

BEFORE THE WASHINGTON UTILITIES AND TRANSPORTATION COMMISSION

**WASHINGTON UTILITIES AND
TRANSPORTATION COMMISSION,**

Complainant,

v.

PUGET SOUND ENERGY, INC.,

Respondent.

DOCKET UG-110723

**INITIAL POST-HEARING BRIEF
OF COMMISSION STAFF
RECOMMENDING REJECTION OF THE
PIPELINE INTEGRITY MANAGEMENT SURCHARGE**

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**ROBERT M. MCKENNA
Attorney General**

**ROBERT D. CEDARBAUM
Assistant Attorney General
Office of the Attorney General
Utilities & Transportation Division**

**1400 S Evergreen Park Drive SW
P.O. Box 40128
Olympia, WA 98504-0128
(360) 664-**

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I. INTRODUCTION

1 On April 26, 2011, Puget Sound Energy, Inc. (“PSE” or the “Company”) filed Schedule 134 with the Washington Utilities and Transportation Commission (“Commission”). Schedule 134 is a new surcharge dedicated to accelerated recovery of Company investments to replace three types of natural gas pipe: wrapped steel services, wrapped steel mains and older Polyethylene Pipe (“Older PE”). PSE asserts that the surcharge will enhance the safety and reliability of its natural gas delivery system by allowing a more proactive approach to pipeline integrity management.¹ The Commission suspended the tariff on July 15, 2011.

2 Commission Staff is well aware that the Company’s provision of safe and reliable natural gas service is of critical importance to the public interest. The Commission’s Pipeline Safety Staff is dedicated to that endeavor through its enforcement of state and federal pipeline safety laws and rules. The Commission’s Regulatory Services Staff is similarly committed through the rate setting process so that PSE receives sufficient revenues to fulfill its public safety obligations.

3 However, the proposed surcharge is flawed in several respects that warrant its rejection by the Commission. First, the new surcharge will require ratepayers to prepay the costs of pipeline infrastructure that is not used and useful to provide them service, in violation of RCW 80.04.250.

4 Second, even if the Commission were not to reject the new surcharge as a matter of law, the surcharge should still be rejected because the Company’s natural gas pipeline system is already safe and reliable, and the Company states it is committed to maintaining a safe and reliable pipeline system even without the surcharge. Indeed, as it has done in the

¹ Exhibit TAD-1T at 2:16-18.

past, PSE has the financial ability to expand the scope of its pipeline integrity efforts with cost recovery of associated investments accomplished successfully through general rate cases. Recent heightened awareness of pipeline safety issues by other states and the Federal government does not warrant a different approach.

5 Third, Schedule 134 will guarantee for PSE and its owners the substantial benefit of expedited cost recovery of pipeline investments between general rate cases. However, the Company did not clarify the scope and timing of pipeline replacement to be funded by the new surcharge, other than to design the surcharge to expedite recovery of investments that are already planned even without the surcharge. Thus, ratepayers will not benefit from the surcharge because they will pay higher rates sooner, but with no assurance that their money will enhance safety through accelerated pipeline replacement.

6 Finally, the Company intends the surcharge to be flexible so that additional programs can be added and a \$25 million annual cap on capital spending can be increased. These changes would require Commission approval, but do not require the consent of Staff or any other interested party. Thus, the surcharge opens the door to further efforts by PSE to transfer the risk of cost recovery from its owners to ratepayers. It also adds another potentially complex and adversarial tariff process to the multitude of risk-reducing mechanisms already enjoyed by PSE.

II. ARGUMENT

A. **The Commission Should Reject the Surcharge as a Matter of Law Because It Allows Recovery of Investments that are Not “Used and Useful”**

7 In order for any capital expenditure made by a utility to be included in rate base for ratemaking purposes, the investment must be “used and useful for service” in Washington

State.² The State Supreme Court has held that “used” means “employed in accomplishing something” and “useful” means “capable of being put to use: having utility: advantageous; producing or having the power to produce good; serviceable for a beneficial end or object.”³ The “used and useful” standard presupposes that actual expenditures have been made for an asset that is operational, before the asset can be included in rate base and recovered from ratepayers.⁴

8 The Company’s proposed surcharge violates the “used and useful” standard because, by its very design, it recovers forecasted investment through October 31st of an upcoming program year.⁵ Thus, beginning on November 1st of each program year, ratepayers prepay PSE for expenditures the Company has not incurred on plant that is neither in service nor capable of providing service. The budgeted funds recovered through the surcharge also do not qualify for the construction work in progress exemption from the “used and useful” standard because the funds are collected from ratepayers for plant construction that has not begun. Therefore, the Commission should reject the surcharge as a matter of law.

² RCW 80.04.250. The legislature has provided only two exceptions to the “used and useful” requirement. One exception is for construction work in progress and, then, only if the Commission finds that including CWIP in rate base is “in the public interest”. RCW 80.04.250. The other exception allows rates to recover funding of a reserve account for capital improvements, but that exception applies only to water companies and then only for capital improvements approved or required by the Department of Health or Department of Ecology. RCW 80.28.022.

³ *Power v. Utils. & Transp. Comm’n*, 430 Wn.2d 452, 430, 679 P.2d 922 (1984) (uncompleted power plant is not “used and useful” because it is neither employed for service nor capable of being put to use for service). The Commission has articulated its view that in order for an asset to be “used and useful” and recovered in rates, the asset must provide quantifiable benefits to Washington ratepayers that are commensurate with their costs. *WUTC v. PacifiCorp d/b/a Pacific Power & Light Co.*, Docket UE-050684, Order 05 at ¶ 27 (July 14, 2006). We demonstrate in Section II.B.1 below, that the Company’s proposal fails the benefits test for rate base treatment.

⁴ Leonard Goodman, *The Process of Ratemaking* 799 (1998).

⁵ Exhibit JHS-3 at 3. For example, for the first program year, the surcharge is based on actual capital investments for the three categories of pipeline from July 1 2010 through July 31, 2011 and forecasted capital investments from August 1, 2011 through October 31, 2012. Exhibit JHS-1T at 3:14-17 and Exhibits JHS-5 (wrapped steel services), JHS-6 (wrapped steel mains), and JHS-7 (Older PE).

9 The Company attempts to challenge this conclusion, but none of its arguments have merit. First, PSE argues that the “used and useful” standard is of no concern because the surcharge is based on an average of monthly average of planned additions to plant.⁶ This argument is a smokescreen because the average of monthly average calculation still includes the budgeted costs of plant that is not in service at the beginning of a program year when ratepayers begin to pay the surcharge.⁷

10 Next, the Company says the “used and useful” standard is not an issue because of a process under which the amounts PSE collects in revenues will be compared to the actual amounts PSE should have collected, and any differences will be trued-up.⁸ The Commission should acknowledge this Company argument and reject the surcharge, because PSE concedes that the surcharge will require ratepayers to prepay for investment PSE has not yet made for plant and, thus, is not used and useful for service.

