

**EXH. SEF-12T
DOCKETS UE-170033/UG-170034
2017 PSE GENERAL RATE CASE
WITNESS: SUSAN E. FREE**

**BEFORE THE
WASHINGTON UTILITIES AND TRANSPORTATION COMMISSION**

**WASHINGTON UTILITIES AND
TRANSPORTATION COMMISSION,**

Complainant,

v.

PUGET SOUND ENERGY,

Respondent.

**Docket UE-170033
Docket UG-170034**

PREFILED REBUTTAL TESTIMONY (NONCONFIDENTIAL) OF

SUSAN E. FREE

ON BEHALF OF PUGET SOUND ENERGY

AUGUST 9, 2017

1 **PUGET SOUND ENERGY**

2 **PREFILED REBUTTAL TESTIMONY (NONCONFIDENTIAL) OF**
3 **SUSAN E. FREE**

4 **CONTENTS**

5 I. INTRODUCTION1
6 II. COMPARISON BETWEEN PSE’S REVENUE DEFICIENCY
7 AND OTHER PARTIES’ REVENUE
8 DEFICIENCIES/SURPLUSES2
9 III. NATURAL GAS AND COMMON ADJUSTMENTS THAT ARE
10 UNCONTESTED BETWEEN PSE AND OTHER PARTIES5
11 A. Tax Benefit of Proforma Interest, Adjustment KJB-20.05
12 and SEF-15.05.....6
13 B. Payment Processing Costs, Adjustment KJB-20.20 and
14 SEF-15.206
15 C. Changes by PSE at Supplemental Ignored by ICNU and
16 NWIGU.....7
17 IV. CERTAIN COMMON CONTESTED ADJUSTMENTS8
18 A. Temperature Normalization, Adjustment KJB-20.02 and
19 SEF-15.029
20 B. Depreciation Study, Adjustment KJB-20.06 and SEF-15.069
21 C. Rate Case Expenses, Adjustment KJB-20.12 and SEF-
22 15.12.....10
23 D. Deferred Gains and Losses on Property Sales, Adjustment
24 SEF-15.1313
25 E. Pension Plan, Adjustment KJB-20.16 and SEF-15.16.....18
26 F. Environmental Remediation, Adjustment KJB-20.19 and
27 SEF-15.1918

1	G.	Working Capital, Adjustment KJB-20.23 and SEF-15.23.....	39
2	H.	Liquefied Natural Gas (“LNG”) and Leasing Costs,	
3		Commission Staff Adjustment 13.24E and 11.24G.....	50
4	1.	Leasing Costs:.....	50
5	2.	LNG Costs:	54
6	I.	Greenwood Incident, NWIGU Adjustment IN-5.....	55
7	V.	CHANGES BY PSE AT REBUTTAL.....	58
8	VI.	MATERIALITY AND OTHER NON-REVENUE	
9		REQUIREMENT ISSUES	59
10	VII.	CONCLUSION.....	59

1 **LIST OF EXHIBITS**

- 2 Exh. SEF-13 Natural gas base rates general rate increase
- 3 Exh. SEF-14 Summary of natural gas proforma and restating adjustments and their
4 impact on the actual results of operations
- 5 Exh. SEF-15 Individual adjustments – common assigned to natural gas
- 6 Exh. SEF-16 Individual adjustment – natural gas only
- 7 Exh. SEF-17 Comparison of the natural gas revenue deficiencies by adjustment
8 currently filed by PSE and opposing parties
- 9 Exh. SEF-18 Excerpts from Commission Staff’s Response to PSE Data Request No. 27
10 – Impact on Commission Staff’s natural gas revenue requirement for
11 various corrections
- 12 Exh. SEF-19 Excerpts from Commission Staff’s Response to PSE Data Request No. 28
13 – Impact on Commission Staff’s working capital calculation for various
14 corrections
- 15 Exh. SEF-20 Comparison of Test Year, Allowed and Total rate case costs per
16 proceeding
- 17 Exh. SEF-21 2014 system entry to transfer Kent property from utility to non-utility
18 property at time of sale
- 19 Exh. SEF-22 System entries for deferred gain on property sales
- 20 Exh. SEF-23 Comparison of PSE’s and Commission Staff’s method for allocating
21 unassigned recoveries to specific sites for environmental remediation
- 22 Exh. SEF-24 Determination of PSE’s Electric Environmental Remediation Adjustment
23 utilizing the low range of future cost estimates
- 24 Exh. SEF-25 Determination of PSE’s Gas Environmental Remediation Adjustment
25 utilizing the low range of future cost estimates
- 26 Exh. SEF-26 Attachment A to PSE’s First Supplemental Response to Commission Staff
27 Data Request No. 269
- 28 Exh. SEF-27 Transmittal letter and report for WNG’s September 30, 1994
29 Environmental Remediation Quarterly Report filed December 23, 1994
- 30 Exh. SEF-28 Calculation of Working Capital - Summary
- 31 Exh. SEF-29 Calculation of Working Capital - Detail

- 1 Exh. SEF-30 Commission Staff's Response to PSE Data Request No. 11.
- 2 Exh. SEF-31 Commission Staff's Response to PSE Data Request Nos. 8 and 14 and a
3 presentation of how to adjust for working capital outside of the working
4 capital exhibit.

1 **PUGET SOUND ENERGY**

2 **PREFILED REBUTTAL TESTIMONY (NONCONFIDENTIAL) OF**
3 **SUSAN E. FREE**

4 **I. INTRODUCTION**

5 **Q. Are you the same Susan E. Free who submitted prefiled direct testimony on**
6 **January 13, 2017, and prefiled supplemental direct testimony on April 3,**
7 **2017, on behalf of Puget Sound Energy (“PSE”) in this proceeding?**

8 A. Yes.

9 **Q. What is the purpose of your rebuttal testimony?**

10 A. My testimony presents the natural gas base rates revenue deficiency based on the
11 updated restating and pro forma adjustments that PSE is proposing. I also discuss
12 most of the common adjustments that relate to both gas and electric operations. I
13 will present the uncontested adjustments between parties and PSE and explain
14 why some of these adjustments have a different impact on the revenue
15 requirement calculation even though they are not contested. I will also discuss
16 specific restating and pro forma adjustments that are common to electric and
17 natural gas and are contested by Commission Staff and other parties.

