

BEFORE THE WASHINGTON UTILITIES AND TRANSPORTATION COMMISSION

WASHINGTON UTILITIES AND)	
TRANSPORTATION COMMISSION,)	
)	
Complainant,)	Dockets UE-121697 and UG-121705
)	<i>(Consolidated)</i>
v.)	
)	
PUGET SOUND ENERGY, INC.,)	Dockets UE-130137 and UG-130138
)	<i>(Consolidated)</i>
)	
Respondent.)	
_____)	

EXHIBIT NO. ___ (MCD-4)

Excerpt of Transcript of Thomas E. Schooley

April 26, 2013

1 revenue from Cap X?

2 A. For operating expenses, yes.

3 Q. All right. And what about the underlying trend in
4 the RPC values?

5 A. That's an "or," so it's not necessarily a part of the
6 collected notions. We were concentrating on the capital
7 expenditures of the past few years, and the budgeted capital
8 expenditures of the next few years, as well as the trends and
9 the operating expenses of the past few years and anticipated
10 operating expenses. The trends for the operating expenses in
11 particular were not adhered to in developing a reasonable
12 K-Factor in that instead of the percentages of the operating
13 expense growth, it was looked at as a -- as a cost of living
14 increase or CPI index minus half a percent was applied to the
15 operating expenses.

16 And then an average of the Cap X depreciation and
17 operating expenses was used. This is explained in Ms. Barnard's
18 testimony in her exhibits.

19 Q. All right. So Staff's analysis consisted of
20 reviewing Ms. Barnard's exhibits?

21 A. And finding them reasonable, and that the 3 percent
22 K-Factor was well below what the trends would indicate, so it
23 seemed like a reasonable proposition.

24 Q. And was anything else reviewed besides her testimony?

25 A. What type of things do you have in mind?

1 Q. Anything that you can tell me about.

2 A. No. The testimony seemed to cover the approach and
3 the needs well.

4 Q. And who on Staff worked on that analysis?

5 A. I did.

6 Q. Any other Staff people?

7 A. No.

8 Q. Does any portion of your testimony in the exhibits
9 filed in support of the global settlement discuss the K-Factor
10 or any analysis Staff conducted in support of the 3 percent
11 K-Factor?

12 A. Yes, I believe it's in my testimony.

13 Q. And that testimony is the testimony supporting the
14 settlement?

15 A. Yes.

16 Q. All right. Any other testimony in the record from
17 Staff with regard to that 3 percent K-Factor?

18 A. No.

19 Q. In terms of the global settlement, what is the
20 problem that the K-Factor is seeking to solve?

21 A. There are the -- as you mentioned, the capital
22 expenditure growth in the next few years, and the operations
23 growth. The K-Factor will provide some relief from the expenses
24 that will be incurred, but not enough, and the Company will need
25 to manage its expenses if it is to earn its authorized return.

1 So I think that's what the K-Factor is intended to do, and it's
2 only in the delivery costs.

3 Q. So is it fair to say it's intended to address
4 earnings erosion?

5 A. It's intended to recover the costs incurred for
6 capital expenditures and expense growth over the next few years.
7 Without it, yes, there would be earnings erosion, as there would
8 be in any event.

9 Q. Ms. Reynolds testifies that the decoupling proposal,
10 which includes the K-Factor, is intended to address attrition;
11 would you agree with that?

12 A. I don't care for the word "attrition." It seems to
13 have been loosely used for many different purposes depending on
14 the -- the purpose the person who's speaking it wishes to have.

15 I think of it as more simply a plan to recover costs
16 that are expected in the future; yet not sufficient to give the
17 Company -- or that alone wouldn't sufficiently compensate the
18 Company for their expenses.

19 So I -- I don't know what term you're using attrition
20 as. It's a loose term in the -- as it's been used in the last
21 couple of years.

22 Q. Would you agree that we could use the definitions
23 that the Commission or Commission Staff people have used to
24 describe attrition?

25 A. I don't think there's been consistent use of it

1 between the Commission and the Staff or -- or over time, so...

2 Q. Do you recall that the Avista general rate case
3 involved attrition issues?

4 A. There were attrition studies and attrition issues
5 raised specifically in that case, yes.

6 Q. All right. Well, you've said that you don't like the
7 term "attrition."

8 Do you have a term that you would use in preference
9 such as earnings erosion? Would you prefer to use that term
10 rather than attrition?

11 A. No. I think -- I don't know if there's a particular
12 term I would use to describe what you imply is the purpose of
13 what we label the K-Factor. I think it's more just a simple
14 rate plan which is -- which the purpose is to avoid general rate
15 cases in the next three to five years. And there will be a
16 general rate case in 2015 or 2016 range, and this plan sort of
17 is able to give the Company some revenue relief for the costs it
18 will be incurring; yet not excessive amounts.

19 Q. But, surely, you would agree that the purpose of
20 that, the rationale for that, is to try to address the Company's
21 claims of attrition or earnings erosion, would you not?

22 A. Well, I would say the primary purpose is to address
23 the Company's known capital needs and expense growth over the
24 next few years. Attrition sort of implies other aspects of
25 moving pieces. If revenues are held constant, then, as they

1 would be coming out of -- or not held constant.

2 If the rates are held constant coming out of the last
3 general rate case and expenses are growing, you could say that's
4 earnings attrition -- or earnings reduction. It sort of just
5 goes with the nature of a regulated business.

6 Q. And how would you define attrition yourself?

7 A. I think the notion that it was used in the 1980s was
8 that there were inflationary impacts to costs absent even any
9 need for capital or new capital expenditures, and the attrition
10 was to show that the rates that were -- had been just set in
11 place or that were in place were insufficient to recover that
12 inflation of those inflationary needs.

13 The trend today isn't based on inflation, as much it
14 is on replacement of plans, which is not producing incremental
15 revenues such as -- as growth would be replacing new people
16 coming on. You have to serve them. They provide new revenues
17 without any rate change.

18 So, in essence, the answer to your question would be
19 that it is showing -- the attrition is showing that there are
20 costs and expenses that are growing faster than what the
21 revenues would.

22 Q. And that would be your definition of attrition today?

23 A. Yes.

24 Q. And does the amended decoupling plan with its
25 K-Factor in the settlement agreement help Puget Sound Energy

1 address that issue?

2 A. Yes, I believe it does; yet not entirely.

3 Q. Do you believe that Puget Sound Energy will be
4 considering filing for additional rate relief during the life of
5 the rate plan since their needs are not being fully addressed
6 based on your last statement?

7 A. I don't believe they'll be filing for additional rate
8 recovery for delivery revenues. The electric generation is a
9 separate issue and will be addressed in a power cost only rate
10 case, and through the power purchase agreement clauses that we
11 have agreed to in the global settlement, will require some
12 increases in the power cost side of things.

13 Absent that, no, I don't think they'll be requesting
14 any additional revenues in the next three to five years.

15 Q. You've referred to the power cost only rate case.

16 Is it correct that the settlement contemplates
17 that -- well, strike that.

18 Is it correct that the settlement does not place any
19 limitation on Puget Sound Energy's ability to file for
20 additional rate relief under the power cost only rate case
21 mechanism?

22 A. It does state that, but I think that was a
23 belts-and-suspenders-type approach to power costs getting out of
24 control. The PCORC, or power cost only rate case, is
25 anticipated to be filed in the next couple months. And as I

1 about 2013, correct?

2 A. Yes.

3 Q. Do you know what that number is for 2014?

4 A. There's no expedited rate filing in 2014. There is
5 only the rate plan, the 3 percent increase, to delivery revenues
6 which would translate to something in the 1 to 1 1/2 percent
7 range in total revenues. It will be a minor increase in total
8 rates.

9 Q. And do you know what the number is? And so the total
10 increase is less than 2 percent for 2014 in electric rates?

11 A. Yes.

12 Q. And do you know what the number -- the percentage is
13 for 2015?

14 A. Less than 2 percent.

15 Q. And do you know what the cumulative impact of the
16 rate plan is in dollars starting with the ERF, and then
17 including all the decoupling K-Factor increments through the
18 maximum life of the rate plan? Do you know what that number is?