11 The Company also offers some examples in an attempt to support its arguments, but upon examination, none excuse the surcharge from compliance with RCW 80.04.250. First, the Company states that conservation expenditures are also forecast and trued-up to actual for the rate year.⁹ However, what PSE did not disclose until hearing is that conservation expenses are expenses that are not included in rate base and, therefore, do not implicate RCW 80.04.250.¹⁰

12 The Company then refers to the inclusion in rate base of new electric generation facilities.¹¹ However, the Commission cannot test this example because PSE did not provide

⁶ Exhibit JHS-10T at 2:3-7.

⁷ For example, the revenue deficiency for wrapped steel services that is based on an average of monthly average includes projected capital expenditures for August 2011 through October 2012. Exhibit JHS-5.

⁸ Exhibit JHS-10T at 2:7-9 and Exhibit JHS-3 at 3.

⁹ Exhibit JHS-10T at 2:14-15.

¹⁰ Tr. 110:7-10 (DeBoer).

¹¹ Exhibit JHS-10T at 2:10-14.

the Commission the name of even one such facility that was included in rate base before that facility actually went into service. Like PSE, Staff also cannot name any facility that somehow escaped application of the “used and useful” standard, and was placed in rate base before it became operational. This is not surprising, because, as PSE agrees, the very purpose of the Power Cost Only Rate Case procedure is to synchronize rate recovery of a new generation facility with the date the facility begins providing service to ratepayers,¹² thereby complying with RCW 80.04.250.

13 Finally, PSE refers to the Commission’s recent discussion of a “flexible approach” to determining whether plant is “used and useful”.¹³ The context of that discussion, however, was the statutory mandate for electricity utilities to acquire renewable resources of sufficient amounts to meet the portfolio standards of the Energy Independence Act, RCW 19.285. In contrast, the Company agrees that the surcharge proposed in this docket is not necessary for PSE to meet its statutory obligation to maintain a safe natural gas delivery system.¹⁴

14 More important, the Company fails to describe fully the Commission’s thinking. While PSE correctly notes the Commission’s statement that it will consider whether plant provides benefits to customers, PSE fails to note the Commission’s admonition that the plant must still be “employed” in accomplishing something beneficial.¹⁵ It is this aspect of the “used and useful” standard that disqualifies the proposed surcharge.

15 In fact, some of the plant that the Company seeks to include in rate base for recovery through the surcharge is not employed in accomplishing anything at the time ratepayers pay

¹² Tr. 214:4-12 (Story).

¹³ Exhibit JHS-10T at 3:1-4, citing, *Report and Policy Statement Concerning Acquisition of Renewable Resources by Investor-Owned Utilities*, Docket UE-100849 (January 3, 2011).

¹⁴ Exhibit TAD-4T at 6:14-15.

¹⁵ *Report and Policy Statement Concerning Acquisition of Renewable Resources by Investor-Owned Utilities*, Docket UE-100849, ¶ 31 (January 3, 2011).

the surcharge because the plant literally does not even exist. The Commission's most recent writing on the "used and useful" standard fully supports Staff's conclusion that the surcharge should be rejected as a matter of law.

B. The Proposed Surcharge Should Be Rejected Because It Is Single-Issue Ratemaking with No Justification or Ratepayer Benefit

16 The proposed surcharge would separate cost recovery for pipeline replacement activities without consideration of all other components of the Company's overall revenue requirement. This constitutes "single-issue ratemaking" which is generally disfavored by the Commission:

In particular, we disfavor and typically avoid single-issue ratemaking and we are careful to preserve so far as is reasonable the "matching principle" that relies on our consideration of all revenues, costs and adjustments in the context of a test year with a definite ending date.¹⁶

The Commission confirmed in PSE's 2006 general rate case that it will not approve mechanisms that constitute single-issue ratemaking without evidence of extraordinary and compelling reasons:

It requires extraordinary circumstances to support a departure from fundamental ratemaking principles. In prior cases the Commission has required 'a clear and convincing showing that the Company will be denied any reasonable opportunity to earn its authorized rate of return without extraordinary relief.'¹⁷

17 Like the proposed surcharge here, the Company's proposal in 2006 was a tracker to address regulatory lag in the recovery of infrastructure replacement costs incurred between general rate cases.¹⁸ The Commission rejected the tracker, stating:

¹⁶ *WUTC vs. Puget Sound Energy, Inc.*, Dockets UE-060266 and UG-060267, Order 08 at ¶ 37 (January 5, 2007).

¹⁷ *Id.* at ¶ 39, citing *WUTC v. Washington Natural Gas Co.*, 4th Supp. Order at 29-30, Docket UG-920840 (September 27, 1993) and stating "Staff is correct to argue that [a departure from fundamental ratemaking principles] should be granted only under extraordinary circumstances and with clear evidence that the utility would be harmed without such relief."

¹⁸ *Id.* at ¶ 36, and Tr. 212:15-213:10 and Tr. 235:16-236:3 (Story).

PSE has not demonstrated financial circumstances that might justify the extraordinary relief represented by the proposed tracker mechanism. Nor has the Company demonstrated that regulatory lag will prevent it from making investments necessary to maintain reliable service to its electric and gas customers.

In short, the record simply does not support and we cannot approve a novel mechanism to change rates that will shift risks and costs to ratepayers without the benefit of a full review of revenue and expenses.¹⁹

18 The Commission has also rejected a tracker to recover the costs of a Company pipeline replacement program, even when that program itself was ordered expressly by the Commission to address public safety. While the Commission did not at that time frame the test in the same terms as it later did in PSE's 2006 rate case, the Commission still did require a showing of unique circumstances before it would diverge from base rate recovery of safety-related expenses:

The Commission rejects the use of a tracker mechanism to recover compliance-related expenditures. A tracker is a unique method of recovering costs and a departure from ordinary ratemaking treatment. Earlier in this proceeding, the Commission stated the factors to be considered in determining when a tracker is appropriate. Expenses which are easily measurable, beyond the company's control, and which are both substantial and essential to the company's operations may be recovered through a tracker. The Commission has also generally required that there be substantial ratepayer benefit.