1 **II. COMPARISON BETWEEN PSE'S REVENUE DEFICIENCY**
2 **AND OTHER PARTIES' REVENUE DEFICIENCIES/SURPLUSES**

3 **Q. Have you prepared an exhibit showing PSE's natural gas base rates revenue**
4 **deficiency you have calculated for this rebuttal filing?**

5 A. Yes. I have updated my natural gas base rates revenue deficiency for this rebuttal
6 filing in Exhibit SEF-13. I discuss the changes since the supplemental filing on
7 April 3, 2017 later in my testimony. Based on natural gas rate base of \$1.771
8 billion and \$123.0 million of pro forma operating income, the natural gas base
9 rates revenue requirement deficiency is \$22.7 million. This represents a reduction
10 of \$0.1 million from the supplemental filing submitted on April 3, 2017.
11 Accordingly, the overall natural gas revenue requirement surplus of \$29.3 million
12 reported on page 2 of Exhibit JAP-45 is now \$29.4 million.

13 **Q. Have you prepared exhibits which detail the updated restating and pro**
14 **forma adjustments that PSE is proposing?**

15 A. Yes. I have prepared Exhibit SEF-14 for this purpose. I have also prepared
16 Exhibit SEF-15 and SEF-16, which contain the detail pages supporting the
17 summarized adjustments in Exhibit SEF-14. Exhibit SEF-14 through SEF-16 are
18 presented in the same format as my Exhibits SEF-10, SEF-11 and SEF-7, and in
19 the same format as Ms. Cheesman's Exhibit MCC-7.

1 **Q. Have you prepared a reconciliation between the revenue deficiency filed by**
 2 **PSE and the revenue deficiency/surplus filed by other parties?**

3 A. Yes. Table 1 below highlights the differences between PSE 's supplemental filing,
 4 PSE's rebuttal filing and the opposing parties' filing on June 30, 2017.

5 **Table 1. Summary of Natural Gas Base Rates Revenue**
 6 **Requirement Deficiencies (Surpluses)**

<u>Comparison of Natural Gas Base Rates Revenue Deficiency by Adjustment Filed by PSE and Intervenor</u>					
Line	Adjustment	PSE	Staff	Public Counsel	NWIGU
(\$000 Thousands)					
1	PSE Supplemental Filing Base Rates Deficiency	\$ 22,813			
2					
3	<u>PSE Rebuttal Changes:</u>				
4	Environmental Remediation	44			
5	Credit Card Processing	(1,252)			
6	Working Capital	1,066			
7	Subtotal Rebuttal Changes	(141)			
8					
9	PSE Rebuttal Filing Base Rates Deficiency	\$ 22,671	\$ 22,671	\$ 22,671	\$ 22,671
10					
11	<u>Contested Issues:</u>				
12	Rate of Return on Actual Results of Operation		(10,301)	(12,806)	(9,466)
13	Depreciation Study		(39)	(17,040)	(36)
14	Pension Plan			(582)	(1,645)
15	Environmental Remediation		(5,893)	(4,419)	(4,419)
16	ISWC and RB Adjustment		(7,891)	(1,233)	(1,233)
17	Net Operating Loss Carryforward				(1,505)
18	Other Adjustments		(752)	(124)	913
19	Total Difference		(24,877)	(36,205)	(17,392)
	Adjusted Base Rates Revenue Deficiency Per Intervenor	\$ (2,206)	\$ (13,534)	\$ (13,534)	\$ 5,279

7 **Q. What are the major differences between PSE's base rates natural gas**
 8 **revenue deficiency and the parties' base rates revenue deficiencies/surpluses?**

9 A. Included in Exhibit SEF-17 is a comparison of the revenue deficiencies/surpluses
 10 by adjustment currently filed by PSE and opposing parties. The major differences
 11 between PSE and opposing parties are the capital structure and the return on
 12 equity embedded in the rate of return along with the other differences highlighted

1 in the above table. The capital structure and return on equity are discussed by Mr.
2 Doyle and Dr. Morin in their prefiled rebuttal testimonies, Exhibit DAD-7T and
3 Exhibit RAM-12T, respectively. The other differences will be discussed in the
4 relevant pro forma or restating adjustment discussions which occur later in my
5 testimony.

6 **Q. Are you aware of any changes related to the natural gas base rates revenue**
7 **requirement presentations of Commission Staff?**

8 A. Yes. During discovery, PSE received Commission Staff's Response to PSE Data
9 Request Nos. 27 and 28 which reflected revisions and corrections to Commission
10 Staff's working capital calculation which impacted Commission Staff's natural
11 gas revenue requirement filed on June 30, 2017. Commission Staff's data request
12 response provided updated work papers for Exhibits BAE-2 and BAE-3
13 (Commission Staff Data Request 28) as well as certain pages within Exhibits
14 MCC-7, MCC-8 and MCC-10 (Commission Staff Data Request 27). I have
15 provided an excerpt of Commission Staff's Data Requests 27 and 28 as Exhibits
16 SEF-18 and SEF-19. PSE is providing these data request responses as they will
17 illustrate that PSE and Commission Staff have fewer differences in position
18 related to working capital once Commission Staff's Response to PSE Data
19 Request Nos. 27 and 28 are taken into account versus the way it is reflected in
20 Table 1 above. I will discuss this in more detail in the working capital discussion
21 in Section IV.G. below.

1 **III. NATURAL GAS AND COMMON ADJUSTMENTS THAT**
 2 **ARE UNCONTESTED BETWEEN PSE AND OTHER PARTIES**

3 **Q. Would you please provide a list of all gas and common adjustments that are**
 4 **uncontested between PSE and the parties?**

5 A. Yes. Table 2 below is a list of adjustments that are uncontested between PSE and
 6 the parties.

7 **Table 2. Listing of Uncontested Adjustments**

Adjustment	NOI	Rate Base
Actual Results of Operations	\$119,145,769	\$1,727,319,760
15.01 - Revenues and Expenses	\$(32,674,131)	
15.03 - Pass-through Rev and Expenses	\$736,148	
15.04 - Federal Income Tax	\$700,822	
15.05 - Tax Benefit of Proforma Interest	\$18,529,101	
15.07 - Normalize Inj & Damages	\$(57,738)	
15.08 - Bad Debt	\$35,240	
15.09 - Incentive Pay	\$104,023	
15.10 - D&O Insurance	\$11,636	
15.11 - Interest on Customer Deposits	\$(50,137)	
15.14 - Property & Liability Ins	\$45,174	
15.16 - Wage Increase	\$(907,409)	
15.17 - Investment Plan	\$(46,689)	
15.18 - Employee Insurance	\$(58,781)	
15.20 - Payment Processing Costs	\$(1,449,117)	
15.21 - South King Service Center	\$212,048	\$7,775,116
15.22 - Excise Tax and UTC Filing Fee	\$33,509	
16.01 - Cost Recovery Mechanism	\$(4,003,724)	\$19,011,807

1 **Q. Are there adjustments where PSE and other parties differ, but which are not**
2 **contested?**

3 A. Yes. Below is a list of those adjustments and an explanation as to why PSE's
4 adjustment has changed since its original filing or why the adjustment differs
5 from other parties' adjustments.