19 A. I would pin that number at about \$130 million.

20 Q. And do you know what -- that's electric only?

21 A. Electric only.

22 Q. And do you know what the number is on the gas side?

23 A. I think it's about \$50 million.

24 Q. Can you turn to your -- I'm sorry. We already are
25 turned to your settlement testimony, Exhibit TES-1T.

1 permission now.

2 MS. DAVISON: I would recommend, given the timing,
3 that perhaps we could defer that --

4 MR. FFITCH: Right. I agree with that.

5 MS. DAVISON: -- issue until the end of the
6 deposition. I would like to get started on my questions with
7 Mr. Schooley.

8 MR. FFITCH: Correct. I agree with that. We will --

9 THE WITNESS: I agree with Ms. Davison.

10 MR. FFITCH: We'll take it up with the judge
11 subsequent to 4:30.

12 MS. DAVISON: All right. Thank you, Mr. ffitich.

13

14 E X A M I N A T I O N

15 BY MS. DAVISON:

16 Q. Mr. Schooley, as you know, I'm Melinda Davison. I
17 represent the Industrial Customers of Northwest Utilities, and I
18 would just like to ask you a few questions about your testimony
19 in this -- these dockets --

20 A. Okay.

21 Q. -- that are the subject of the global settlement.

22 Whose interest does Staff represent in these
23 proceedings?

24 A. The public interest.

25 Q. And can you define what the public interest is?

1 A. The public interest is a balance between the
2 customers of the utility, the utility itself, and broader needs
3 of the -- of the public.

4 Q. Thank you. Is it correct that the global settlement
5 agreement was negotiated between Staff and PSE?

6 A. Yes.

7 Q. And who represented the --

8 A. And NW Energy Coalition.

9 Q. My understanding is that the NW Energy Coalition came
10 in later at the end of the process; is that not correct?

11 A. Well, they were parties to the decoupling proposal
12 and were never excluded. Whether they directly participated in
13 certain terms, I'm not sure, but they were always present.

14 Q. Oh, I see. So the NW Energy Coalition attended all
15 settlement meetings that occurred between Staff and PSE?

16 A. I think so. I'm not sure. I mean, I wasn't
17 necessarily at all the meetings myself, so...

18 Q. Okay. Who represented the customer interest in the
19 settlement negotiations?

20 A. Staff had customers in mind.

21 Q. But isn't it true that Staff has to balance interests
22 that includes balancing the interest of the utility?

23 A. Which means we must keep the customers in mind when
24 we are proposing changes on accepting or rejecting the Company's
25 ideas.

1 Q. And isn't it true that no party in the settlement
2 negotiations strictly represented the customers' interests?

3 A. Staff did.

4 Q. Okay. Thank you. Do you believe that an attrition
5 study is necessary to validate a utility's claim of
6 under-earning?

7 A. No.

8 Q. Why not?

9 A. That's not the only way to determine whether there's
10 under-earning. I think historically, historic reports show that
11 adequately as well.

12 Q. And in this particular global settlement, you have
13 testified to PSE's under-earning. I think today you've called
14 it "chronic under-earning."

15 How did Staff go about validating that claim?

16 A. We reviewed and looked at the Commission basis
17 reports of the last several years, and -- as well as the history
18 of rate cases that have been presented.

19 Q. I would like to hand you -- sorry. That's a long
20 reach.

21 (Exhibit No. 4 marked.)

22 BY MS. DAVISON:

23 Q. You've been handed a document that is an excerpt of
24 your testimony dated December 7, 2011, from Docket UE-111048 and
25 049; do you recognize this testimony?

1 A. Yes.

2 Q. I would ask you to turn to page 6 of Exhibit 5 -- or
3 I'm sorry -- is it 4? -- of Exhibit 4.

4 A. I only have pages 8 and 9.

5 MS. DAVISON: Sorry. Maybe I've handed you the wrong
6 document. Let me try this one. Okay.

7 Here's another excerpt. Let's call this Exhibit 5.

8 (Exhibit No. 5 marked.)

9 BY MS. DAVISON:

10 Q. So Exhibit 5 is also another excerpt of your
11 testimony dated December 11, two thousand -- December 7, 2011,
12 in Dockets UE-111048 and 049.

13 And if I could ask you to turn to page 6 of your
14 testimony, and I would refer you to lines 12 through 19, do you
15 see that?

16 A. Yes.

17 Q. And, specifically, starting on line 13 in response to
18 a question you've posed, "Has PSE adequately proven its claim of
19 persistent under-earning," and you answer that question, "No,"
20 and go on to say: "...in general, the Company in its direct case
21 could have, but did not, provide an attrition study to determine
22 whether, and by how much, PSE is experiencing attrition due to
23 its need to invest in new rate base thereby denying it the
24 opportunity to earn a fair rate of return during the rate year";
25 do you see that?

1 A. Yes.

2 Q. Can you explain why Staff considered the failure to
3 provide an attrition study in the 2011 Puget rate case to be a
4 flaw but not in the current proceeding?

5 A. Well, I think in further review of the granting of
6 rates over the past several years versus the Commission basis
7 reports, it is more apparent that even in spite of regular rate
8 increases, the earnings are not materializing, so I've had
9 something of a change of heart.

10 Q. So you don't agree with the testimony that you
11 presented on page 6, lines 13 through 17 any longer?

12 A. I think in a sense this was, you know, more valid at
13 that time than it is now, so, I mean, "agree" is a little
14 strong. I think I have stated it that it's something of a
15 change of heart.

16 Q. And if I understand your testimony, you had a change
17 of heart based on looking at the results of operations or
18 Commission basis reports or -- or perhaps you could tell me why
19 you --

20 A. If we turn to Exhibit 4 --

21 Q. Okay.

22 A. -- and page 8 and the general rate cases filed in --
23 on line 14, 13 and 14, general rate cases were filed in 2004,
24 2006, 2007, 2009, 2010, and 2011. That history also is a strong
25 indication of under-earning chronically and the need for greater

1 revenues and the need for streamlining the process or coming up
2 with new ways to allow the Company a better opportunity to earn
3 its rate of return. The global settlement accomplishes that, or
4 we hope it will.

5 Q. And what do you mean by "accomplishes that"?

6 A. A new way of looking at rates. A new way of planning
7 for regular small increases. A new way to allow the Company to
8 manage its business as well.

9 Q. Did you read the deposition transcript of
10 Ms. Reynolds?

11 A. Most of it. It got boring at times.

12 (Reporter interruption for clarification.)

13 BY MS. DAVISON:

14 Q. So both you and Ms. Reynolds are referring to the
15 increases that are being proposed by the global settlement as
16 small increases.

17 Can you define specifically what you consider small
18 versus large?

19 A. I think large increases are more on the order of 7,
20 8, 9 percent, and the companies have often filed for even much
21 greater numbers than that.

22 Small increases are probably ones that are, you know,
23 4 percent or less.

24 Q. Okay. Thank you. In ICNU Data Request 4.8 --

25 A. To Staff?

1 Q. To Staff, and there's a response. I'm sorry. I
2 didn't bring multiple copies of it, but I just wanted to refer
3 you to...

4 A. 4.8?

5 Q. 4.8. ICNU has asked you for your documents that
6 demonstrate PSE's need for the 32 million revenue requirement
7 increase, and I believe that's the revenue requirement increase
8 being proposed by the expedited rate filing; is that correct?

9 A. Correct.

10 Q. And you see your response to that?

11 A. Yes.

12 Q. And do the documents that follow, which -- I believe
13 I have one, two, three, four, five, six, seven -- I have eight
14 pages that follow.

15 A. Yes.

16 Q. Are those all the documents that you considered in
17 reaching your independent determination for the need of a
18 \$32 million revenue requirement increase?

19 A. Well, there are also the documents provided by
20 Ms. Barnard in her testimony which are supportive of the
21 \$32 million.

22 Q. Right. And what we're asking for is any independent
23 analysis that Staff would have done to verify Ms. Barnard's
24 assertions.

25 A. Well, we -- my review of her filings and supporting

1 work papers, I concluded that the case filed was legitimate. It
2 was -- it didn't contain any -- any extraneous or nefarious
3 counts or a need for any other changes. It seemed to be a clean
4 case.