In this case, the tracker would offer dollar-for-dollar recovery of certain safety-related expenditures, most of which have not been shown by the company to be incremental to its normal operations. Additionally, the total amount to be expended is unknown at this time, but the expenditures are within the company's control. To the extent these safety-related expenditures, for which recovery is sought via a tracker, are prudently incurred and required by the company's obligation to serve, they are recoverable as operating expenses or as incremental investment when they are known and measurable. Recovery will be considered in future proceedings.²⁰

¹⁹ *Id.* at ¶¶ 41-42.

²⁰ *WUTC v. Washington Natural Gas Company*, Docket No. UG-920840, Fourth Suppl. Order at 6 (September 27, 1993). The pipeline replacement program at issue was the cast iron system of Washington Natural Gas Company that the Commission previously ordered replaced in Docket UG-920487. *WUTC v. Washington Natural Gas Company*, Docket No. UG-920487, First Suppl. Order (June 19, 1992).

19

PSE argues that it must not show extraordinary circumstances for the Commission to approve the surcharge because WAC 480-07-505(2)(a) recognizes that the Commission can authorize periodic rate adjustments and the Commission has done so in the past.²¹ The issue, however, is not whether the Commission has the authority to approve a periodic rate adjustment and that it has previously exercised that authority. Clearly it has that authority and clearly that authority has been exercised. Rather, the issue is the standard to be applied for approval. PSE's argument is irrelevant to that issue.

20

But even if PSE is correct that extraordinary circumstances need not be proven, PSE failed to present evidence of any reason, extraordinary, compelling or otherwise, that would justify Commission approval of the new surcharge. Nor has the Company demonstrated that approval of the surcharge is essential to PSE's operations or will create substantial ratepayer benefits. In fact, just the opposite has been proven on this record.

1. The Surcharge Will Benefit the Company with Guaranteed Accelerated Cost Recovery but with No Assurance for Ratepayers of Enhanced Safety through Accelerated Pipeline Replacement

a. Ratepayer Benefits from the Surcharge Cannot Be Assessed Because the Scope, Timing and Cost of Pipeline Replacement has Not Been Determined

21

The Company states that the proposed surcharge is intended to "promote a more proactive approach to pipeline integrity management that will benefit ratepayers by encouraging increased levels of investment in pipeline replacement that will enhance the

²¹ Exhibit TAD-4T at 12:3-5. The Company also argues that the Commission noted in the 2006 general rate case that recovery of infrastructure replacement could be undertaken outside of a general rate case. Exhibit TAD-4T at 12:1-7, citing, *WUTC vs. Puget Sound Energy, Inc.*, Dockets UE-060266 and UG-060267, Order 08 at ¶ 51 (January 5, 2007). However, PSE ignores the Commission's statement in the very same paragraph of the very same order, that recovery of infrastructure replacement outside a general rate case is allowed only if "the investments are shown to be prudent, the amounts are reasonable, and the plant is demonstrated to be used and useful." Earlier we demonstrated that PSE's surcharge fails the "used and useful" test. Elsewhere in this brief we demonstrate that the Company's proposal is vague as to the process for addressing the remaining issues of prudence and reasonableness.

safety and reliability of PSE's natural gas delivery system."²² PSE makes this claim even though it did not first analyze the costs and benefits for ratepayers of an accelerated pipeline replacement program.²³ Nor did the Company propose any ongoing method to evaluate the success or failure of the surcharge in achieving ratepayer benefits.²⁴

22

The Company argues that specific performance criteria and cost/benefit analysis are unnecessary because ratepayer benefits from the surcharge are qualitative in nature and should be accepted by the Commission on the basis of intuition alone.²⁵ However, PSE did not estimate the amount of pipeline that would be replaced with the new surcharge in effect nor did it develop a schedule over which pipeline remediation will occur.²⁶ Without this information, the Commission has no reason to take the leap of faith PSE requests because the Commission cannot judge whether efforts funded by the surcharge will actually result in accelerated pipeline replacement and, even if it does, whether the cost to ratepayers is worth those efforts.²⁷ In fact, ratepayers may be worse off with the surcharge because they will pay higher rates faster, but with no assurance that their money will fund accelerated replacement of pipeline infrastructure. PSE and its owners, on the other hand, will receive the substantial benefit of guaranteed full cost recovery on an expedited basis.

²² Exhibit TAD-1T at 2:16-18 and Exhibit DAH-1T at 16:3-5.

²³ Exhibit DAH-29.

²⁴ Exhibit DAH-30. The one apparent exception is that PSE claims that the effectiveness of the pipeline replacement program will be evaluated based on trending leak performance. Exhibit DAH-21. However, the Company admitted it will not be able to attribute any improvements in leak performance to efforts funded through the surcharge because PSE will not know what pipe would have been replaced absent the surcharge. *Id.* and Tr. 148:13-24 (Henderson). Thus, the leak performance evaluation will have no probative value in assessing ratepayer benefits from the surcharge itself.

²⁵ Exhibit TAD-4T at 3:13-4:7 and Exhibit DAH-30.

²⁶ Exhibit DAH-1T at 6:9-15 (wrapped steel services), 8:1-5 (wrapped steel mains) and 9:10-14 (Older PE). Exhibit DAH-4T at 5:8-9. No estimates or timeline for pipeline replacement have been developed because the Company is still in the process of gathering information, monitoring performance, calibrating various risk models, and, in the case of Older PE, implementing a geographic information system to better understand the inventory and location of pipeline. Exhibit DAH-1T at 6-9 and Tr. 132:21-133:1 (Henderson).

²⁷ Exhibit DAH-1T at 10: Table, which includes expenses planned currently, but does not estimate the cost of additional pipeline that may be replaced under the surcharge.

23

The Company does not deny the lack of specific planning around the scope, timing and cost of a pipeline replacement program. It asks the Commission to approve the surcharge despite that missing information because its proposal includes annual consultations with Staff and other interested parties whom PSE envisions will agree on a pipeline replacement program for each following year.²⁸ The Company acknowledges, however, that the parties will not always agree on eligible investments and that additional litigation may be required to resolve outstanding issues.²⁹ It is ill-advised for the Commission to approve a new tariff mechanism that, by its very design, may create additional litigation, especially given the frequency and complexity of other filings already to be made by PSE that will require significant agency time and resources.³⁰

b. The New Surcharge Will Not Encourage Investment Above and Beyond Expenditures Already Planned Without the Surcharge

24

The Company's asserted goal for the new surcharge is for ratepayers to benefit from enhanced pipeline system safety and reliability. To accomplish that goal, the surcharge should be designed to encourage pipeline investment above and beyond what the Company already budgets in its normal course of business without the surcharge.³¹

25

PSE's proposal does not meet that requirement because the new surcharge would recover pipeline remediation expenditures defined expressly as the difference between plant

²⁸ Exhibit TAD-4T at 7:14-22.