6 **A. Tax Benefit of Proforma Interest, Adjustment KJB-20.05 and SEF-**
7 **15.05**

8 Parties do not contest the way that the tax benefit of interest is calculated.
9 However, since rate base is a factor in determining the tax benefit of interest, the
10 total amount of this adjustment will differ between PSE and other parties where
11 there are differences associated with rate base items.

12 **B. Payment Processing Costs, Adjustment KJB-20.20 and SEF-15.20**

13 PSE has accepted the lengthening of the Payment Processing Deferral from one
14 year to three years that has been proposed by Commission Staff and Public
15 Counsel. ICNU and NWIGU have indicated they are neutral related to this
16 adjustment.¹ Therefore, this adjustment is no longer contested and the change to
17 net operating income for this adjustment is a decrease of \$2,010,221 for electric
18 and \$1,449,117 for natural gas operations.

¹ Mullins, Exh. BGM-4 at 1:21.

1 **C. Changes by PSE at Supplemental Ignored by ICNU and NWIGU**

2 **Q. Are there other adjustments to natural gas operations where ICNU and**
3 **NWIGU differ from PSE that were not described as differences by Mr.**
4 **Mullins?**

5 A. Yes. After reviewing Mr. Mullins' work papers, it became apparent that there are
6 other adjustments to natural gas operations where ICNU and NWIGU differ from
7 PSE, but that were not described as differences by Mr. Mullins. It appears that
8 Mr. Mullins has ignored the updates made by PSE in its supplemental filing and
9 did not specifically accept or reject these updates.

10 **Q. What adjustments were updated at supplemental and ignored by Mr.**
11 **Mullins?**

12 A. The following natural gas adjustments were changed in PSE' supplemental filing
13 made on April 3, 2017 for the reasons discussed in my prefiled supplemental
14 testimony, Exhibit SEF-8T:

15 SEF-11.02 Temperature Normalization
16 SEF-11.08 Bad Debt Expense
17 SEF-11.09 Incentive Pay
18 SEF-11.11 Interest on Customer Deposits
19 SEF-11.16 Wage Increase
20 SEF-11.17 Investment

21 Commission Staff filed testimony addressing temperature normalization, but other
22 than that, no party provided testimony contesting these adjustments, including
23 Mr. Mullins for ICNU and NWIGU. Absent testimony directly contesting these
24 adjustments, PSE must assume that it was an oversight on the part of Mr. Mullins.

1 Therefore, any differences in the proposed revenue requirement between PSE and
2 ICNU and NWIGU resulting from these adjustments should be rejected and
3 PSE's adjustment should be approved.

4 **IV. CERTAIN COMMON CONTESTED ADJUSTMENTS**

5 **Q. Would you please describe the difference between PSE and other parties on**
6 **the contested adjustments you are addressing in your testimony?**

7 A. The impact on natural gas net operating income and rate base for each PSE
8 adjustment is summarized on Exhibit SEF-14. All of the contested adjustments I
9 will discuss are common to both electric and natural gas, and I will discuss why
10 the Commission should adopt PSE's proposed adjustments. Additionally, I am
11 presenting the impact of these adjustments on natural gas operations and am
12 presenting the overall impact on the natural gas revenue deficiency in my
13 testimony. PSE witness Ms. Katherine J. Barnard will be presenting the electric
14 only adjustments and the remaining common adjustments that are contested
15 between PSE and the parties, and she explains why the Commission should adopt
16 PSE's proposed adjustments. Ms. Barnard will also present the impact of those
17 adjustments on electric operations and will present PSE's base rates revenue
18 deficiency for electric.

1 **A. Temperature Normalization, Adjustment KJB-20.02 and SEF-15.02**

2 **Q. Please explain the difference between PSE and Commission Staff with**
3 **respect to the temperature normalization adjustment.**

4 A. Commission Staff recommends this adjustment be calculated using the system
5 level weather normalization. Please see the Rebuttal Testimony of Dr. Chun K.
6 Chang, Exhibit CKC-3T, for the reasons why the Commission should disregard
7 Commission Staff's recommendation and accept PSE's adjustment as proposed.
8 This adjustment has not changed since PSE's supplemental filing and increases
9 natural gas net operating income by \$16,046,445.

10 **B. Depreciation Study, Adjustment KJB-20.06 and SEF-15.06**

11 **Q. Has PSE changed its adjustment for natural gas depreciation expense in its**
12 **rebuttal filing?**

13 A. No. Public Counsel witness Ms. Roxie M. McCullar proposes changes to PSE's
14 natural gas and common depreciation rates. Mr. John J. Spanos in Exhibit JJS-
15 04T and Ms. Katherine J. Barnard in Exhibit KJB-17T each discuss why Ms.
16 McCullar's recommendations should be rejected. Additionally, Ms. Barnard
17 discusses errors in the way Mr. Ralph C. Smith, for Public Counsel, has applied
18 the depreciation rates recommended by Ms. McCullar and why his proposed
19 changes should be rejected. Accordingly, PSE has not changed its natural gas
20 depreciation adjustment in this rebuttal filing.

1 **C. Rate Case Expenses, Adjustment KJB-20.12 and SEF-15.12**

2 **Q. Please provide the background related to the rate case expense adjustment.**

3 A. Commission Staff's proposed adjustment is not consistent with the Commission's
4 long established requirement to normalize rate case expenses. The current method
5 to normalize a representative level of rate case expenses was proposed by
6 Commission Staff and approved in PSE's 2004 general rate case. The method for
7 determining a representative level of rate case expenses was further defined in
8 PSE's 2006 general rate case. Since then, PSE has used this normalized approach,
9 which was presented and approved in PSE's 2006, 2007, 2009 and the 2011
10 general rate cases. Normalization of expenses to provide a smoothing effect for
11 fluctuating costs that are not consistent from year to year is a common practice.
12 This adjustment recognizes that rate case expenses by their nature are incurred
13 after the test year, are incurred on an irregular basis, are highly variable and that
14 in order to normalize the test year, a representative amount of rate case expense is
15 determined. Since the 2006 general rate case, that representative basis has been
16 the average cost of the prior two general rate cases. Then, the amount is
17 normalized over a representative period between cases.

