by the Commission, customers are informed of the annual service quality results and the dollar amount of any penalty that results for the failure to meet a performance standard in a PSE "report card" to customers. The penalty dollars are credited to the Electric Conservation Service Tracker as an offset to the tariff rider account.

Q. Do you recommend any change in how SQI penalty dollars are returned to customers?

A. Yes. I recommend that SQI penalty dollars be returned directly to customers in the form of a one-time bill credit that is appropriately identified on customer bills as a result of a service quality failure. PSE's customers should see the results of the SQI performance as a direct reduction in their overall rates. While I do not suggest that anything incorrect has occurred in the prior method of handling SQI penalty dollars, it is appropriate that the customers be informed of the impact of SQI failures directly since one of the key purposes served by the SQI mechanism is to link the rates that customers pay with PSE's customer service performance. Furthermore, the current method of applying any SQI penalty dollars to the Electric Conservation Service Tracker is complicated and confusing because of the need to assure that shareholders and not ratepayers bear responsibility for any SQI penalty payments to customers.

Q: Does PSE track and properly monitor the performance of their contractors who provide new installation services to customers?

A: PSE does track customer satisfaction with its service provider contractor services and reports these results to the Commission annually in a Service Provider Report. The results of customer satisfaction with new customer construction dropped dramatically in 2007 compared to 2006, which PSE attributes in part to the volume of storm recovery work that took precedence over new service installation. PSE has developed customer satisfaction level objectives or targets for their contractors, but these targets were not met in 2007. Furthermore, the target satisfaction levels are different, 83 percent for the gas contractor and only 75-78 percent for the electric construction contractor.[46] The current SQI, in contrast, requires that the transaction-based customer satisfaction survey results show a 90 percent customer satisfaction performance. In fact, when the SQI was modified as part of the 2002 PSE rate case settlement, all three customer satisfaction measures were set at 90 percent. However, the survey results for new customer installation reflected in these Service Provider reports are not reflected in the SQI customer satisfaction transaction surveys.[47]

Q: What is your recommendation with respect to PSE's customer satisfaction performance for new installation of service performed by its contractors?

A: I recommend that PSE be required to include penalties in its outside contractor agreements so that the failure to meet customer satisfaction targets is linked to payments to the contractors. With respect to the proper customer satisfaction targets, there is no reason why these satisfaction targets should be any different than those already applicable to PSE in the SQI for its field operations, i.e., 90 percent. PSE should then report on any penalties incurred in its outside contractor agreements to the Commission as part of the current Service Provider Reports that are filed annually. Any penalty dollars paid for substandard contractor

[46] PSE Response to WUTC Staff Data Request No. 164.
[47] PSE Response to WUTC Staff Data Request No. 187.

performance will result in lower costs incurred by PSE for the contracted services, in effect providing a benefit to PSE because the expected costs for these contracted services are reflected in the revenue requirement. In the event that contractor performance results in penalties, any penalties should be added to any penalty dollars incurred by PSE under the SQI and paid to customers. This approach will ensure that shareholders bear the risk of any poor performance by PSE's contractors.

In addition, I recommend that the current SQI customer satisfaction survey for PSE's field performance include a representative sample of new installation service customers reflected in these service provider contracts beginning in 2008.

Q: Have you reviewed PSE's performance with respect to Gas Safety and Electric Safety Response Time?

A: Yes. PSE is required to respond to Gas and Electric safety calls and appear on site within 55 minutes on average over an entire year. In other words, PSE's actual performance will naturally vary, but the average response time during the entire year must be 55 minutes or less. I asked PSE to restate their recent performance using a different performance standard that is used in other service quality plans with which I am familiar, that is, to provide the percentage of response calls in which PSE arrived within 60 minutes. Based on this response, it appears that PSE responded to gas safety calls within 60 minutes in 2007 only 86 percent of the time and there is a noticeable deterioration from 2005 through

2007.[48] PSE's response to electric safety calls shows a similar deterioration in performance.

Q: Do you have a recommendation for a change in the standard for Gas and Electric Safety Response Time in the SQI?