²⁹ Exhibit TAD-4T at 8:10-16 and Tr. 115:5-16 (DeBoer). In fact, it is possible that disagreement could arise within the Commission itself between Pipeline Safety Staff agreeing to a replacement program from an engineering perspective and Regulatory Services Staff contesting the program from a cost perspective. Tr. 114:20-115:4 (DeBoer).

³⁰ The Company analogizes to its Conservation Resource Advisory Group ("CRAG") as the type of collaborative process it envisions for the new surcharge. Exhibit TAD-4T at 8:6-9. However, the Company's latest conservation targets were the subject of recent litigation because the CRAG participants could not initially reach agreement. *WUTC v. Puget Sound Energy, Inc.*, Docket 100177, Order 05 (September 28, 2010). Staff recommends that the Commission not establish a similar potentially adversarial process for pipeline replacement programs.

³¹ Exhibit MV-1T at 3:20-4:6.

balances already budgeted and plant balances at the end of the test year established in the Company's most recent general rate case.³² Since these "incremental" expenditures are already planned, they are contemplated even without the new surcharge.³³ No additional mechanism is necessary to encourage PSE to make these investments if they are necessary to maintain a safe and reliable pipeline system.

26 As noted above, the Commission rejected a prior Company surcharge for safety-related expenditures, in part, because "the tracker would offer dollar-for-dollar recovery of certain safety-related expenditures, most of which have not been shown by the company to be incremental to its normal operations."³⁴ The same reason exists for the Commission to reject the proposed surcharge in this docket.

2. No Reason, Extraordinary or Otherwise, Has Been Proven that Would Warrant Commission Approval of the New Surcharge

a. The Company's Pipeline System is Already Safe and Reliable and PSE is Committed to Keeping the System Safe and Reliable Without the Surcharge

27 There are two points that the Company readily and adamantly asserts without equivocation: first, the current pipeline system is safe and reliable and, second, PSE will continue to invest in pipeline replacement to keep the system safe and reliable even without the new surcharge.³⁵ The record supports the Company's conclusion that the new surcharge

³² Exhibit JHS-1T at 4:1-8. It is, therefore, error for the Company to state that the new surcharge will allow PSE the ability to accelerate funding for pipeline integrity initiatives "beyond the level currently budgeted in any particular year." Exhibit TAD-1T at 4:20-22.

³³ For example, the end of the test year in the last general rate case was June 30, 2010. Thus, the proposed revenue deficiency in this case of \$1.9 million is calculated from planned additions to plant of \$16.4 million from July 2010 through October 2012. Exhibit JHS-4. That additional investment of \$16.4 million is planned by PSE even without the surcharge. Likewise, replacement of wrapped steel services and mains designated for Priority Replacement or Scheduled Replacement was already budgeted by PSE without the surcharge, but still was used to develop the revenue deficiency to be recovered through the surcharge. Exhibit MV-1T at 8:2-19.

³⁴ *WUTC v. Washington Natural Gas Company*, Docket No. UG-920840, Fourth Suppl. Order at 6 (September 27, 1993).

³⁵ Pipeline system already safe and reliable: Exhibit TAD-1T at 3: 14-15, 4:12-13 and 6:14-16; Tr. 84:8 (DeBoer). PSE will continue to invest in pipeline replacement without surcharge: Exhibit DAH-1T at 18:14-

is not necessary to maintain a safe and reliable pipeline delivery system that PSE asserts already exists and will continue to exist.

28 First, under federal law, the Company is required to develop and implement a distribution integrity management program (“DIMP”) that requires PSE to continually identify, assess and monitor risks on its pipeline system.³⁶ DIMP does not require pipeline replacement, but it does formalize PSE’s existing practices that already include comparable pipeline integrity methods and activities for wrapped steel services and mains and Older PE.³⁷ Thus, the new surcharge is not necessary for PSE to comply with DIMP requirements. Nor is it necessary to comply with federal requests for the Company to review its system to identify high risk pipeline and prioritize critical repair.³⁸ PSE has no plans to discontinue any pipeline integrity management practices even if the Commission rejects the surcharge.³⁹ To the contrary, PSE states that as new emerging trends are identified it will develop strategies and policies to mitigate risks in order to meet the requirements of DIMP.⁴⁰

29 Indeed, PSE has already increased the frequency of leak surveys for wrapped steel and the Company believes that its current regimen of leak survey frequency is assigned appropriately so that all categories of pipe are continually inspected and monitored.⁴¹ These pipeline integrity management efforts have yielded significant information about the condition of pipeline that would be addressed by the new surcharge. According to PSE, a majority of the remaining wrapped steel services fall within the lower risk category and are

19, Exhibit TAD 4T at 9:19-22, Exhibit DAH-7 at 2 (paragraphs b and c); Tr. 118:17-23 (DeBoer), Tr. 119:16-20 (DeBoer), Tr. 169:5-10 (Henderson), Tr. 170:5 and 24-25 (Henderson).

³⁶ Exhibit DL-1T at 2:18-3:17.

³⁷ Exhibit DAH-1T at 3:1-7, 16:13-14 and 17:1-7, Exhibit DAH-11 and Exhibit DAH-12; Tr. 86:11-13; Tr. 156:9-13 (Henderson).

³⁸ Tr. 165:21-166:5 (Henderson).

³⁹ Tr. 165:9-12 (Henderson).

⁴⁰ Exhibit DAH-7 at 15.

⁴¹ Exhibit DAH-7 at 13 and 28; Tr. 142:12-15, Tr. 150:4-8 and 15-19 (Henderson), and Tr. 154:25-155:2 (Henderson).

“in good condition and will continue to reliably and safely provide natural gas service for many years.”⁴² Of the 91 and 303 wrapped steel services designated for the highest “Priority Replacement” and “Scheduled Replacement”, respectively, all but two have already been replaced.⁴³ Likewise, according to the Company, “a majority of wrapped steel mains are performing very well and we expect they will continue to reliably provide gas services for years to come.”⁴⁴

30 Staff acknowledges heightened concern with Older PE that may be more prone to failure and has a higher chance for leaks to be hazardous than other categories of pipe.⁴⁵ However, according to PSE, higher risk “Dupont” pipe is a relatively small portion (one-eighth) of the Company’s plastic pipe system.⁴⁶ The remaining Older PE uses other high quality materials which have performed as designed.⁴⁷ Even the Dupont plastic pipe that does exist has operated without a high leak rate or number of incidents.⁴⁸ It has performed well and is expected to continue doing so.⁴⁹

31 In fact, the new surcharge would have no impact on the leading threat to the safety of the Company’s pipeline system, namely, damage from third party excavation which is the leading cause of both pipeline leaks (54 percent) and reportable incidents on the Company’s system.⁵⁰ Moreover, PSE’s bare steel pipeline system has the highest number of active leaks

⁴² Exhibit DAH-1T at 6:5-6 and Exhibit DAH-4T at 7:20-8:4.