18 **Q. What normalization period has been used in past cases?**

19 A. The normalization period has changed over the years. The 2004 general rate case
20 set it at three years. In the 2006 general rate case, two years was used, and in the
21 2011 rate case, the normalization period for power cost only rate cases

1 (“PCORC”) was lengthened to four years in recognition of the slowed paced at
2 which PSE was then filing PCORCs.

3 **Q. What normalization period does PSE propose in this case?**

4 A. PSE’s proposed adjustment follows this long-standing methodology. Although
5 PSE has not filed a general rate case every two years in the recent past, no change
6 was made to the normalization period for rate case expenses as PSE is not
7 proposing another rate case “stay out” in this proceeding. The last five years, with
8 the multi-year rate plan and “stay-out” requirements, are not representative of
9 PSE’s general rate case frequency on a going forward basis. Therefore, a change
10 to the normalization period is not warranted. Likewise, although in the recent past
11 PSE has filed PCORCs more frequently than every four years, PSE did not
12 propose to shorten the normalization period for PCORCs because not enough
13 information is available to establish that the existing normalization period will not
14 continue to be reasonable in the future.

15 **Q. Please explain why the Commission Staff adjustment to Rate Case Expense**
16 **should not be accepted.**

17 A. Ms. Cheesman relies on the test year balance of FERC 928 regulatory expense
18 because she claims it is representative of the last six years of expenses. However,
19 her adjustment ignores the fact that PSE has not filed a general rate case since
20 2011 due to the multi-year rate plan and, therefore, the six-year average is not a
21 representative comparison for purposes of this adjustment.

1 Additionally, Ms. Cheesman's use of the entire FERC 928 regulatory expense
2 masks the issue. Rather than comparing the level of general rate case expense in
3 the test year to the average level of general rate case expenses, she utilizes the
4 entire FERC 928 regulatory expense account. This is improper because more than
5 80 percent of the account balance in any given year is related to regulatory fees,
6 not filing related expenses. It is not reasonable to assume that the test period
7 general rate case expense of \$269,000, which represents only three percent of the
8 FERC 928 test year total, is representative of the costs associated with
9 adjudicating a rate case. Therefore, the Commission should approve the
10 continuation of PSE's rate case expense adjustment as calculated by PSE.

11 Ms. Cheesman in part supports her recommendation based on PSE's Response to
12 Data Request No. 382, which requested PSE to provide a breakdown of FERC
13 account 928 for calendar years 2011, 2013 and the test year. According to
14 Ms. Cheesman, the average expenses related to UTC filings (including general
15 rate case filings) represented about ten percent of the overall balance in each of
16 those years. She then assumes the test year level of FERC 928 is reasonable
17 because UTC filings represent approximately ten percent of the test year balance.

18 **Q. Is Ms. Cheesman's assumption correct?**

19 A. No. This is an incorrect assumption for two reasons. First, Ms. Cheesman picks
20 selective years for her average and does not disclose that there is a wide variance
21 in the three years she has selected with the low being five percent and the high
22 being three times higher at fifteen percent. This wide range demonstrates the

1 variability of the costs and the need for a normalizing adjustment. Second,
2 Ms. Cheesman fails to recognize that many of the costs associated with a general
3 rate case fall outside of a test year period and rarely are captured entirely within
4 the calendar year of filing. For example, using the test year for the current case
5 fails to pick up costs for discovery such as the more than 1,000 data requests PSE
6 responded to in this case, nor does it pick up the costs for prehearing conferences,
7 preparation of rebuttal testimony or the hearing. I have included Exhibit SEF-20
8 that demonstrates the relationship of a rate case procedural calendar to when the
9 rate case expenditures are made relative to that calendar and, specifically, to the
10 relative test year within that proceeding. This exhibit demonstrates that the bulk
11 of rate case expenses are spent in between test years. So while it may be true that
12 test year rate case expenses are relatively consistent with 2011 and 2013²,
13 Ms. Cheesman's request does not fully reflect the actual costs associated with
14 preparing and adjudicating a rate case and therefore her adjustment should be
15 rejected.

16 **D. Deferred Gains and Losses on Property Sales, Adjustment SEF-15.13**

17 **Q. Have you updated this adjustment in this rebuttal filing?**

18 A. No. For the reasons stated below, PSE believes the Commission should accept
19 PSE's adjustment as filed and so I have not updated this adjustment.

² It is worth noting that there would not have been general rate case costs included in 2013.

1 **Q. Please explain the change Commission Staff is recommending to this**
2 **adjustment.**

3 A. Ms. Cheesman recommends removing \$280,362 of a deferred loss from this
4 adjustment because she believes that PSE is seeking to recover a deferred loss
5 associated with the sale of a property that she believes was non-utility property.

6 **Q. Does PSE agree with Ms. Cheesman's assessment of this loss?**

7 A. No. The transaction in question involves a real property parcel located in Kent,
8 Washington used to install a high pressure gas main. The property was used and
9 useful from 2004, when it was purchased, placed in service and recorded in FERC
10 101, and it remained used and useful and recorded in FERC 101 until 2014 when
11 it was sold.

12 **Q. Why does Ms. Cheesman believe that this property was not used and useful**
13 **and in utility operations for the entire time PSE owned this property?**

14 A. It is not clear what information Ms. Cheesman is relying on to state that the
15 property was booked in non-utility property for more than a decade, which is not
16 correct. Ms. Cheesman indicates that the property was recorded in non-utility
17 plant for more than a decade³ despite the opposite being stated in PSE's response
18 to the data request on which Ms. Cheesman relies. On page 2 of part of PSE's
19 response, provided as Exhibit MCC-17, PSE reported the property was "Held in
20 utility plant," which is a reference to the FERC account (FERC 101) in which the

³ Cheesman, Exh. MCC-1T at 22:10-14.

1 property was booked. In order for there to be no doubt, Exhibit SEF-21 provides a
2 copy of the journal entry showing that the property was moved from utility
3 property to non-utility property in 2014 at the time it was sold.

4 Ms. Cheesman appears to be basing her claim that the property was non-utility
5 property on Exhibit MCC-17, PSE's Response to Commission Staff Data Request
6 No. 372, which included a copy of the journal entry showing the proceeds from
7 the sale and original cost being posted to FERC 121 Non-Utility Property
8 accounts. It appears, Ms. Cheesman puts more reliance on only one of the journal
9 entries provided than on the fact that PSE stated the property was in service and in
10 utility plant from the time it was owned until the time it was sold. PSE stated in
11 that response that "the property was held in utility plant in service from 2004
12 when it was owned until 2014 when it was sold."⁴ In PSE's response to the data
13 request, PSE provided the initial entry recorded to a non-utility account on which
14 Ms. Cheesman is basing her claim, but PSE also provided the additional
15 downstream journal entries that are required to be booked at the same time in
16 order to recognize the transactions in the appropriate FERC accounts.