5 Q. Okay. Thank you. Did Staff conduct an analysis of
6 PSE's earnings for the year 2012?

7 A. We have -- I have seen no documents concerning the
8 whole of year 2012.

9 Q. Do you know whether PSE under-earned in the year
10 2012?

11 A. There have been no documents filed concerning the
12 whole year, 2012.

13 Q. Well, I'm asking you whether you know whether or not
14 PSE under-earned in the year 2012.

15 A. I don't know, because there's been nothing filed on
16 that regard.

17 Q. Okay.

18 A. It's not due to the Commission until the end of this
19 month.

20 MS. DAVISON: All right. We're on Exhibit 6.

21 (Exhibit No. 6 marked.)

22 BY MS. DAVISON:

23 Q. I want to hand you a document that is being marked as
24 Exhibit 6, and this is PSE's...

25 THE WITNESS: I can reach a little easier than Greg,

1 so...

2 BY MS. DAVISON:

3 Q. Sorry. Exhibit 6 is an excerpt of PSE's Form 10-K
4 report that is for the fiscal year ending December 31, 2012.

5 Have you reviewed this report?

6 A. (Witness reviews document.)

7 THE WITNESS: Were you going to say something?

8 MR. TRAUTMAN: Well, I'm objecting for the lack of
9 foundation. There's no evidence that the witness is even
10 familiar with this.

11 THE WITNESS: I have not seen this report.

12 MS. DAVISON: Well, that was the point of my
13 question, so I don't think -- and this is a deposition. I don't
14 have to lay a foundation. My question was whether Mr. Schooley
15 has reviewed this report or not.

16 THE WITNESS: No.

17 BY MS. DAVISON:

18 Q. Thank you.

19 A. When did this come out?

20 Q. It's dated December 31, 2012.

21 A. Well, when did it -- when was it submitted?

22 Q. I think you would have to ask PSE that question, but
23 I do have some follow-up questions about this particular
24 document.

25 A. I will be unable to answer them.

1 Q. If you look at this document marked Exhibit 6, and
2 you take a look at page 70, which I apologize for the
3 pagination. It is about halfway through that is entitled
4 (as read): "PUGET SOUND ENERGY CONSOLIDATED STATEMENTS OF
5 INCOME"; do you see that page?

6 MR. TRAUTMAN: Same objection to the question. Lack
7 of foundation. The document speaks for itself.

8 MS. DAVISON: Well, I understand that the document
9 speaks for itself, but the lack of foundation is not an
10 appropriate objection for a deposition in which I am inquiring
11 of the witness what he's reviewed and what he knows --

12 MR. TRAUTMAN: And he indicated --

13 MS. DAVISON: -- about the income in the earnings of
14 PSE, a topic in which he has testified to.

15 MS. BARNETT: I'm going to join in the objection. I
16 think you're asking about this particular document, not a
17 separate question about their earnings.

18 So to the regards to what PSE -- what PSE's document
19 says, I agree that there's a lack of foundation for Mr. Schooley
20 to answer.

21 MS. DAVISON: Well, you can pose that objection, but
22 I'm going to continue on with my questions.

23 BY MS. DAVISON:

24 Q. If you take --

25 A. May I clarify something?

1 In the lower right corner, there are numbers 112 of
2 263, 113 of 263, which page are you looking at?

3 Q. I am looking at...

4 A. Look in the lower right-hand corner.

5 Q. I'm looking at page 70 where the 70 is in the middle
6 of -- right there, and it's entitled "PUGET SOUND" --

7 A. So it's page 111 of 263 --

8 Q. Yes.

9 A. -- in the lower right corner?

10 Q. Yes.

11 A. Okay. I'm on that page.

12 Q. Okay. And do you see where -- let's see.

13 If you take a look at this, it talks about net income
14 on the very bottom line of that page; do you see that?

15 A. Yes.

16 Q. And do you see that Puget's net income is
17 substantially increasing leading up to 2012 where it's stated at
18 356 million; do you see that?

19 A. Yes. These are not regulated earnings. They contain
20 many other factors in Puget's operations. They are not
21 normalized for weather. They're not normalized for hydro
22 generation. There's -- not relevant to the regulated
23 operations.

24 Q. If you turn -- so the next page is 71, which a
25 partial page, 72 is a full page, and then I would like you to

1 focus on page 73, which doesn't actually say 73 on it, but it is
2 a document that says (as read): "PUGET SOUND ENERGY
3 CONSOLIDATED BALANCE SHEET CAPITALIZATION AND LIABILITIES"; do
4 you see that page?

5 MR. TRAUTMAN: Is this 114/263?

6 MS. DAVISON: Yes.

7 THE WITNESS: Okay.

8 BY MS. DAVISON:

9 Q. And if you look at the line that is -- one, two,
10 three, four, five, six -- seven lines down that says, "Total
11 common shareholder's equity," that is...

12 A. \$859.

13 Q. I'm asking for the total common shareholder's equity
14 number; do you see that?

15 A. Yes.

16 Q. And that is also something that you have not looked
17 at?

18 A. I have not seen this document before.

19 Q. And is it possible to compare the numbers on page 70
20 to page 73 and reach any -- a conclusion about the earnings of
21 the Company?

22 A. (Witness reviews document.)

23 No.

24 Q. I would like to hand you a document that was produced
25 in discovery.

1 (Exhibit No. 7 marked.)

2 BY MS. DAVISON:

3 Q. And if you turn the page where it says on the bottom,
4 "Page 58"; do you see that?

5 A. (Witness reviews document.)

6 Yes.

7 Q. And do you see where Mr. Elgin has relied upon the
8 numbers that I showed you in Puget's 10-K report ending December
9 31, 2012, and he indicates that Puget earned 10.75 percent
10 return on average equity for 2012; do you see that?

11 MR. TRAUTMAN: Objection. Just to the -- where does
12 it indicate this was Mr. Elgin's testimony?

13 MS. DAVISON: If you look at the first page, it's not
14 his testimony. It was provided to us in discovery.

15 MR. TRAUTMAN: I understand that.

16 MS. DAVISON: And it was marked as documents provided
17 by Mr. Elgin.

18 MR. TRAUTMAN: That's correct. But where does it --
19 where on this page does it -- okay.

20 Well, maybe you should rephrase your question.

21 MS. DAVISON: All right. I can rephrase the
22 question, but I am assuming that documents that were provided by
23 Mr. Elgin in discovery were in Mr. Elgin's possession and would
24 be authored by Mr. Elgin. But I can rephrase the question.

25 MR. TRAUTMAN: I think you used the word "testimony."

1 MS. DAVISON: Oh. I'm sorry if I used the word
2 "testimony." I didn't intend to say that, but I'll rephrase the
3 question.

4 BY MS. DAVISON:

5 Q. Mr. Schooley, have you seen the notes that are
6 contained on page 58?

7 A. No.

8 Q. And does that appear as something that Mr. Elgin
9 would have calculated?

10 A. I don't know.

11 Q. Is this the area of expertise that Mr. Elgin
12 possesses?

13 A. I don't believe this is indicative of an area of
14 expertise. There's -- I don't know what this is purporting to
15 depict, nor what it was created for.

16 Q. It appears to me, reading the first paragraph, that
17 it is looking at Puget's --

18 MR. TRAUTMAN: Objection.

19 MS. BARNETT: Objection.

20 MR. TRAUTMAN: That's speculation.

21 MS. DAVISON: And can I at least get the question out
22 before you object?

23 MS. BARNETT: No, because I -- I'm going to object,
24 too, because you are stating what your opinion was, and I don't
25 think you're testifying --

1 MS. DAVISON: I was referring to the language in the
2 document.

3 MS. BARNETT: But you stated you --

4 MS. DAVISON: So if I can please get my question out,
5 then you can...

6 MS. BARNETT: Then I'm objecting --

7 MS. DAVISON: And then you can object.

8 MS. BARNETT: -- to the form of the question.

9 MS. DAVISON: It is appropriate to object after I ask
10 my question, not to cut me off while I'm still formulating my
11 question.