⁴³ Exhibit DAH-9 and Exhibit DAH-22

⁴⁴ Exhibit DAH-1T at 7:6-7 and Exhibit DAH-4T at 8:12-13.

⁴⁵ Exhibit DL-1T at 5:12-6:14 and Exhibit DAH-7 at 36.

⁴⁶ Tr. 161:2-8 (Henderson). Staff was not as certain as the Company on the amount of Dupont plastic pipe, stating that the extent of Dupont pipe is uncertain since historical documentation does not provide sufficient detail to determine the precise quantities and location of installations. Exhibit DL-1T at 6:20-23 and Tr. 242:17-243:10 (Lykken).

⁴⁷ Exhibit DL-1T at 6:23-7:3.

⁴⁸ Tr. 253:9-13 (Lykken).

⁴⁹ Tr. 161:13-17 (Henderson).

⁵⁰ Exhibit DAH-22 at 13, Pie Chart. Corrosion and material and weld failure are the next leading causes of leaks on the system, but they represent only 8 percent and 7 percent of leak repairs, respectively. Exhibit DAH-7 at 36.

per mile, the highest number of repaired leaks per mile, and the highest number of leaks scheduled for repair per mile.⁵¹ Thus, the Company's main focus of attention is already being addressed without the surcharge through PSE's existing bare steel replacement program, which will conclude at the end of 2014.⁵²

32 For other types of pipeline, a majority of leaks are designated Class C, meaning they are non-hazardous and are expected to remain non-hazardous.⁵³ Higher risk Class A and B leaks have declined 50 percent and 65 percent, respectively, because of the replacement of cast iron, bare steel and Older PE.⁵⁴ The bottom line from the Company's own analysis is that overall system performance shows significant improvement as the number of hazardous leaks in each material type has declined.⁵⁵

b. The Company Has Already Taken Action to Enhance the Safety and Reliability of Its Pipeline System without a Surcharge

33 As Staff described, the Company has already taken a proactive approach to pipeline integrity management:

PSE has taken a number of steps to improve system performance and reduce the public's exposure to risk. Most of these safety management programs relate to safety and compliance, training, compliance auditing, and continuing surveillance. In addition, many programs have already been implemented and some completed to address the risk associated with older vintage materials such as cast iron and bare steel pipe. PSE is also focusing on the highest priority areas including reducing third party damage and replacing and leak surveying pipe where there are integrity concerns. As a result, the number of hazardous and total leaks repaired has continued to decline. These decreases indicate that the overall system performance has improved.⁵⁶

⁵¹ Exhibit DAH-4T at 8:17-9:8 and Exhibit DAH-7 at 12

⁵² Exhibit DAH-1T at 4:11-12

⁵³ Exhibit DAH-7 at 24 and 28, and Exhibit DAH-24, Graph.

⁵⁴ Exhibit DAH-7 at 11 and Exhibit DAH-8; Tr. 139:3-7 (Henderson) and Tr. 143-144:2 (Henderson).

⁵⁵ Exhibit DAH-7 at 11 and 21.

⁵⁶ Exhibit DL-1T at 4:20-5:6.

The Company could provide no reason why it could not continue its proactive approach to pipeline integrity management without the new surcharge.⁵⁷

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In fact, the Company was eager to explain how its gas pipeline integrity programs have expanded over the past decade, when no special ratemaking treatment was allowed. Some specific examples PSE presented of these new and expanded integrity management initiatives include:

- Complete replacement of all cast iron pipe,
- Expediting the replacement of bare steel pipe,
- Developing and implementing a risk ranking and remediation methodology for wrapped steel mains and services and Older PE,
- Remediating buried meters and risers,
- Conducting increased leak surveys,
- Enhancing the damage prevention program, and
- Implementing transmission and distribution integrity management programs.⁵⁸

It is the case that the cast iron and bare steel replacement programs resulted from Commission complaints and orders. However, many of these enhanced pipeline integrity initiatives go above and beyond Commission-ordered activities, as do other opportunities identified by PSE to reduce overall system risk such as integrating the Wrapped Steel Services Assessment Program Priority Replacement and Scheduled Replacement services with the Bare Steel Risk Model.⁵⁹

⁵⁷ Exhibit DAH-8.

⁵⁸ Exhibit DAH-1T at 3:13-4:4 and Exhibit DAH-3.

⁵⁹ Tr. 207:14-208:13 (Henderson) and Exhibit DAH-7 at 54.

35 Indeed, the Company's 2010 Continuing Surveillance Annual Report states that PSE's overall strategy is to initiate new pipeline integrity management programs and enhancements to existing programs as necessary.⁶⁰ For example, to address damage from third party excavation, the Company is continuing to increase and refine its damage and prevention awareness program, under which it has seen significant reductions in third party damage over the past several years.⁶¹ The Company also initiated a new policy in 2010 to replace pre-1986 PE services as part of larger main replacement programs such as the bare steel replacement program.⁶² According to PSE, leak survey trend analysis shows that PSE's leak survey, odorization and public education programs are effective in detecting and proactively mitigating leaks.⁶³

36 A full list of current and completed gas system maintenance programs is described in the 2010 Continuing Surveillance Annual Report at pages 53-65. All of these proactive measures were undertaken without expedited cost recovery through any means. The vast majority of them were not Commission-ordered activities.

c. Cost Recovery Through Traditional Ratemaking Procedures is Sufficient To Support an Accelerated Pipeline Replacement Program

37 The new surcharge would guarantee the Company and its owners accelerated recovery of the cost to replace wrapped bare steel mains and services, and Older PE. PSE agrees, however, that the Commission has never disallowed recovery of the costs to replace any category of pipeline under traditional, general rate case ratemaking.⁶⁴

⁶⁰ Exhibit DAH-7 at 9-10 and Tr. 136:16-21 (Henderson).

⁶¹ Exhibit DAH-7 at 52.

⁶² Exhibit DAH-7 at 60.

⁶³ Exhibit DAH-7 at 13.

⁶⁴ Exhibit TAD-4T at 8:20-21 and Exhibit TAD-10.