17 **Q. Please describe PSE's procedure for recording land sales transactions.**

18 A. The following documentation from PSE's Controller's Manual, which was
19 provided to parties in discovery, provides PSE's accounting process for recording
20 land sales transactions;

⁴ Cheesman, Exh. MCC-17 at 2, part f. "Held in utility plant" is a reference to the FERC account (FERC 101) in which the property was booked.

1 Utility Property should be transferred to Nonutility Property when
2 there is no longer a plan to use the property in Utility Operations.
3 *All land sale orders (LBSA) are set up in PowerPlant to*
4 *automatically post costs to the nonutility account (121) before*
5 *continuing to calculate the gain or loss. It does not make any*
6 *difference which account (101 - Plant in service or 105 – Future*
7 *Use) the land is in at the time of sale, the cost in the LBSA order*
8 *will go to FERC Account 121 – Nonutility Property. At month end*
9 *when the gain/loss is calculated, the costs in the Account 121 –*
10 *Nonutility Property will be transferred to the appropriate gain/loss*
11 *account.*⁵

12 It is an administrative processing function of PSE’s property accounting system
13 that resulted in the original cost and net proceeds being booked to a non-utility
14 SAP account number, not because the property was ever held as non-utility
15 property. This is why the property and net proceeds were originally booked to
16 non-utility plant and the resulting loss was transferred to the appropriate FERC
17 187 Account in the same month the property was sold.⁶ Because the property was
18 used and useful and in service from the time it was purchased to the time it was
19 sold, PSE has appropriately included the deferred loss in its adjustment, and
20 Commission Staff’s adjustment should not be accepted.

21 **Q. Do you have any other concerns with Ms. Cheesman’s testimony related to**
22 **gas deferred gains and losses?**

23 A. Yes. On page 22 of her testimony, she states “it is very important that utilities do
24 not count proceeds, and possibly gains, as non-utility property but then count

⁵ PSE’s Controller’s Manual, CTM-1 on Land Accounting Transactions, p. 4 (emphasis added).

⁶ PSE originally posted the manual entry to an electric FERC 187 account. *See* Cheesman, Exh. MCC-16 at 5-6. The correction to move the amounts from the electric FERC 187 account to a gas FERC 187 account was made in February 2015. *See* Cheesman, Exh. MCC-16 at 4.

1 losses as utility property.” Ms. Cheesman’s innuendos lack support and should be
2 disregarded by the Commission. PSE does not count proceeds and gains as non-
3 utility property and then count losses as utility property and there is no evidence
4 supporting such a practice. As an example of a deferred gain being processed in
5 the same manner as the loss on the Kent property, I have provided Exhibit SEF-
6 22, which contains a copy of the system entries associated with this deferred gain.
7 The same accounting procedures were followed where the property was
8 transferred to non-utility at the time it was sold, and the initial PowerPlant
9 interface entry to record the gain was posted to a non-utility account. Then, the
10 gain was manually transferred to the appropriate electric FERC 256 account. In
11 summary, PSE is following the same procedures as set forth in its Controller’s
12 Manual whether the transaction results in a deferred gain or a deferred loss.

13 **Q. Should the Commission accept Commission Staff’s proposed adjustment to**
14 **natural gas deferred gains and losses?**

15 A. No. PSE has demonstrated that for the entire time the property was owned, it was
16 used and useful for utility operations and was recorded in utility plant in service.
17 PSE has also demonstrated that it followed its own internal accounting processes
18 in the way it booked the loss to a FERC 121 non-utility account and, within the
19 same month that the property was sold, transferred the loss to a FERC 187
20 account. Therefore, the deferred loss is appropriate for recovery, and Commission
21 Staff’s recommendation to disallow it should not be accepted.

1 **E. Pension Plan, Adjustment KJB-20.16 and SEF-15.16**

2 **Q. Has PSE changed its adjustment for natural gas pension expense in its**
3 **rebuttal filing?**

4 A. No. Ms. Katherine J. Barnard in her Prefiled Rebuttal Testimony, Exhibit KJB-
5 17T, explains the proposals made by Public Counsel, ICNU and NWIGU for this
6 adjustment and why their proposals should be rejected. Accordingly, PSE has not
7 changed its natural gas pension adjustment in this rebuttal filing.

8 **F. Environmental Remediation, Adjustment KJB-20.19 and SEF-15.19**

9 **Q. Do you agree with Ms. O’Connell’s view of PSE’s unassigned insurance**
10 **recoveries for environmental remediation?⁷**

11 A. No. Ms. O’Connell indicates that PSE’s practice of holding certain insurance
12 recoveries for environmental remediation costs as unassigned means “they can be
13 used at the Company’s discretion to offset the costs of any project.”

14 Ms. O’Connell’s interpretation of why PSE held the insurance recoveries as
15 unassigned misunderstands the reasons PSE held the recoveries in this way.

16 **Q. Why does PSE elect to not assign some insurance recoveries?**

17 A. As discussed in more detail in the Prefiled Rebuttal Testimony of Mr. Steven R.
18 Secrist, Exhibit SRS-1T, the insurance recoveries were held as unassigned
19 because many of PSE’s insurance policies covered past, current and future costs

⁷ O’Connell, Exh. ECO-1CT at 8:12-13.

1 for multiple sites and because at the time of recovery, allocating the recoveries to
2 a specific site would be premature until all cleanup costs were known for a
3 particular site. Thus, prematurely assigning recoveries to a particular site when
4 cleanup costs were not fully known could harm PSE and its predecessors in
5 litigation and settlement positions with PSE'S insurers. By not prematurely
6 assigning recoveries to specific projects in settlement agreements and
7 subsequently in the tracking of those recoveries, PSE was able to appropriately
8 optimize the amount of recoveries received through litigation and settlement.
9 Through insurance buyback agreements, PSE was able to secure recoveries that
10 were not allocable to specific sites, but to groups of sites that covered past and
11 future expenses.

12 **Q. Do you agree with Ms. O'Connell that assigning the unassigned insurance**
13 **recoveries to specific projects would result in a more accurate accounting of**
14 **PSE's obligations⁸?**

15 A. No. In fact, from an accounting perspective, it is clearer if the project costs and
16 recoveries are tracked separately. During the test year, PSE had existing deferrals
17 of environmental remediation costs totaling \$9.5 million for electric and \$72.2
18 million for gas and had recoveries of \$5.3 million for electric and \$50.3 million
19 for gas.⁹ Ignoring Ms. O'Connell's other recommendations to write off certain

⁸ O'Connell, Exh. ECO-1CT at 3:21 – 4:1, and at 15-16.