12 BY MS. DAVISON:

13 Q. So, Mr. Schooley, if you look at the beginning of
14 this document, it says that it is pulling numbers out of PSE's
15 December 31, 2012, SEC 10-K filing, and isn't it true that I
16 pointed to the 10-K filing and showed to you those numbers that
17 are contained in that paragraph?

18 MS. BARNETT: Objection. Lack of foundation.
19 Reading testimony into evidence that is not in testimony into
20 evidence, and inappropriately asking Mr. Schooley what appears
21 to be excerpts --

22 MS. DAVISON: Wait.

23 MS. BARNETT: -- from a records request.

24 MS. DAVISON: Wait, wait, wait, wait, wait. Let's
25 just stop. That is an objection that is not appropriate. You

1 know...

2 MS. BARNETT: Actually, we'll let the judge rule.

3 MS. DAVISON: Can I just let him --

4 MS. BARNETT: I think the judge rules on what
5 objections are appropriate. I'm noting an objection for the
6 record.

7 MS. DAVISON: Speaking objections are not appropriate
8 under the Washington rules, and this is a speaking objection.

9 MS. BARNETT: I'll let the judge rule on what is
10 appropriate.

11 MS. DAVISON: This is a speaking objection, and it is
12 not appropriate under the Washington rules. I can pull out the
13 rule that shows you that speaking objections are not
14 appropriate.

15 MS. BARNETT: Objection. No foundation.

16 MS. DAVISON: Thank you.

17 BY MS. DAVISON:

18 Q. You may answer the question.

19 A. I don't know where these numbers come from. I don't
20 know why they were created, nor to whom he submitted this, so I
21 don't know what relevance this document is; nor do I know what
22 relevance the 10-K of 2012 is because it's covering a period
23 that is not in evidence, it is not the subject of the ERF, which
24 ends on 6 of '12, and these numbers have -- are not regulated.
25 The number's based on regulated operations, so I cannot speak to

1 their -- other than perhaps the calculations or, you know, the
2 dividing may be correct, but I don't know what relevance that
3 is, so I don't have an answer to your question.

4 Q. Do you have any basis to conclude that 10.75 percent
5 return on average equity for 2012 is incorrect?

6 A. Like I said -- I mean, he may have divided one number
7 by another and received 10.75 as the answer. But I don't know
8 what those two numbers would be, nor what relevance they have.

9 Q. But wouldn't it be relevant if it shows that PSE is
10 over-earning?

11 A. No.

12 Q. Why not?

13 A. Because these are not regulated numbers. There's
14 no -- the tie between the SEC filing and the regulated
15 operations is nebulous at best.

16 Q. So you're saying that the earnings that Puget is
17 portraying to the public has no bearing on the earnings that are
18 being considered by the Commission?

19 A. The earnings in the 10-K are not the same as the
20 earnings for the regulated operations. They are many items
21 filed for financial purposes that are not relevant for regulated
22 purposes.

23 Q. In your testimony, page 15, lines 5 through 10, you
24 state that it's highly unlikely that PSE will earn more than its
25 authorized rate of return as a result of the rate plan

1 increases?

2 A. Yes.

3 Q. And is that speculation on your part?

4 A. I think it's sort of an informed speculation, yes.

5 Q. Thank you. If you turn back to Exhibit 4, which is
6 your testimony from December 11, 2011 -- I mean -- I'm sorry. I
7 keep saying this wrong -- December 7, 2011, on page 9, lines 3
8 through 4, you state that the public deserves a less complex,
9 more streamlined process.

10 Do you still --

11 A. Exhibit 4, what page?

12 Q. It's page 9, lines 3 through 4.

13 A. (Witness reviews document.)

14 Yes.

15 Q. Do you still agree with that statement?

16 A. Yes, and I think that's what we're trying to
17 accomplish here.

18 Q. Can you explain how the adoption of the decoupling
19 mechanism and the PCORC rate cases will contribute to a less
20 complex and more streamlined process?

21 A. You're tying together two different documents. I'm
22 not sure.

23 I mean, do you want to take them individually, or is
24 that a collective question?

25 Q. It's a collective question, which I can explain,

1 perhaps, better to you, which is there's going to be ongoing
2 cases. This proposed settlement is not going to prevent
3 additional cases from being filed. You testified earlier this
4 afternoon that a PCORC will be filed in the next few months.
5 The decoupling mechanism requires evaluation, monitoring, and
6 ongoing scrutiny of it, plus it has the K-Factor, which you have
7 testified, has annual rate increases associated with it.

8 And my question is: With all that in mind, how does
9 this give the public a more streamlined rate process?

10 A. I think individually they're all far less complex.
11 In the case of the rate plan, it is more formulaic and will not
12 require great analysis, other than determining that the revenue
13 per customer times the next iteration of the rate plan creates a
14 financial revenue, and those revenues will be required to --
15 will drive an increase in rates, which is also formulaic, so I
16 don't think that's a complex process.

17 The PCORC process is there, as it always has been,
18 and is in lieu of a general rate case, which brings power costs
19 into rates, so it is somewhat less complex in that it is only
20 dealing with one aspect of the business. So that is -- its
21 origins and in its intent was to streamline the ability of the
22 utility to bring in power costs in a more -- it's also in a more
23 streamlined and straightforward manner.

24 Q. Thank you.

25 MS. DAVISON: Melinda, may I just interject for the

1 reporter, explaining PCORC, PCORC?

2 THE WITNESS: We've gone through that earlier today.

3 MS. DAVISON: Yeah, we have, and I think she knows
4 it's with a C. We talked about that from the last case.

5 MR. FFITCH: P-C-O-R-C.

6 BY MS. DAVISON:

7 Q. I'd like to just quickly go through some questions
8 that Ms. Reynolds referred to you in her deposition. One of
9 them was I asked the question why the settlement permits PSE to
10 file a PCORC and if it results in a rate increase -- well, let
11 me back up.

12 Under the PCORC, as it currently stands, if there is
13 a rate increase associated with PCORC, then Puget must file a
14 general rate case within three months for the purposes of
15 looking for offsetting revenue; is that correct?

16 A. Yes.

17 Q. And my question is: Why is Staff allowing PSE to
18 avoid a general rate case if there is an increase associated
19 with PCORC?

20 A. I have never found that to be a necessary feature of
21 the PCORC process; that that is sort of just begging to have
22 higher rates set because it never goes the other direction.

23 I would -- I don't -- I don't think that it's
24 necessary to file a general rate case after a PCORC, because
25 like I said, you're just begging to have higher rates at that

1 point, so it seems an anathema to me that it was ever put in
2 there. It would have been more relevant if you said they're
3 forbidden from filing a rate case for a year after a PCORC, or
4 something like that. Therefore, I think releasing that
5 constraint is a positive thing in this process, and allowing the
6 Company to proceed with the rate plan also with the knowledge
7 that there will be a rate case in the not too distant future
8 where they're required to file one in 2016, or no later -- or no
9 earlier than 2015.

10 So to me, I think that's a positive direction, and
11 it's something that should be stricken from the PCORC process
12 all together.

13 Q. Thank you. How does Staff arrive at the decision to
14 create a rate plan in which 449 customers see an automatic
15 3 percent rate increase per year?

16 A. First, I'd like to clarify that the Schedule 449
17 customers will not see a 3 percent increase in their total
18 electricity costs. They will see a 3 percent increase as driven
19 by the 3 percent times the delivery cost revenue per customer
20 that is valid, because all customers should be receiving the
21 same increase for delivery costs. And the fact that they may
22 buy electricity from somebody else does not mean they're getting
23 a 3 percent increase in total electricity costs, only in the
24 delivery costs like everybody else.

25 Q. Was the 3 percent derived on a cost-of-service basis?

1 A. The 3 percent is based on the label, the K-Factor, of
2 all the customers and the customer groups, so it's not based on
3 the cost of service. It is based on the revenues that will help
4 recover the Company's ongoing infrastructure and expense growth.

5 Q. Do you know how many 449 customers receive their
6 service in a distribution voltage versus transmission level
7 voltage?