38 Indeed, the Company filed natural gas general rate cases in 2004, 2006, 2007, 2009,
2010 and 2011.⁶⁵ These cases, and others, have, without exception, allowed PSE to recover
significant costs related to accelerated pipeline replacement programs, including \$80 million
for cast iron pipeline replacement and \$83.5 million for bare steel pipeline replacement.⁶⁶

39 This trend should continue for the pending general rate case in Docket UG-111049
and the general rate case the Company expects to file in 2012.⁶⁷ PSE agreed that it will
always be able to recover budgeted expenditures for pipeline replacement through general
rate cases once costs have been incurred and the amounts are shown to be prudent.⁶⁸
Likewise, PSE agreed that it could accelerate pipeline replacement beyond budgeted levels
and recover related costs through existing cost recovery methods without a surcharge.⁶⁹

40 PSE's sole complaint is regulatory lag: the requirement of having to wait until the
next general rate case to recover costs associated with any accelerated pipeline replacement
program.⁷⁰ However, the Company ignores the fact that not all general rate cases require the
full statutory suspension period. In its 2010 general rate case, the Commission approved a
full settlement and granted rate relief only 6 months after the case was filed and only 9
months after the test year used in the case.⁷¹ A key driver for that rate relief was continued
high levels of capital funding to meet significant pipeline infrastructure investments.⁷²

41 Moreover, the Commission has held that regulatory lag is a self-regulating
mechanism inherent in historical test year ratemaking that creates the proper incentives for

⁶⁵ Tr. 211:6-22 (Story).

⁶⁶ Cast iron: Exhibit DAH-13 and Tr. 127:24-128:15 (Henderson); Bare steel: Exhibit DAH-10: Table 10 (2003-2009) and Tr. 60:23-61:3 (DeBoer).

⁶⁷ Tr. 67:18-22 (DeBoer).

⁶⁸ Tr. 60:10-13 (DeBoer) and Tr. 62:16-18 (DeBoer).

⁶⁹ Tr. 63:14-22 (DeBoer) and Tr. 65:19-66:10 (DeBoer), Exhibit DAH-5, and Tr. 212:15-213:13(Story).

⁷⁰ Tr. 212:15-213:10 (Story) and Tr. 235:16-236:3 (Story).

⁷¹ Exhibit MV-1T at 9:13-10:4.

⁷² *Id.*, citing Exhibit SML-1T at 14-15 (Docket UG-101644).

an efficient and effective management.⁷³ The Company states that it always has and always will have sole responsibility for the operation and safety of its pipeline system.⁷⁴

Commission rejection of the surcharge will hold the Company to that responsibility.

d. The Company Has the Financial Ability to Fund an Accelerated Pipeline Replacement Program Without the New Surcharge

42 The record shows that the Company has the financial wherewithal to fund an accelerated pipeline replacement program even without the new surcharge. The Company's investment in pipeline replacement has increased over the last decade without accelerated cost recovery and is expected to continue to increase without accelerated cost recovery.⁷⁵ PSE has spent at least \$28 million beginning in 2008. The Company's current investment plans call for spending of \$34 million in 2011 and greater amounts in later years.

43 PSE does not dispute that it is financially able to accelerate the replacement of targeted pipeline without the new surcharge. PSE argues, instead, that a majority of actual and budgeted spending has been devoted to the bare steel replacement program.⁷⁶ Therefore, according to PSE, the surcharge will "remove barriers" by allowing the Company to accelerate the replacement of other pipeline beyond current plans without those efforts having to compete in the Company's overall capital investment budgeting process.⁷⁷

44 However, the bare steel replacement program will be completed in 2014. This will free up a significant funding that can be devoted to the replacement of the categories of pipeline that would be targeted by the proposed surcharge.

⁷³ *WUTC v. Puget Sound Energy, Inc.*, Dockets UE-090704 and UG-090705, Order 11 at ¶ 23 (April 2, 2010). See also *WUTC v. Puget Sound Power & Light Company*, Cause No. U-81-41, 2nd Supp. Order at 20 (March 12, 1982) and *Bluefield Water Works and Improvement Co. v. Public Service Commission of West Virginia*, 262 U.S. 679, 693 (1923) (establishment of a fair rate of return reflects expectation that utility is operated efficiently).

⁷⁴ Exhibit TAD-4T at 9:9-10 and Exhibit DAH-4T at 3:6-9.

⁷⁵ Exhibit DAH-1T at 10, Table.

⁷⁶ Exhibit TAD-4T at 12:15-13:3.

⁷⁷ Exhibit TAD-1T at 3:2-11 and Exhibit DAH-1T at 14:15-19.

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Moreover, the accelerated pipeline replacement program envisioned by the PSE is an exceedingly small part of the Company's overall budget for its utility operations, which is financed on total-Company basis, not an individual program basis.⁷⁸ Indeed, the \$25 million that PSE might spend on targeted programs is miniscule compared to the \$2.5 billion the Company may spend in the next 3 years to support energy supply and delivery infrastructure needs.⁷⁹ Despite expectations of these significant overall capital expenditures, PSE's bond ratings have improved.⁸⁰ These improved ratings occurred given investor expectations that regular general rate cases will occur in order to minimize the effects of regulatory lag.⁸¹

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It is, therefore, difficult to envision there being any obstacle to accelerated pipeline investment without accelerated cost recovery through the proposed surcharge. But even if such obstacles do arise, they would not interfere with the Company's ability to insure the safety of its pipeline system. PSE committed that public safety would never take a back seat to other capital spending and management will always approve funds for additional spending on pipeline infrastructure whenever necessary to protect the public safety.⁸²

e. The Surcharge Is Not Justified By Federal and Other State Initiatives Regarding Pipeline Replacement

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PSE must install and maintain facilities as are necessary to provide safe and reliable service to the public. This responsibility is not new or remarkable. It is PSE's fundamental and long-standing statutory obligation.⁸³ Thus, any need to proactively replace aging and higher risk pipeline is not an extraordinary circumstance. It is part of the normal course of infrastructure improvements to ensure continued safety and reliability.

⁷⁸ Tr. 89:1-3 (DeBoer) and Tr. 261:25-262:22 (Crane).

⁷⁹ Exhibit TAD-9 at Public Counsel, page 4.

⁸⁰ Exhibit TAD-9 at Public Counsel, page 3.

⁸¹ Exhibit TAD-9 at Public Counsel, page 4.

⁸² Tr. 107:23-108:5 (DeBoer), Tr. 137:18-138:10 (Henderson), Tr. 185:6-10 (Henderson), and Tr. 187:25-188:3 (Henderson).

⁸³ RCW 80.28.010(2).