A: Yes. I think that the annual average of 55 minutes allows a much broader range of acceptable performance than should be permitted for responding to safety calls, particularly with natural gas service. I recommend that the performance standard require PSE to answer 95 percent of such calls within 60 minutes. According to one natural gas utility in Pennsylvania, this is an "industry average" for natural gas utilities. In addition, this standard is in effect for Massachusetts natural gas utilities.[49]

V. PSE'S LOW INCOME PROGRAMS: PROPOSED CONDITIONS

Q: Please describe PSE's low income bill payment assistance program.

A: PSE's HELP program served approximately 18,000 low-income residential customers in 2007 (approximately 14,000 electric customers and 6,000 gas customers, but note that approximately 2,300 HELP customers are duel fuel PSE customers). The average 2007 electric benefit was $373 and the average gas benefit was $344. The total dollar amount of HELP electric bill payment assistance was $5.2 million. The total dollar amount of HELP gas bill payment

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[48] PSE Response to Public Counsel Data Request No. 672, Attachment A.
[49] Columbia Gas of Pennsylvania tracks its performance in answering natural gas safety calls and reports that it arrives on site in 60 minutes or less 95 percent of the time. [Data response issued in pending rate case before the Pennsylvania PUC, Docket No. R-2008-2011621]. The Massachusetts Commission has established a performance standard of 95 percent response within 60 minutes applicable to all natural gas utilities in its Order establishing Service Quality Standards in 2001 in Docket 99-84, pages 39-40. See http://www.mass.gov/Eoca/docs/dte/electric/99-84/masterorder.pdf.

assistance was $2.2 million, resulting in total HELP benefits equal to $7,501,705.[50] In addition, administrative and enrollment costs were $1.8 million. The costs of this program are recovered from all customers through PSE's electric and gas tariff rider Schedules 129. PSE customers are qualified for HELP based on the same household income guidelines that are used by LIHEAP, which in Washington is 50 percent of the area's median household income, with an upper bound cap of 150 percent of federal poverty guidelines and a lower bound of 125 percent of federal poverty guidelines, depending on the local area's median household income. As a practical matter, this means that the eligibility criterion for LIHEAP and HELP is 125 percent of the federal poverty guidelines in PSE's service territory. I should point out that Washington's LIHEAP criteria are below the maximum allowed by federal law which is 150 percent of federal poverty guidelines.

The HELP benefit is calculated by the local community action agencies who deliver LIHEAP. The benefit reflects a formula that takes into account the customer's household income and energy usage and attempts to target larger benefit amounts to those with the most significant energy burden, i.e., the largest disparity between the actual bill and the customer's ability to pay the bill. The benefit is provided in the form of a lump sum benefit on the customer's bill, similar to the manner in which the LIHEAP benefit is applied to the customer's bill.

[50] PSE Response to Public Counsel Data Request No. 689, Attachment A.

Q: Does PSE know whether this program meets the needs of its low-income customers in terms of penetration rate and impact of the program on bill payment and retention of essential electricity or gas service?

A: PSE does not know what percentage of low-income customers are served by HELP. Furthermore, PSE has not done any evaluation of the effectiveness of the HELP program in terms of impact on affordability and retention of service. PSE's reports on this program do not reflect any analysis of HELP's impact on regular bill payment, keeping payment plans, or avoiding disconnection of service.[51] Nor has PSE done an analysis of HELP on PSE's customer collection costs, including bad debt expense.[52]

Q: Please describe the energy needs of PSE's low-income customers.

A: According to a recent report on Washington state energy needs, done by Apprise, Inc. for the Washington Office of Community Trade and Economic Development,[53] 14 percent of all households in Washington have a total household income at or below 125 percent of the federal poverty level and an additional 4 percent of all households have an income between 125 percent and 150 percent of the federal poverty level. Of these households, 72 percent of the households in Washington with income at or less than 125 percent of the federal poverty level have an energy burden that is greater than 5 percent of their annual household income and 46 percent of these households have an energy burden greater than 10 percent of income. With regard to PSE's low-income households, the report

[51] PSE Response to Public Counsel Data Request No. 472.
[52] PSE Response to Public Counsel Data Request No. 471.
[53] Washington State Energy Needs: Final Report (December 2007). Available at www.appriseinc.org.

estimated that 73 percent had a household energy burden in excess of 5 percent and 49 percent had an energy burden at 10 percent of more. Such households would have to allocate 10 percent of their household income to pay for vital and essential electric and gas service.