8 A. No.

9 Q. Did Staff analyze that?

10 A. No.

11 Q. Would you be surprised if I told you all -- most, if
12 not all, receive their service at a transmission voltage?

13 A. And they receive lower costs because of that. Less
14 cost is passed on to them. They still receive delivery. And
15 the cost of service study takes that into effect, so they don't
16 receive the distribution side of it. They're only receiving
17 what they're allocated in the cost of service study for their
18 portion of the total delivery cost.

19 Q. But isn't it true if they're taking service at a
20 transmission level, that they're paying for that through PSE's
21 transmission rates?

22 A. Could you add a little more context to that, please?

23 Q. Is it correct that 449 customers pay for their
24 transmission delivery based on PSE's FERC-approved transmission
25 rates?

1 A. I guess what I'm getting at: Are you referring to
2 what is the acronym O-A-T-T?

3 Q. Yes.

4 A. I'm just trying to clarify what you're trying to talk
5 about, so...

6 Q. Well, I mean you could call it a -- I was just making
7 it more generic, but...

8 A. Yes, I understand. I assume so, and I don't --
9 that's a detail I'm not terribly familiar with and how this is
10 working within the context of the rate plan. Mr. Piliaris would
11 be able to answer that question.

12 Q. Okay. Before the proposed rate plan, there are a
13 variety of exceptions which allow PSE to request rate changes.
14 Has Staff done any analysis on the total potential
15 rate impact for each of these exceptions?

16 A. No, in part because those exceptions are going to
17 happen regardless of whether it's this plan or another plan, so
18 it's really just a given throughout the process.

19 Q. All right. So then I would take you back to one of
20 your statements from your 2011 testimony, which is the public
21 deserves a less complex, more streamlined process.

22 Isn't it true that the public has the normal rate
23 increases that you will see through these filings that are
24 accepted from the rate plan, and then in addition to that, they
25 will see annual increases due to decoupling and the K-Factor?

1 A. Like I said before, those other exceptions are things
2 that will happen anyway, if you're speaking of things like the
3 conversation tariff or the power -- the purchase gas
4 adjustments. Those are already scheduled -- increased scheduled
5 changes that could go either direction.

6 And if the timing of such things is of interest to
7 you, that is something you could bring up in the discussions to
8 be held later this month.

9 MS. DAVISON: All right. I'm --

10 MR. TRAUTMAN: Okay. We're at 4:33.

11 MS. DAVISON: Yes. Thank you for the additional
12 time, and I'm done.

13 MR. TRAUTMAN: Okay. All right. Thank you.

14 THE WITNESS: Thank you.

15 MR. FFITCH: Okay. At this time we're going to
16 recess but not adjourn the deposition.

17 MR. TRAUTMAN: And Staff will object to that; object
18 to continuing the deposition.

19 MR. FFITCH: And we'll go off the record.

20 (Deposition was adjourned at 4:33 p.m.)

21

22 (By agreement between counsel
23 and the witness, signature was
24 reserved.)

25

-o0o-

Exhibit No. ___ T (TES-1T)
Dockets UE-111048/UG-111049
Witness: Thomas E. Schooley

BEFORE THE WASHINGTON STATE UTILITIES AND TRANSPORTATION COMMISSION

WASHINGTON UTILITIES AND
TRANSPORTATION COMMISSION,

Complainant,

v.

PUGET SOUND ENERGY,

Respondent.

DOCKET UE-111048
DOCKET UG-111049
(Consolidated)

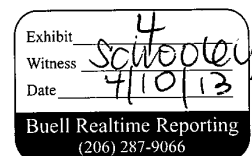
TESTIMONY OF

THOMAS E. SCHOOLEY

STAFF OF
WASHINGTON UTILITIES AND
TRANSPORTATION COMMISSION

Introduction and General Policy

December 7, 2011



1 proposes holding certain expenses constant, such as the power cost adjustment
2 baseline, wages, and overall administrative and general expenses, to hold the
3 Company accountable for cost effective management decisions.
4

5 **Q. Will this expedited ratemaking process have any other benefits besides**
6 **alleviating regulatory lag, as Mr. Elgin describes?**

7 A. The expedited rate case process will also have the positive benefit of streamlining
8 rate making procedures for the Commission and all parties. Our recent experience of
9 repeated rate case filings by all regulated companies warrants a streamlined
10 approach, as I explain next.
11

12 **Q. What is PSE's recent history of general rate case filings?**

13 A. PSE has had a history of regular general rate cases for several years. General rate
14 cases were filed in 2004, 2006, 2007, 2009, 2010 (gas only), and now 2011. There
15 have also been power cost only rate cases in 2003, 2005, 2006, and 2007. A similar
16 general rate case pattern has been experienced with Avista and PacifiCorp. Staff
17 expects that all three companies will continue this pattern of regularly seeking rate
18 relief via general rate cases.
19

20 **Q. Does Staff have concerns about this situation that would be assisted through the**
21 **expedited rate case process?**

22 A. Yes. For Staff to effectively process almost annual rate cases from PSE, Avista and
23 PacifiCorp, along with all of the other types of filings and applications submitted by

1 all companies, we must find a more consistent, efficient approach to processing rate
2 cases. While each utility presents different challenges, it is, after all, the same
3 industry under the same regulatory and statutory environment. The public deserves a
4 less complex, more streamlined process.

5 The complexities of PSE's rate cases are particularly perplexing. PSE's
6 Power Cost Adjustment ("PCA") is a burdensome mechanism giving PSE a full
7 return of and on certain regulatory assets; recovery of the cost of lines-of-credit,
8 taxes, insurance, payroll; and a guaranteed rate of return on \$2 billion of rate base.
9 One-half of PSE's total rate base now receives a guaranteed return. PSE recovers all
10 PCA costs by updating the base line through frequent rate filings. The purpose of
11 the PCA -- to share the risk of power cost variation between ratepayers and the
12 Company -- is thwarted by this situation.

13 PSE's rate cases present other complications such as determining revenues
14 after removing many different tariff riders or offsets;⁸ multiple averaging methods
15 for administrative and general expenses; and projections of expenses into future
16 years.

17 On top of the constant rate case pressure, PSE continues to demand greater
18 attention by regularly filing petitions for approval of deferred accounting treatment,
19 which establish a voluminous range of regulatory assets and liabilities that must
20 eventually be addressed in rate cases. Exhibit No. ___ (TES-2) includes a data
21 request response from PSE in Docket UE-110723 listing all of the deferred
22 accounting treatments currently in effect for PSE.

⁸ These riders and offsets include Production Tax Credits, Merger Rate Credit, Tenaska Regulatory Asset Tracker, conservation program riders, low-income riders, municipal taxes, residential exchange, green power, and renewable energy credits.

Exhibit No. ___ T (TES-1T)
Dockets UE-111048/UG-111049
Witness: Thomas E. Schooley

BEFORE THE WASHINGTON STATE UTILITIES AND TRANSPORTATION COMMISSION

WASHINGTON UTILITIES AND
TRANSPORTATION COMMISSION,

Complainant,

v.

PUGET SOUND ENERGY,

Respondent.

DOCKET UE-111048
DOCKET UG-111049
(Consolidated)

TESTIMONY OF

THOMAS E. SCHOOLEY

STAFF OF
WASHINGTON UTILITIES AND
TRANSPORTATION COMMISSION

Introduction and General Policy

December 7, 2011



1 **Q. Please describe the crux of PSE's presentation**

2 A. The Company's case for its electric operations is driven primarily by PSE's
3 investment in LSR Phase 1 plus the associated transmission. As a result, PSE is
4 seeking more than \$170 million in additional revenues using the overall cost of
5 capital PSE proposes for ratemaking purposes.² This amount is offset by reductions
6 in net power cost, but, none the less, LSR Phase 1 is the single largest factor driving
7 PSE's proposal for greater revenues.

8 The Company's case includes increases in other electric rate base.³ The
9 natural gas business also includes costs of new investments.⁴

10 Finally, it should be noted that PSE requests an increase in profits for its
11 entire rate base through a 10.80 percent return on equity compared to the 10.1
12 percent the Commission determined fair in the Company's last contested rate case.