Nevertheless, the Company argues that the surcharge responds to a “nationally recognized need to accelerate the replacement of pipeline that is prone to failure and is pervasive throughout the natural gas delivery system in this country.”⁸⁴ However, the federal initiatives cited by PSE also recognize that pipeline incidents resulting in serious injury or death are down nearly 50 percent over the last 20 years.⁸⁵ While recent incidents certainly have ramped up attention to the replacement of pipeline infrastructure, those incidents involved facilities not targeted by the surcharge: a high pressure transmission pipeline in California and old cast iron systems in Pennsylvania.⁸⁶ Indeed, federal initiatives emphasize pipelines made of bare steel and cast iron that are many decades old and not expected to be replaced for many decades in the future.⁸⁷ None of these circumstances pertain to PSE’s system which has no cast iron pipe and which is already scheduled to eliminate all bare steel pipe by 2014.

PSE cites other state commissions that have approved surcharges for accelerated pipeline replacement programs as evidence of a “new landscape” encouraging such activity. However, in the only relevant court case we could find, the Illinois Court of Appeals recently overturned a commission decision approving an accelerated pipeline replacement surcharge.⁸⁸ The court held that the surcharge constituted single-issue ratemaking that was not justified by special circumstances warranting a deviation from traditional ratemaking procedures.⁸⁹ The court was not persuaded by the utility’s argument that the program would benefit the public because of enhanced safety.⁹⁰ The court also rejected the utility’s

⁸⁴ Exhibit TAD-4T at 12:8-11. See also, Exhibit TAD-1T at 8:10-13.

⁸⁵ Exhibit TAD-5 at 2 and 3.

⁸⁶ Tr. 168:11 and 168:23-169:1 (Henderson).

⁸⁷ Exhibit TAD-5 at 3 and 5-6 and Exhibit TAD-6 at 4; Tr. 166:16-167:4 (Henderson).

⁸⁸ *People ex rel, Lisa Madigan v. Illinois Commerce Comm’n*, 2011 WL 4580558 (Ill. App. 1 Dist.).

⁸⁹ *Id.* at 10, ¶ 42.

⁹⁰ *Id.* at 4, ¶ 16.

argument that the surcharge would allow it to proceed with the accelerated pipeline replacement program and avoid regulatory lag.⁹¹

50 Even the commission decisions cited by PSE should be viewed with caution by the Commission. Of the forty-four utilities granted such mechanisms, almost half (nineteen) hailed from states with specific statutes (Kansas, Kentucky, Missouri, Nebraska, Texas and Virginia) or state economic recovery initiatives (New Jersey) authorizing such mechanisms.⁹² No such initiatives are present in our state.

51 In fact, in a state like ours without such initiatives, the Maryland Public Service Commission recently denied an accelerated pipeline replacement surcharge even though it approved the underlying pipeline replacement program itself:

The Commission has reviewed the issues and positions of the parties and finds that the Company's proposed [Accelerated Pipeline Replacement Plan] has merit and represents a laudably proactive approach to mitigate risk. The Company should, in our view, replace aging pipelines proactively as part of its normal course of infrastructure improvements to ensure continued safety and reliability, and should do so at a pace that minimizes health and safety risks to its customers.

We are not, however, convinced that surcharge recovery is an appropriate, let alone necessary, quid pro quo for the Company to accelerate the replacement of aging pipes, as in several cases, we decline to deviate from traditional ratemaking process and adopt the proposed Rider surcharge.⁹³

In rejecting the surcharge, the Maryland commission noted factors similar to those on record in this case: the utility's commitment to maintain a safe and reliable pipeline system for its customers that would continue even without the surcharge, and the company's operational and financial ability to accelerate its existing pipe replacement program and recover the associated costs in base rates with an appropriate return.

⁹¹ *Id.* at 4, ¶ 16.

⁹² Exhibit TAD-3.

⁹³ *In the Matter of the Application of Washington Gas Light Company*, Case No. 9267, Order 84475 at 106-108 (November 14, 2011). http://webapp.psc.state.md.us/Intranet/Maillog/orders_new.cfm.

52 Our point is that different commissions take different approaches based upon the specific facts and circumstances they are presented. The Commission should reject PSE's tactic that urges the Commission to "jump on the band wagon" and approve the new surcharge given the shortcomings of the Company's proposal that we have highlighted.

f. The Surcharge is Not Necessary for Commission Pipeline Safety Staff to Advocate for Enhanced Pipeline Replacement

53 The Company argues that the annual consultation process envisioned by the new surcharge will allow members of the Commission's Pipeline Safety Staff more opportunity than they have presently to advocate for work they would like to see done by PSE.⁹⁴ However, the record demonstrates that Pipeline Safety Staff already has full opportunity to promote pipeline safety measures it wants the Company to undertake. The surcharge process adds nothing of significance.

54 In fact, Pipeline Safety Staff and PSE already communicate on a more regular and frequent basis than would be required under the surcharge.⁹⁵ Those meetings occur both quarterly and monthly.⁹⁶ They provide a forum for Pipeline Safety Staff to advocate for pipeline replacement work they believe PSE should pursue.⁹⁷ They also have already resulted in Pipeline Safety Staff review of the risk model used by PSE to set priorities for pipeline replacement.⁹⁸

55 Both Pipeline Safety Staff and PSE agree that these communications will continue even if the Commission rejects the surcharge.⁹⁹ That forum will include Pipeline Safety

⁹⁴ Exhibit TAD-4T at 11:2-5 and Exhibit DAH-4T at 2:17-19 and 8:1-3.

⁹⁵ Tr. 52:9-15 (DeBoer).

⁹⁶ Tr. 128:25-130:5 (Henderson).

⁹⁷ Tr. 52:9-15 (DeBoer) and Tr. 130:6-13 (Henderson)

⁹⁸ Tr. 198:22-199:1 (Henderson) and Tr. 243:21-24 (Lykken).

⁹⁹ Tr. 246:1-8 (Lykken), Tr. 53:2-5 (DeBoer), and Tr. 130:6-16 (Henderson).

Staff consultation on the Company's plastic pipeline replacement efforts, as well as the Company's integration of DIMP regulations that went into effect recently in August 2011.¹⁰⁰

56 The Company does not dispute that consultations between PSE and Pipeline Safety Staff have resulted in accelerated replacement of higher risk pipeline. The Company's accelerated cast iron and bare steel pipeline replacement programs are examples.¹⁰¹

57 Instead, PSE argues that these prior efforts occurred in the context of Commission formal complaints, rather than through non-adversarial collaboration between Pipeline Safety Staff and the Company.¹⁰² As we explained above, however, non-adversarial results are still not guaranteed under the annual consultations that would occur with the surcharge.

58 Moreover, since prior Commission complaints were successful in accelerating the replacement of higher risk pipeline like cast iron and bare steel, perhaps that is the process that should also be used to accelerate pipeline replacement targeted by the new surcharge.