This study also found that a high percentage of low-income households have "high" electric bills in Washington: 62,000 had high baseload electric bills (over 8,000 kWh annual usage), 84,000 had high electric heating bills (over 16,000 kWh annual usage), and 6,000 had high gas heating bills (over 1,200 therms annual usage). The percentage of PSE's low-income customers with "high" usage was estimated at 69 percent, 34 percent and 16 percent, respectively. This information confirms that low-income customers have a high penetration rate for electric heat. In fact, the Report estimates that the main heating fuel for 67 percent of PSE's low-income customers is electric heat and only 21 percent rely on natural gas for their main heating fuel.

PSE has over 1 million residential electric customers and 713,000 residential gas customers. The Report estimates that 10 percent of PSE's customers or 171,300 have income at or below 125 percent of poverty. Based on the 18,000 customers served by HELP in 2007, PSE's program only serves 10-11 percent of those eligible for the program. I calculate that PSE's HELP program reaches approximately 12 percent of eligible electric customers based on the higher level of participation of PSE's electric customers in HELP.

Q: Are your concerns about the needs of PSE's low-income customers exacerbated by the current economic recession?

A: Of course. The credit and mortgage crisis and the crushing burden of just paying for gasoline and food are beginning to ripple through the economy. Job losses or lack of growth in employment, increased applications for Food Stamps and other financial assistance programs are indicators of the impact these economic trends are likely to have on the ability of PSE's low-income customers to pay for and retain essential electricity and natural gas service. For example, the Washington Economic and Revenue Forecast Council's February 2008 Forecast documented the decrease in housing starts and rising unemployment rate.[54]

Q: What is your response to the Joint Applicants' proposal to continue the current funding level for PSE's low income programs as a commitment in this proceeding?

A: A continuation of current funding for HELP is not sufficient. The historical practice of linking increased HELP funding to the percentage increase in rates at the time of a base rate case does not respond to the sale transaction at issue here. Furthermore, this approach is an insufficient method to establish the funding level for this program. HELP funding should also be increased beyond that level to begin to assure a steady progress in reaching out and enrolling qualified low-income customers into this program.

I recommend that the Commission should approve an approach that focuses on increasing the enrollment of qualified HELP customers over a several year period. PSE can recover the actual costs associated with any level of HELP enrollment and reset the ratepayer recovery mechanism to reflect actual costs. As

[54] This report is available at the ERF website: www.erfc.wa.gov.

a condition of the approval of this transaction, I recommend that PSE be authorized to file for a change in the Schedule 129 HELP cost recovery surcharge no more than once per year and that the Commission authorize cost recovery for a total increase in customer participation of approximately 5,000 new HELP customers over the 2007 program performance of 18,087. Furthermore, I recommend that PSE establish a priority to increase its enrollment of electric low-income customers. Based on the current average electric benefit of $373, additional HELP benefits for 4,500 electric customers would cost approximately $1.68 million. Based on the average gas benefit of $344, HELP benefits for an additional 500 gas customers would cost approximately $173,000. My recommendation is intended to focus primarily on low-income electric customers since they have the greatest energy burden and there are fewer low-income gas customers served by PSE.

In conclusion, the new owners of PSE should commit to an increase in the total HELP budget to reflect (1) the percentage of any future residential rate increase approved by the Commission; (2) the new enrollment objectives described above so that the program can grow to meet the needs of low income customers; and (3) the proportional administrative and program costs associated with the implementation of this increased enrollment.

Q: Please describe PSE's funding for low-income energy efficiency and demand side management programs.