13
14 **Q. Does PSE claim an inability to earn a sufficient return on its growing utility
15 investments?**

16 A. Yes. PSE raises this issue of attrition in the direct testimony of Mr. Gaines and Dr.
17 Olson who present and comment on comparisons of actual (per books) returns on
18 equity with "authorized" returns on equity.⁵

19

² The rate base increases for Adjustments 5.02 and 5.03 total \$798,249,674, and the decrease to net operating income is \$39,877,591. Exhibit No. ___ (JHS-4), page 4.02. Given the requested rate of return of 8.42 percent and the conversion factor, we derive the Company proposed increase in revenues of \$172,517,738 for LSR Phase 1.

³ Exhibit No. ___ (JHS-3), page 3.01.

⁴ Mr. Stranik's Exhibit No. ___ (MJS-3) compares the rate base total in the present case to that in the 2009 rate case, Docket UG-090705. He should more appropriately compare the present period to Docket UG-101644 which was based on a test year ending June 30, 2010 where the total rate base was \$1,593,833,326. The gas rate base increase since June 2010 is \$66,901,785.

⁵ Exhibit No. ___(DEG-1T) at 23, Chart 1 and Exhibit No. ___(CEO-1T) at 8:10-12 and 15-17.

1 **Q. What is Staff's view of PSE's claim of attrition caused by continued investments**
2 **in rate base?**

3 A. Staff recognizes that Washington regulated utilities are entitled to an opportunity to
4 earn a fair return on their prudent investments. Balanced with that interest is the
5 Commission's obligation to set rates, or prices, to be paid by customers that are fair,
6 just, and reasonable.

7 PSE and other utilities assert persistent under-earning and present ever more
8 creative ways to address claims of declining sales and regulatory lag. Staff is open
9 to new approaches, provided the utility adequately proves its claim of persistent
10 under-earning.

11

12 **Q. Has PSE adequately proven its claim of persistent under-earning?**

13 A. No. Mr. Elgin details this area of the Staff case. But, in general, the Company in its
14 direct case could have, but did not, provide an attrition study to determine whether,
15 and by how much, PSE is experiencing attrition due to its need to invest in new rate
16 base thereby denying it the opportunity to earn a fair rate of return during the rate
17 year. If an attrition study had been presented and had confirmed that situation,
18 additional revenues could have been proposed. PSE's presentation of actual versus
19 authorized returns on equity, however, is insufficient to support a claim of attrition.

20

21 **Q. Are there other means Staff would consider to address attrition, if adequately**
22 **proven?**

1 A. Yes. Again assuming adequate proof of attrition, Staff would consider proposals
2 using end-of-period rate base and/or including construction work in progress in rate
3 base. These methods are within the authority and precedent of the Commission.
4

5 **Q. Does the Company attribute its claim of under-earning to factors other than its**
6 **growing rate base?**

7 A. Yes. PSE also asserts that the Commission's current historical test-year ratemaking
8 practices, and resulting regulatory lag, cause its returns on equity to be consistently
9 less than what the Commission grants.⁶
10

11 **Q. Does Staff propose a way to address this complaint?**

12 A. Yes. Staff proposes expedited rate filings as a step toward addressing regulatory lag.
13 Once PSE receives a general rate order, it may file its next case based on the latest
14 Commission-basis Report and Staff will support a schedule that implements new
15 rates before the next heating season, if rate relief is warranted.⁷

16 The details of this proposal are presented by Mr. Elgin. However, I would
17 add that for the Commission-basis report to be useful for ratemaking purposes in the
18 expedited process Staff supports, the report will need certain limited modifications.
19 Examples include annualizing any rate increases instituted during or just after the
20 reporting period and including any new directives from the Commission. Staff also

⁶ Exhibit No. ___ (CEO-1T) at 7:20-8:4.

⁷ The Commission-basis Report is an annual filing by each utility required by WAC 480-90-257 for natural gas companies and WAC 480-100-257 for electric companies. It depicts a utility's operations for the prior year with sales based on normal temperatures and power costs based on average hydroelectric conditions, but without annualized expenses or revenues. The results of operations must also include adjustments required by the Commission by order. The report must be filed by April 30 each year.

1 proposes holding certain expenses constant, such as the power cost adjustment
2 baseline, wages, and overall administrative and general expenses, to hold the
3 Company accountable for cost effective management decisions.
4

5 **Q. Will this expedited ratemaking process have any other benefits besides**
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15 have also been power cost only rate cases in 2003, 2005, 2006, and 2007. A similar
16 general rate case pattern has been experienced with Avista and PacifiCorp. Staff
17 expects that all three companies will continue this pattern of regularly seeking rate
18 relief via general rate cases.
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21 **expedited rate case process?**

22 A. Yes. For Staff to effectively process almost annual rate cases from PSE, Avista and
23 PacifiCorp, along with all of the other types of filings and applications submitted by

4/9/13

PE 2012 10K

10-K 1 pe201210k.htm PUGET ENERGY AND PUGET SOUND ENERGY FORM 10-K FOR YEAR ENDED DECEMBER 31, 2012

UNITED STATES
SECURITIES AND EXCHANGE COMMISSION
Washington, D.C. 20549

FORM 10-K

/X/ ANNUAL REPORT PURSUANT TO SECTION 13 OR 15(d) OF THE SECURITIES EXCHANGE ACT OF 1934

For the fiscal year ended December 31, 2012

OR

// TRANSITION REPORT PURSUANT TO SECTION 13 OR 15(d) OF THE SECURITIES EXCHANGE ACT OF 1934

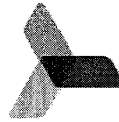
For the transition period from _____ to _____

Commission
File Number

Exact name of registrant as specified in its charter,
state of incorporation,
address of principal executive offices, zip code
telephone number

I.R.S.
Employer
Identification
Number

PugetEnergy



1-16305

PUGET ENERGY, INC.
A Washington Corporation
10885 NE 4th Street, Suite 1200
Bellevue, Washington 98004-5591
(425) 454-6363

91-1969407

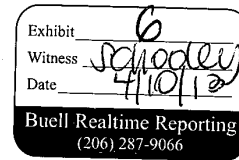


PUGET SOUND ENERGY

1-4393

PUGET SOUND ENERGY, INC.
A Washington Corporation
10885 NE 4th Street, Suite 1200
Bellevue, Washington 98004-5591
(425) 454-6363

91-0374630



Securities registered pursuant to Section 12(b) of the Act:

None

Securities registered pursuant to Section 12(g) of the Act:

None

4/9/13

PE 2012 10K

PUGET ENERGY, INC.
CONSOLIDATED BALANCE SHEETS
(Dollars in Thousands)

CAPITALIZATION AND LIABILITIES

	December 31,	
	2012	2011
Capitalization:		
Common shareholder's equity:		
Common stock \$0.01 par value, 1,000 shares authorized, 200 shares outstanding	\$ —	\$ —
Additional paid-in capital	3,308,957	3,308,957
Earnings reinvested in the business	208,100	22,873
Accumulated other comprehensive income (loss), net of tax	(32,829)	(30,907)
Total common shareholder's equity	3,484,228	3,300,923
Long-term debt:		
First mortgage bonds and senior notes	3,351,412	3,362,000
Pollution control bonds	161,860	161,860
Junior subordinated notes	250,000	250,000
Long-term debt	1,834,000	1,793,000
Debt discount and other	(264,072)	(289,493)
Total long-term debt	5,333,200	5,277,367
Total capitalization	8,817,428	8,578,290
Current liabilities:		
Accounts payable	288,059	339,361
Short-term debt	181,000	25,000
Current maturities of long-term debt	13,000	—
Purchased gas adjustment liability	32,587	25,940
Accrued expenses:		
Taxes	95,623	90,727
Salaries and wages	38,438	40,892
Interest	82,262	69,329
Unrealized loss on derivative instruments	177,519	327,089
Power contract acquisition adjustment loss	3,902	8,547
Other	72,799	74,409
Total current liabilities	985,189	1,001,294
Long-term and regulatory liabilities:		
Deferred income taxes	1,261,636	1,153,172
Unrealized loss on derivative instruments	83,276	196,558
Regulatory liabilities	600,697	369,403
Regulatory liabilities related to power contracts	507,009	582,836
Power contract acquisition adjustment loss	33,753	37,655
Other deferred credits	512,591	488,098
Total long-term and regulatory liabilities	2,998,962	2,827,722
Commitments and contingencies (Note 16)		
Total capitalization and liabilities	\$ 12,801,579	\$ 12,407,306

4/9/13

PE 2012 10K

The accompanying notes are an integral part of the consolidated financial statements.