⁹ See Rork, Exh. JKR-3. While some recoveries were directly netted against the deferred costs for reporting purposes, they are for the most part tracked in separate SAP balance sheet accounts so as to still be separately identifiable.

1 balances, which I will address later, if the recoveries were netted against the
2 deferred costs as Ms. O'Connell recommends, PSE's books would only reflect
3 deferred costs of \$4.2 million for electric and \$21.7 million for gas. This is less
4 informative than knowing the amount of the original costs and original recoveries.
5 While at some point deferred costs can be settled and recoveries can be applied
6 and accounts closed, it does not provide clarity to net recoveries against deferred
7 cost balances that have the potential to incur additional future costs, particularly if
8 doing so would harm PSE in litigation or negotiations with existing insurers.
9 Further, zeroing out deferred costs by offsetting them with recoveries would
10 artificially mask the amount of total costs deferred on sites where remediation is
11 not complete. Therefore, the more appropriate way to handle the accounting for
12 deferred costs and recoveries is to only apply recoveries to sites when the
13 potential for significant additional costs or recoveries is low. Exhibit SEF-23
14 contains a listing of the gas and electric environmental remediation deferral
15 accounts and a comparison of PSE's and Commission Staff's recommendations of
16 which environmental deferral accounts should have recoveries applied to them
17 and their balances closed.¹⁰ In the end, whether or not PSE's or Commission
18 Staff's recommendations for assignment of unallocated recoveries is utilized, the
19 total amounts set in rates does not change; however, PSE's recommendation

¹⁰ Staff's recommendations were obtained from Staff's work papers entitled "170033-Staff-WP-ECO-Environ Rem 13.19.xlsx" and "170034-Staff-WP-ECO-Environ Rem 11.19.xlsx" which are presented as pages 3 and 4 in Exhibit SEF-23.

1 provides a more sensible allocation based on the actual conditions of the
2 remediation sites being tracked.

3 **Q. Commission Staff, Public Counsel, ICNU and NWIGU all recommend that**
4 **PSE should pass back 100 percent of the insurance recoveries now, rather**
5 **than reserving a portion to be passed back to offset the costs of remediation**
6 **in the future.¹¹ Should their approach be accepted?**

7 A. No. As stated in the Prefiled Rebuttal Testimony of . Steven R. Secrist, Exhibit
8 SRS-1T, PSE has substantially exhausted its ability to recover insurance on
9 legacy policies held by PSE's predecessors and the prospect of significant
10 additional recoveries is low. However, PSE continues to incur costs for
11 environmental remediation projects. Given this situation, PSE has proposed to
12 allocate a portion of the proceeds currently recovered to the existing deferred
13 costs and to reserve the remaining insurance recoveries to use to offset future
14 remediation costs to be requested in future proceedings. Providing all of the
15 recoveries now does not provide a proper matching of the underlying costs for
16 which the recoveries were received. The insurance policies and third-party
17 recoveries PSE has obtained are intended to cover costs for past, present, and
18 future environmental remediation on the covered sites. Applying all of these
19 proceeds to past and current costs would unnecessarily harm future customers
20 who would be responsible for paying for remediation costs without receiving the

¹¹ Smith, Exh. RCS-1CT at 65:4-13; Mullins, Exh. BGM-1CTr at 47:20-23; O'Connell, Exh. ECO-1CT at 16:8-10.

1 offsetting benefit of related insurance recoveries. Likewise, existing customers
2 would receive a disproportionate amount of the insurance recoveries while only
3 paying a portion of the related remediation costs.

4 **Q. Mr. Ralph C. Smith for Public Counsel claims that PSE indicated that the**
5 **actual unassigned insurance recoveries received to date do not represent**
6 **future remediation or monitoring obligations.¹² Is this an accurate portrayal?**

7 A. No. Mr. Smith cites to page 12 of his Exhibit RCS-9, which contains PSE's
8 Response to Commission Staff Data Request No. 284. That data request asked
9 how much of the future obligations were identified in the recoveries received.
10 Because obligations are a completely different category than recoveries, PSE
11 indicated that the recoveries being pointed to in the data request did not represent
12 obligations – meaning, there were no obligations recorded within the recoveries
13 account balance that was being referenced in the question. Mr. Smith's testimony
14 is misleading because it attempts to present PSE's response to mean that the
15 insurance recoveries received were not designated to recover future cost
16 obligations. Please see the Prefiled Rebuttal Testimony of Steven R. Secrist,
17 Exhibit SRS-1T, which discusses the applicability of the insurance recoveries and
18 how they were obtained through PSE's release of claims for all current and future
19 obligations. Mr. Smith's misrepresentation of what the insurance proceeds cover
20 and his use of this to justify inclusion in rates now of 100 percent of the
21 recoveries should be rejected.

¹² Smith, Exh. RCS-1CT at 62:1-6.

1 **Q. Ms. O’Connell claims that PSE’s proposal to pass back a pro-rated portion**
2 **of the insurance recoveries is an arbitrarily-sized contingency fund and**
3 **departs from Commission guidance.¹³ Do you agree?**

4 A. No. I disagree with her claim for several reasons. First, Ms. O’Connell ignores
5 relevant parts of the prevailing Commission orders on PSE’s accounting for
6 environmental remediation. She states that the orders explicitly instruct that
7 deferred amounts should be net of all recoveries before being eligible for
8 amortization and recovery in rates.¹⁴ However, there is language in multiple
9 orders that state *all costs* and recoveries must be known prior to requesting
10 recovery.¹⁵ As an example, Ms. O’Connell cites to a Commission accounting
11 order which states that:

12 Costs that are deferred will be reduced by any insurance or third
13 party proceeds before being eligible for amortization.¹⁶

14 However, Ms. O’Connell omits reference to the next condition shown in
15 paragraph (e) of the order that states:

16 Allowed net deferred costs will be amortized over a five year
17 period on the date *all costs* net of recoveries become known and

¹³ O’Connell, Exh. ECO-1CT at 16:10-12.

¹⁴ O’Connell, Exh. ECO-1CT at 16:3-4.

¹⁵ See *Petition of Puget Sound Energy, Inc. for An Accounting Order Regarding the Accounting Treatment for Costs of its Electric Environmental Remediation Program*, Dockets UE-070724 and UE-072060 and UE- 081016, Order 01, 3 § (e) (Oct. 8, 2008); and *Application of Puget Sound Power & Light Company and Washington Natural Gas Company for An Order Authorizing Merger*, Docket UE-951270 and UE-960195, Fourteenth Supplemental Order Accepting Stipulation; Approving Merger, 22 § 2 (Feb. 5, 1997).