C. The Proposed Surcharge is Flawed Because It Does Not Define the Process by Which Pipeline Replacement Projects Would be Reviewed

59 Earlier we explained why the lack of specificity by PSE regarding the scope, cost and timing of a pipeline replacement program negates any showing of ratepayer benefit from paying higher rates sooner under the new surcharge. This lack of clarity extends to the process PSE envisions for review by stakeholders and the Commission itself of pipeline replacement projects that nevertheless would be recovered through the new surcharge.

60 In fact, it became quite clear during the hearings that the Company simply has not thought through important procedural details of its proposal, including exactly when and

¹⁰⁰ Tr. 246:12-247:2 (Lykken).

¹⁰¹ Tr. 126:16-127:23 (Henderson).

¹⁰² Tr. 52:17-53:1 (DeBoer). The cast iron replacement program was ordered by the Commission on June 19, 1992 in its First Supplemental Order in Docket UG-920487. The bare steel replacement program was ordered by the Commission on January 31, 2005 in Order No. 02 in Dockets PG-030080 and PG-030128.

how projects would be reviewed for prudence and cost. All PSE could clarify is that the Commission would be presented with an initial filing that would contain a rate designed to recover budgeted costs for projects that may or may not be listed with the filing or agreed upon by stakeholders:

Chairman Goltz: Now, at your proposal, you started talking about this collaborative process to result in a prudence determination. Is that what you are envisioning?

Mr. DeBoer: In an ideal world, yes.

Chairman Goltz: But that's not necessarily your proposal, or is it your proposal?

Mr. DeBoer: Well, no – I don't know that we – we haven't got to that level of detail. I guess in discussions here, you know, in the initial filing, we would say here's our list of proposals, here's the budgets that go with them, here's the rate to collect it. And whether we say, you know, as part of the order we want a prudence determination or whether that waits until the true-up in the following year, we haven't – we haven't gotten that far.

* * *

Chairman Goltz: But would your mechanism, as proposed, work if you were way at the informal end of the continuum I described; that is to say that Mr. Henderson and his staff had informal conversations with Mr. Lyyken and his staff about what you're planning to do, not dissimilar to, I believe, what is happening now?

Mr. DeBoer: I'm comfortable with that, as long as – I mean, what it really boils down to is what's in the filing when you say here's the budget and here's the rate we want to collect in this filing, and how much backup or, you know, the Commission or parties to the proceeding want to see backing up that rate. I'm comfortable without the [project] list.¹⁰³

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The Company asks the Commission to ignore these important process issues because any question concerning the prudence or cost of a project can be addressed at a later time when projected costs are true-up to actual costs.¹⁰⁴ As we suggested above for the used and useful issue, the Commission should accept PSE's argument as a concession to the underlying vagueness of its proposal, and reject the surcharge on that basis.

¹⁰³ Tr. 101:4-19 (DeBoer) and Tr. 103:4-17 (DeBoer).

¹⁰⁴ Exhibit TAD-4T at 7:20-22 and Tr. 116:9-11713 (DeBoer).

D. The Surcharge Mechanism Does Not Limit the Cost or Categories of Pipeline for Which Accelerated Recovery Could Be Guaranteed

62 The proposed surcharge states that it is limited to the replacement of wrapped steel mains and services, and Older PE.¹⁰⁵ The tariff also states that it is limited to total annual capital expenditures of \$25 million and will expire in 2016.¹⁰⁶

63 However, the Company stated that the surcharge is intended to be flexible to allow the addition of other safety programs and higher levels of costs.¹⁰⁷ Thus, the limitations on scope and annual expenditures apply only at the outset.

64 The tariff does state that Commission approval is required before pipeline replacement costs can be increased above \$25 million per year or qualified programs enlarged beyond wrapped steel mains and services and Older PE. However, the Company can request Commission approval to expand the scope and dollar limit of the surcharge without the consent of Staff and other interested parties, who would, then, have the burden to recommend that a revised surcharge should be rejected or suspended in the face of Company claims of potential threats to public safety.¹⁰⁸

65 Moreover, PSE has been quite successful in securing Commission approval of accounting petitions and other mechanisms that reduce regulatory lag and mitigate PSE's risk of cost under-recovery.¹⁰⁹ The Commission should be wary of any tariff mechanism intended specifically as a means to further insulate PSE from the risk of cost under-recovery not only for the initial programs and costs allowed by the tariff, but additional programs and higher costs PSE can unilaterally request to be covered by the surcharge.

¹⁰⁵ Exhibit JHS-3 at 3.

¹⁰⁶ Exhibit JHS-3 at 4.

¹⁰⁷ Exhibit TAD-1T at 3:17-20, Exhibit DAH-6, and Exhibit DAH-19.

¹⁰⁸ Tr. 62:1-7 (DeBoer) and Tr. 113:23-114:13 (DeBoer).

¹⁰⁹ Exhibit JHS-12.

III. CONCLUSION

66 As explained above, the Commission should reject the proposed surcharge as unlawful under RCW 80.04.250. The surcharge should also be rejected on the merits because it has not been shown to benefit ratepayers or to be necessary for the Company to either maintain or enhance existing pipeline integrity measures or to adopt new measures to meet its public service obligation to provide safe and reliable natural gas service. Unresolved process issues also warrant rejection of the new surcharge.

67 Nevertheless, Staff is sympathetic to the concern expressed by the Citizen Advisory Committee on Pipeline Safety, which did not take a position on the proposed surcharge, but did state that:

The Committee understands that this filing represents a rate policy discussion that is beyond our scope of knowledge and responsibility. Our mission is the safety of the state's pipeline systems. We believe all parties share this concern. If this particular case does not result in a replacement investment strategy for PSE, we encourage all parties to continue to work together to find a consensus approach to spurring investment in replacing vintage pipe. We ask the Commissioners to establish a process for such discussions to continue until resolution.¹¹⁰

Staff agrees that the discussions requested by the Committee should continue, but believes they should be industry-wide rather than focusing on one company. Staff suggests that the Commission establish a workshop among all regulated natural gas companies and interested stakeholders to explore generally the policy and ratemaking considerations inherent in

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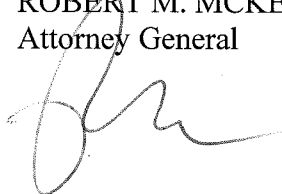
¹¹⁰ Exhibit BE-1 at 5.

pipeline replacement strategy. Such a workshop could also be the jumping off point for an interpretive and policy statement or other appropriate proceeding such as a rulemaking.

DATED this 16th day of December 2011.

Respectfully submitted,

ROBERT M. MCKENNA
Attorney General



ROBERT D. CEDARBAUM
Assistant Attorney General
Counsel for Washington Utilities and
Transportation Commission Staff