67

4/9/13

PE 2012 10K

PUGET ENERGY, INC.
CONSOLIDATED STATEMENTS OF COMMON SHAREHOLDER'S EQUITY
(Dollars in Thousands)

	<u>Common Stock</u>		Additional Paid-in Capital	Earnings Reinvested in the Business	Accumulated Other Comprehensive Income (Loss)	Total Equity
	Shares	Amount				
Balance at December 31, 2009	200	\$ —	\$ 3,308,957	\$ 91,024	\$ 23,487	\$ 3,423,468
Net income	—	—	—	30,311	—	30,311
Common stock dividend	—	—	—	(104,311)	—	(104,311)
Other comprehensive income	—	—	—	—	(26,556)	(26,556)
Balance at December 31, 2010	200	\$ —	\$ 3,308,957	\$ 17,024	\$ (3,069)	\$ 3,322,912
Net income	—	—	—	123,290	—	123,290
Common stock dividend	—	—	—	(117,441)	—	(117,441)
Other comprehensive income	—	—	—	—	(27,838)	(27,838)
Balance at December 31, 2011	200	\$ —	\$ 3,308,957	\$ 22,873	\$ (30,907)	\$ 3,300,923
Net income	—	—	—	273,821	—	273,821
Common stock dividend	—	—	—	(88,594)	—	(88,594)
Other comprehensive income	—	—	—	—	(1,922)	(1,922)
Balance at December 31, 2012	200	\$ —	\$ 3,308,957	\$ 208,100	\$ (32,829)	\$ 3,484,228

The accompanying notes are an integral part of the consolidated financial statements.

4/9/13

PE 2012 10K

PUGET ENERGY, INC.
CONSOLIDATED STATEMENTS OF CASH FLOWS
(Dollars in Thousands)

	Year Ended December 31,		
	2012	2011	2010
Operating activities:			
Net income (loss)	\$ 273,821	\$ 123,290	\$ 30,311
Adjustments to reconcile net income (loss) to net cash provided by operating activities:			
Depreciation	337,952	299,597	292,634
Amortization	55,819	72,381	71,572
Conservation amortization	114,177	107,646	90,109
Deferred income taxes and tax credits, net	100,457	31,774	(32,955)
Net unrealized (gain) loss on derivative instruments	(146,680)	45,043	50,495
Derivative contracts classified as financing activities due to merger	92,681	182,710	371,621
AFUDC - equity	(25,469)	(32,431)	(12,677)
Funding of pension liability	(22,800)	(5,000)	(12,000)
Regulatory assets	(64,368)	30,232	26,198
Regulatory liabilities	14,054	21,031	28,821
Other long-term assets	(1,644)	(61,734)	(50,009)
Other long-term liabilities	95,166	46,473	31,944
Change in certain current assets and liabilities:			
Accounts receivable and unbilled revenue	35,537	(5,977)	7,261
Materials and supplies	(6,284)	8,154	(19,378)
Fuel and gas inventory	11,527	(4,852)	3,591
Income taxes	6,174	65,213	58,434
Prepayments and other	393	605	(2,345)
Purchased gas adjustment	6,647	31,932	(55,579)
Accounts payable	(25,963)	1,098	(26,396)
Taxes payable	4,896	9,222	4,203
Accrued expenses and other	32,598	43,921	10,094
Net cash provided by operating activities	888,691	1,010,328	865,949
Investing activities:			
Construction expenditures - excluding equity AFUDC	(859,791)	(976,513)	(859,091)
Energy efficiency expenditures	(106,006)	(94,405)	(95,726)
Treasury grant payment received	205,261	—	28,675
Restricted cash	483	1,287	14,374
Other	(38,923)	(7,184)	6,001
Net cash used in investing activities	(798,976)	(1,076,815)	(905,767)
Financing activities:			
Change in short-term debt and leases, net	148,437	(227,651)	141,941
Dividends paid	(88,594)	(117,441)	(104,311)
Long-term notes and bonds issued	1,314,000	1,382,000	1,025,000
Redemption of bonds and notes	(1,273,000)	(769,000)	(675,000)
Derivative contracts classified as financing activities due to merger	(92,681)	(182,710)	(371,621)
Issuance cost of bonds and other	430	(18,033)	(18,161)
Net cash provided by (used in) financing activities	8,592	67,165	(2,152)
Net increase (decrease) in cash and cash equivalents	98,307	678	(41,970)
Cash and cash equivalents at beginning of period	37,235	36,557	78,527

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Cash and cash equivalents at end of period	\$	135,542	\$	37,235	\$	36,557
<u>Supplemental cash flow information:</u>						
Cash payments for interest (net of capitalized interest)	\$	318,305	\$	280,847	\$	278,926
Cash payments (refunds) for income taxes		(1,898)		(64,016)		(22,243)

The accompanying notes are an integral part of the consolidated financial statements.

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PUGET SOUND ENERGY, INC.
CONSOLIDATED STATEMENTS OF INCOME
(Dollars in Thousands)

	Year Ended December 31,		
	2012	2011	2010
Operating revenue:			
Electric	\$ 2,128,230	\$ 2,147,220	\$ 2,107,469
Gas	1,086,095	1,168,850	1,011,531
Other	1,934	3,733	3,217
Total operating revenue	3,216,259	3,319,803	3,122,217
Operating expenses:			
Energy costs:			
Purchased electricity	622,288	771,983	774,007
Electric generation fuel	204,956	199,471	268,147
Residential exchange	(73,555)	(71,147)	(75,109)
Purchased gas	538,612	622,088	535,933
Unrealized (gain) loss on derivative instruments, net	(119,120)	54,146	166,953
Utility operations and maintenance	512,765	497,921	486,701
Non-utility expense and other	9,977	11,147	11,159
Depreciation	337,952	299,597	292,634
Amortization	55,819	72,381	71,572
Conservation amortization	114,177	107,646	90,109
Taxes other than income taxes	319,399	323,527	292,520
Total operating expenses	2,523,270	2,888,760	2,914,626
Operating income (loss)	692,989	431,043	207,591
Other income (deductions):			
Other income	49,056	58,041	45,153
Other expense	(11,770)	(5,380)	(5,673)
Interest charges:			
AFUDC	22,216	29,949	14,157
Interest expense	(246,811)	(231,212)	(234,793)
Interest expense on parent note	(202)	(204)	(218)
Income (loss) before income taxes	505,478	282,237	26,217
Income tax (benefit) expense	149,308	78,117	122
Net income (loss)	\$ 356,170	\$ 204,120	\$ 26,095

The accompanying notes are an integral part of the consolidated financial statements.

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PUGET SOUND ENERGY, INC.
CONSOLIDATED STATEMENTS OF COMPREHENSIVE INCOME
(Dollars in Thousands)

	Year Ended December 31,		
	2012	2011	2010
Net income (loss)	\$ 356,170	\$ 204,120	\$ 26,095
Other comprehensive income (loss):			
Net unrealized gain (loss) from pension and postretirement plans, net of tax of \$(3,911), \$(28,474) and \$2,446, respectively	(7,294)	(52,927)	3,610
Reclassification of net unrealized (gain) loss on energy derivative instruments, net of tax of \$4,500, \$11,673 and \$26,140	8,358	21,678	48,546
Amortization of treasury interest rate swaps to earnings, net of tax of \$171, \$171 and \$171, respectively	317	317	317
Other comprehensive income (loss)	1,381	(30,932)	52,473
Comprehensive income (loss)	\$ 357,551	\$ 173,188	\$ 78,568

The accompanying notes are an integral part of the consolidated financial statements.