¹⁶ Dockets UE-070724, UE-072060 and UE- 081016, Order 01, page 3 ¶ (d).

1 declared prudent. The deferrals will be consistent with the
2 Commission's Merger Order in Docket UE-960195.¹⁷

3 **Q. Are all costs net of recoveries known?**

4 A. No. As mentioned earlier in my testimony, all costs of many of PSE's remediation
5 sites are not fully known. As evidenced by PSE's history, environmental
6 remediation projects can take several decades to fully resolve, and even then,
7 there are often changes that require additional work based on reopeners and
8 requirements of state and federal laws. The intention of the environmental
9 remediation orders was a reasonable one, to net recoveries against costs, and once
10 all costs and recoveries are known, approval and amortization could begin. In
11 reality, however, it is PSE's experience that for some sites, not all costs can be
12 known with certainty even once the projects have been closed. The one thing that
13 is certain at this time is that insurance recoveries on PSE's legacy policies have
14 been exhausted.

15 **Q. How should the Commission proceed on the costs and recoveries for**
16 **environmental remediation that span several decades?**

17 A. Based on current Commission guidance, there are really two choices. Continue to
18 hold recoveries until all costs are known—which could be decades from now—
19 and then request the net deferrals be set in rates, or as PSE is proposing, approve
20 costs to date to be set in rates and net against those costs a commensurate amount
21 of recoveries. PSE's proposal strikes a reasonable balance given current

¹⁷ *Id.* ¶ (e) (emphasis added).

1 Commission guidance based on the reality of environmental remediation projects
2 and the complicated process of optimizing recoveries for the benefit of customers.
3 Additionally, it properly addresses the matching of the benefits of existing
4 insurance recoveries to the current and future costs for which the recoveries were
5 received and best addresses the intergenerational aspects of complex, ongoing,
6 remediation projects, the handling of which has been determined prudent by
7 Commission Staff.

8 **Q. How do you respond to the additional Commission guidance identified by**
9 **Ms. O’Connell?**

10 A. Ms. O’Connell cites guidance from the Commission that states:

11 Any recovery of insurance proceeds...would be treated *in a*
12 *manner that corresponds* with the treatment of the underlying costs
13 to which the recovery relates.¹⁸

14 This Commission guidance is relevant in determining how to handle the existing
15 situation where recoveries are known but not all cost are known. Matching of the
16 recoveries to the past and future cost can be considered to be corresponding
17 treatment in conformity with the citation above.

18 Finally, it is worth noting that Ms. O’Connell again narrowly cites to a section of
19 another Commission order which reads:

¹⁸ *Washington Natural Gas Company’s Accounting Petition for Environmental Remediation Program*, Docket UG-920781, 2 § (d) (Nov. 25, 1992)(emphasis added). Language very similar to this also appears in *Petition of Puget Sound Power & Light for An Order Regarding the Accounting Treatment for Costs of its Environmental Remediation Program*, Docket UE-911476, Order Authorizing Accounting Treatment, 3 § (3) (Apr. 1, 1992).

1
2
3
4
5
6
7
8
9
10
11
12
13

Deferred costs will be reduced by any insurance proceeds or payments from other responsible parties recovered by Petitioner in respect of such costs....¹⁹

Again, she omits another relevant section in part b on the same page, which provides guidance that would allow discretion in how rates can be set related to environmental costs:

Deferred costs will be recovered in rates using an appropriate method as determined in such proceedings²⁰

Therefore, based on the foregoing and given the existing Commission guidance and the current set of circumstances associated with PSE's environmental remediation program costs and recoveries, PSE's balanced and reasonable proposal for reserving a portion of unassigned recoveries for future remediation costs should be accepted.

¹⁹ *Petition of Puget Sound Power & Light for An Order Regarding the Accounting Treatment for Costs of its Environmental Remediation Program*, Docket UE-911476, Order Authorizing Accounting Treatment, 5 § (d) (Apr. 1, 1992).

²⁰ *Id.*

1 **Q. On page 15 of her Response Testimony, Ms. O’Connell states that PSE’s**
2 **underlying rationale for reserving unassigned recoveries is based on**
3 **Generally Accepted Accounting Principles (“GAAP”) under Financial**
4 **Accounting Standards Board Accounting Standards Codification No. 410-30-**
5 **25 Asset Retirement and Environmental Obligations (“ASC 410-30-25”).²¹ Is**
6 **that true?**

7 A. No. PSE’s rationale for reserving unassigned recoveries is based on the reasons
8 set forth in the preceding answer. PSE’s use of the estimates of future costs that
9 are developed in order to conform with ASC 410-30-25 is merely the means by
10 which PSE established a reasonable measure for how much of the recoveries to
11 reserve to offset future costs. PSE estimated the total costs for each project by
12 taking the existing costs at September 30, 2016, and adding to it the mid-range of
13 the future cost estimate.²² The existing costs for all projects were then divided by
14 the total estimated cost for all projects to develop the percentage of proceeds to
15 pass back with the existing costs being requested for recovery in this case. The
16 remaining recoveries PSE proposes be held to cover the estimated future costs.
17 These future costs are known to exist based on the highly regulated and formal
18 process that exists related to managing environmental remediation projects.²³ The
19 estimates are measured by third party environmental experts who provide a range
20 of costs based on their expertise in the industry. PSE utilized the mid-point of the

²¹ O’Connell, Exh. ECO-1CT at 15:15-21.

²² As had already been developed for use in conformity with PSE’s GAAP accounting requirements under ASC 410-30-25.

²³ *See generally* O’Connell, Exh. ECO-1CT at 12 and 15.

1 range to develop its proration. Use of the future cost estimates developed for
2 conformity with ASC 410-30-25 presents a reasonable basis for calculating the
3 portion of unassigned recoveries that can be reserved for future costs and the
4 portion that can be applied to current costs.

5 **Q. Do you agree with the way that Mr. Bradley G. Mullins for ICNU and**
6 **NWIGU is questioning the legitimacy of PSE's net environmental**
7 **remediation deferrals?²⁴**

8 A. No. Other parties were able to research the relevant prevailing orders and
9 determine that in general all costs are subject to prudence review for recovery
10 purposes.²⁵ It is unclear why Mr. Mullins did not conduct similar research before
11 accusing PSE of having illegitimate deferrals.