A: PSE provides funding for cost-effective home weatherization measures for low-income gas and electric heat customers. Funds are used for single-family, multifamily, and mobile home residences. The participants in this program are referred by the low-income and crisis service agencies and qualification is done by the same agencies that operate the U.S. Department of Energy Weatherization Program. PSE recently has agreed to increase the amount paid for the various measures that are installed under these programs, a welcome development since the reimbursement rates for these measures had not changed in many years and the older rates do not reflect the increased cost of materials, labor and transportation for these programs. However, the overall budget has not increased to reflect these increased payments for the weatherization measures.

Prior to 2007, PSE spent an average of $2.2 million for this program as part of a large and very robust energy efficiency and conservation budget.[55] In general, PSE's energy efficiency program funding has increased significantly for residential and commercial customers, but the comparable level of increase has not been implemented for the low-income programs. PSE has increased energy efficiency program funding from $18.7 million in 2003 to $35.4 million in 2006**,** an 89 percent increase. However, the funding for the low-income program essentially remained level during this same period.

Q: Do you think this is adequate funding for this program?

A: No. The flat funding for this program does not reflect the underlying increases in prices charged for electricity and gas service by PSE since 2003 with the constant filing of base rate and fuel price increases. Nor does this level of funding reflect

[55] PSE Response to Public Counsel Data Request No. 566, Attachments A and B are the source of the spending levels for the various energy efficiency programs in this section.

the impact of PSE's intent to provide additional financial support for the various measures allowed to be paid for by this program. PSE's Response to Public Counsel Data Request No. 92 states that the Company filed an updated measures list in April 2008, pursuant to Section 2 of the Company's conservation tariffs, based on an analysis of the cost effectiveness of the weatherization measures included in the program. According to this data response, this update resulted in an increase in the low-income weatherization (LIW) measure payment levels by 45.8 percent for electric (over prior levels) and by approximately 45 percent for gas (in total). Therefore, it would be necessary to increase the current level of funding by approximately 45 percent just to reflect the increased cost of these existing measures.

While it is no doubt appropriate to increase payments for these measures due to the underlying costs incurred by the weatherization contractors and the cost-effectiveness of the new guidelines, the ultimate result is that a flat level of funding will reduce the number of homes that can be weatherized. Finally, this flat level of funding does not reflect the impact of higher prices likely to come from implementation of Washington's green house gas and carbon legislation and the growing indicators of an economic recession. All of these factors will put significant pressures on low-income families to afford the basic necessities of electricity and natural gas service and suggest that PSE should increase the funding for low-income weatherization programs.

Q: Please describe the additional funding for low income energy efficiency that was provided as a result of the Puget/Washington Natural Gas merger.

A: As part of its discussions with representatives of low income agencies and advocate organizations, PSE agreed to a $5 million contribution from its shareholders for low-income energy efficiency programs over a five year period (1998 through 2002). This funding was in addition to tariffed funding for this purpose. This valuable contribution was used to greatly expand the number of weatherization "jobs" that could otherwise have been done using the tariffed funding during this time period. A total of $2.9 million was used for electric low income customer weatherization measure installation and $1.27 million for low income gas customer weatherization measures, with the balance allocated to other administrative purposes.[56]

Q: What level of increased funding for low-income energy efficiency programs do you recommend?

A: I have two recommendations, both of which are intended to increase funding for low income energy efficiency and weatherization programs. First, I recommend that PSE increase its ratepayer funding for the low-income energy efficiency program by $1.5 million each year beyond PSE's current budget for the 2008-2009 biennium. Due to the increased cost of the approved low-income measures, this is actually only a $500,000 increase in the total budget for this program. Second, it would be reasonable and I recommend that the Commission require as a condition for approval of this proposed sale of PSE for an additional shareholder contribution to the low-income energy efficiency programs in the amount of $7.25

[56] PSE confirmed this arrangement and provided background information on how the funds were allocated and spent in PSE's Response to Public Counsel Data Request No. 570 (with attachments).

million over five years, similar to the contribution that PSE made to this effort in 1997. This amount is calculated with a 45 percent increase from the 1997 contribution to account for the increased cost of the approved low-income weatherization measures. In both cases, PSE should work with the provider agencies to develop a plan to implement this increased level of funding over a 12-24 month period.

Q: Does this complete your testimony at this time?

A: Yes.