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PUGET SOUND ENERGY, INC.
CONSOLIDATED BALANCE SHEETS
(Dollars in Thousands)

ASSETS

	December 31,	
	2012	2011
Utility plant (including construction work in progress of \$766,035 and \$1,282,462, respectively):		
Electric plant	\$ 9,048,356	\$ 8,413,846
Gas plant	2,998,188	2,855,794
Common plant	555,549	518,318
Less: Accumulated depreciation and amortization	(4,045,402)	(3,714,913)
Net utility plant	8,556,691	8,073,045
Other property and investments:		
Other property and investments	103,646	113,528
Total other property and investments	103,646	113,528
Current assets:		
Cash and cash equivalents	135,530	31,010
Restricted cash	3,700	4,183
Accounts receivable, net of allowance for doubtful accounts of \$9,932 and \$8,495, respectively	287,989	336,483
Unbilled revenue	204,359	191,150
Materials and supplies, at average cost	82,353	76,069
Fuel and gas inventory, at average cost	85,547	97,074
Unrealized gain on derivative instruments	6,869	6,647
Income taxes	4,796	10,970
Prepaid expenses and other	13,414	13,807
Deferred income taxes	68,015	112,204
Total current assets	892,572	879,597
Other long-term and regulatory assets:		
Regulatory asset for deferred income taxes	119,279	61,344
Power cost adjustment mechanism	3,773	6,818
Other regulatory assets	813,171	777,341
Unrealized gain on derivative instruments	14,814	10,084
Other	90,330	186,386
Total other long-term and regulatory assets	1,041,367	1,041,973
Total assets	\$ 10,594,276	\$ 10,108,143

The accompanying notes are an integral part of the consolidated financial statements.

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PUGET SOUND ENERGY, INC.
CONSOLIDATED BALANCE SHEETS
(Dollars in Thousands)

CAPITALIZATION AND LIABILITIES

	December 31,	
	2012	2011
Capitalization:		
Common shareholder's equity:		
Common stock \$0.01 par value – 150,000,000 shares authorized, 85,903,791 shares outstanding	\$ 859	\$ 859
Additional paid-in capital	3,246,205	3,246,205
Earnings reinvested in the business	344,280	163,735
Accumulated other comprehensive income (loss), net of tax	(187,198)	(188,579)
Total common shareholder's equity	3,404,146	3,222,220
Long-term debt:		
First mortgage bonds and senior notes	3,351,412	3,362,000
Pollution control bonds	161,860	161,860
Junior subordinated notes	250,000	250,000
Debt discount and other	(14)	(15)
Total long-term debt	3,763,258	3,773,845
Total capitalization	7,167,404	6,996,065
Current liabilities:		
Accounts payable	288,257	339,568
Short-term debt	181,000	25,000
Short-term note owed to parent	29,598	29,998
Current maturities of long-term debt	13,000	—
Purchased gas adjustment liability	32,587	25,940
Accrued expenses:		
Taxes	95,623	90,727
Salaries and wages	38,438	40,892
Interest	55,806	55,843
Unrealized loss on derivative instruments	170,948	301,879
Other	69,882	68,346
Total current liabilities	975,139	978,193
Long-term and regulatory liabilities:		
Deferred income taxes	1,274,602	1,115,056
Unrealized loss on derivative instruments	68,323	169,359
Regulatory liabilities	596,324	364,085
Other deferred credits	512,484	485,385
Total long-term and regulatory liabilities	2,451,733	2,133,885
Commitments and contingencies (Note 16)		
Total capitalization and liabilities	\$ 10,594,276	\$ 10,108,143

The accompanying notes are an integral part of the consolidated financial statements.

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PUGET SOUND ENERGY, INC.
CONSOLIDATED STATEMENTS OF COMMON SHAREHOLDER'S EQUITY
(Dollars in Thousands)

	<u>Common Stock</u>		Additional Paid-in Capital	Earnings Reinvested in the business	Accumulated Other Comprehensive Income (loss)	Total Equity
	Shares	Amount				
Balance at December 31, 2009	85,903,791	\$ 859	\$ 2,959,205	\$ 333,128	\$ (210,120)	\$ 3,083,072
Net income	—	—	—	26,095	—	26,095
Common stock dividend	—	—	—	(186,733)	—	(186,733)
Other comprehensive income	—	—	—	—	52,473	52,473
Balance at December 31, 2010	85,903,791	\$ 859	\$ 2,959,205	\$ 172,490	\$ (157,647)	\$ 2,974,907
Net income	—	—	—	204,120	—	204,120
Common stock dividend	—	—	—	(212,875)	—	(212,875)
Capital Contribution	—	—	287,000	—	—	287,000
Other comprehensive income	—	—	—	—	(30,932)	(30,932)
Balance at December 31, 2011	85,903,791	\$ 859	\$ 3,246,205	\$ 163,735	\$ (188,579)	\$ 3,222,220
Net income	—	—	—	356,170	—	356,170
Common stock dividend	—	—	—	(175,625)	—	(175,625)
Capital Contribution	—	—	—	—	—	—
Other comprehensive income	—	—	—	—	1,381	1,381
Balance at December 31, 2012	85,903,791	\$ 859	\$ 3,246,205	\$ 344,280	\$ (187,198)	\$ 3,404,146

The accompanying notes are an integral part of the consolidated financial statements.

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PUGET SOUND ENERGY, INC.
CONSOLIDATED STATEMENTS OF CASH FLOWS
(Dollars in Thousands)

	Year Ended December 31,		
	2012	2011	2010
Operating activities:			
Net income (loss)	\$ 356,170	\$ 204,120	\$ 26,095
Adjustments to reconcile net income (loss) to net cash provided by operating activities:			
Depreciation	337,952	299,597	292,634
Amortization	55,819	72,381	71,572
Conservation amortization	114,177	107,646	90,109
Deferred income taxes and tax credits, net	145,040	77,174	(16,284)
Net unrealized (gain) loss on derivative instruments	(119,120)	54,146	166,953
AFUDC - equity	(25,469)	(32,431)	(12,677)
Funding of pension liability	(22,800)	(5,000)	(12,000)
Regulatory assets	(64,368)	29,271	26,198
Regulatory liabilities	14,054	21,031	28,821
Other long-term assets	932	(62,682)	(48,258)
Other long-term liabilities	79,789	28,814	1,701
Change in certain current assets and liabilities:			
Accounts receivable and unbilled revenue	35,285	(6,204)	7,584
Materials and supplies	(6,284)	8,154	(19,618)
Fuel and gas inventory	11,527	(4,852)	3,591
Income taxes	6,174	51,144	37,834
Prepayments and other	393	605	(2,345)
Purchased gas adjustment	6,647	31,932	(55,579)
Accounts payable	(25,972)	688	(25,780)
Taxes payable	4,896	9,222	4,203
Accrued expenses and other	(954)	18,666	11,021
Net cash provided by operating activities	903,888	903,422	575,775
Investing activities:			
Construction expenditures - excluding equity AFUDC	(859,791)	(976,513)	(859,091)
Energy efficiency expenditures	(106,006)	(94,405)	(95,726)
Treasury grant payment received	205,261	—	28,675
Restricted cash	483	1,287	14,374
Other	(18,022)	9,043	6,001
Net cash used in investing activities	(778,075)	(1,060,588)	(905,767)
Financing activities:			
Change in short-term debt and leases, net	148,437	(227,651)	141,941
Dividends paid	(175,625)	(212,875)	(186,733)
Long-term notes and bonds issued	—	595,000	575,000
Loan from (payment to) parent	(400)	7,400	(300)
Redemption of bonds and notes	—	(285,000)	(232,000)
Investment from parent	—	287,000	—
Issuance cost of bonds and other	6,295	(12,018)	(10,003)
Net cash provided by (used in) financing activities	(21,293)	151,856	287,905
Net increase (decrease) in cash and cash equivalents	104,520	(5,310)	(42,087)
Cash and cash equivalents at beginning of period	31,010	36,320	78,407

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Cash and cash equivalents at end of period	\$	135,530	\$	31,010	\$	36,320
<u>Supplemental cash flow information:</u>						
Cash payments for interest (net of capitalized interest)	\$	216,128	\$	191,666	\$	198,496
Cash payments (refunds) for income taxes		(1,898)		(50,022)		(20,632)

The accompanying notes are an integral part of the consolidated financial statements.