12 **Q. Can you please respond to Mr. Mullins' comments about PSE's method for**
13 **setting aside insurance recoveries as being speculative?²⁶**

14 A. Yes. As stated above, the need to expend additional funds on remediation sites is
15 known to exist and the estimates of those future costs are measured by third party
16 environmental experts who provide a range of costs based on their expertise in the
17 industry. Mr. Mullins believes that the wide range of costs is a basis for not
18 approving the method for determining the allocation. To address this, in its
19 original filing, PSE advocated using the middle of the range of estimated

²⁴ Mullins, Exh. BGM-1CT at 47:1-6.

²⁵ O'Connell, Exh.ECO-1CT at 9:13.

²⁶ Mullins, Exh. BGM-1CT at 47:7-14.

1 environmental remediation costs for purposes of calculating the allocation.
2 However, if the Commission is concerned about the wide range of estimated
3 costs, the low end of the range could be utilized to calculate the allocation. Doing
4 so would result in a reduction to operating expense of approximately \$200,000 for
5 electric and close to \$800,000 for natural gas operations. I have prepared Exhibits
6 SEF-24 and SEF-25 showing the calculation for these impacts.

7 **Q. Do you agree with Ms. O’Connell’s recommendation to disallow \$5.6 million**
8 **of deferred costs associated with the Tacoma Historical Coal Gasification**
9 **Plant situated on the Tacoma Tide Flats (“Tacoma Tar Pits”)²⁷?**

10 A. No. Ms. O’Connell is using flawed logic to conclude that there should be a \$5.6
11 million write off of the Tacoma Tar Pits deferral. PSE should not be required to
12 write off expenses or recoveries that it has prudently incurred or received related
13 to its deferred environmental remediation orders.

14 **Q. Can you please provide a background of the Tacoma Tar Pits deferral and**
15 **Ms. O’Connell’s proposal?**

16 A. To understand this issue, it is important to understand the insurance litigation that
17 occurred related to the Tacoma Tar Pits and other remediation sites. As is
18 described in the Prefiled Rebuttal Testimony of Mr. Steven R. Secrist, Exhibit
19 SRS-1T, during the early to mid-1990s, a PSE predecessor company, Washington
20 Natural Gas (“WNG”), engaged in extensive and aggressive insurance litigation

²⁷ O’Connell, Exh. ECO-1CT at 18.

1 to recover from legacy insurers costs related to past and future remediation
2 obligations at manufactured gas plant sites, the largest by far of which was the
3 Tacoma Tar Pits site. The litigation encompassed dozens of insurers and lasted
4 many years during which time WNG engaged in settlement discussions with the
5 multitude of insurers. In pre-trial negotiations, many of the insurers settled with
6 WNG and prior to the 1993 trial, WNG had already received \$7.6 million in
7 settlement proceeds. WNG then went to trial against the four remaining insurers
8 and in October 1993, received a favorable verdict. The trial defendants all filed
9 appeals. During post-trial adjudication, WNG and the trial defendants were able
10 to reach settlement and \$29 million of additional recoveries was received for the
11 Tacoma Tar Pits site.

12 In developing her recommendation to order PSE to write-off \$5.6 million of
13 prudently incurred and deferred costs, Ms. O'Connell again points to very narrow
14 information provided by PSE and ignores other relevant information that
15 undermines her recommendation.

16 **Q. Please elaborate on the incomplete information Ms. O'Connell relies on to**
17 **propose a disallowance of \$5.6 million.**

18 A. Ms. O'Connell pairs two numbers together – \$29 million of recoveries received in
19 1995 and \$34.6 million of deferred costs reported in 1998 – and erroneously
20 presents them as if they are the totality of the information related to the Tacoma
21 Tar Pits remediation site. She points to a letter from Mr. Secrist to the
22 Commission in November 1995 (“November 1995 letter”), which stated that the

1 \$29 million would “pay substantially all unreimbursed remediation costs incurred
2 by WNG for the remediation of the Tacoma Tar Pits site.”²⁸ She then points to the
3 opening system conversion entry on PSE’s books that occurs in September 1998²⁹
4 reflecting net deferred costs of \$34.6 million for Tacoma Tar Pits. And by netting
5 only the \$29 million of recoveries against the \$34.6 million of costs, she
6 apparently assumes that the \$34.6 million of costs included in one account on
7 PSE’s general ledger three years after the recoveries are received are the same
8 “unreimbursed costs” referenced in Mr. Secrist’s November 1995 letter. In fact,
9 she testifies that “[t]he company documented to the Commission that the recovery
10 would offset all or substantially all of the remediation obligation” and uses this as
11 the basis for her write-off.³⁰ Ms. O’Connell’s testimony ignores the language in
12 Mr. Secrist’s November 1995 letter that the \$29 million would pay substantially
13 all unreimbursed remediation costs incurred by WNG. She erroneously presents
14 the \$34.6 million as the “unreimbursed costs”.

²⁸ O’Connell, Exh. ECO-13 (emphasis added).

²⁹ PSE was unable to locate the original transactions that existed in WNG’s legacy accounting system. Conversion from the legacy systems of Puget Sound Power & Light and WNG to the newly established PSE accounting system occurred in September 1998. In PSE’s Response to Commission Staff DR 269, PSE was able to reflect information prior to September 1998 related to the insurance recoveries through use of legacy reports produced from WNG’s accounting system. See O’Connell, Exh. ECO-12. In an attachment to the supplemental response that was submitted shortly before Commission Staff filed their Response Testimonies, PSE was able to produce invoices which supported all but approximately \$400,000 of the \$34.6 million of deferred costs that comprised the conversion entries which established PSE’s general ledger. This attachment from the supplemental response is included in Exhibit SEF-26.

³⁰ O’Connell, Exh. ECO-1CT at 19:10-12.

1 **Q. What is the amount of unreimbursed cost that is being referred to in the**
2 **November 1995 letter?**

3 A. Based on information included in Ms. O’Connell’s own exhibits, the amount of
4 unreimbursed costs referenced in the November 1995 letter is approximately \$27
5 million, which takes into account the earlier recovery of over \$7 million in pre-
6 trial settlements.

7 **Q. Was this information available to Ms. O’Connell?**

8 A. Yes. Ms. O’Connell does not mention the \$7.6 million of recoveries received
9 from pre-trial defendants that are also applicable to Tacoma Tar Pits, which are
10 shown in her exhibit.³¹ When properly taken into consideration, the \$7.6 million
11 of settlements funds from the pre-trial defendants along with the \$29 million of
12 settlement funds from the post-trial defendants, totals \$36.6 million. This does in
13 fact substantially cover the roughly \$34 million of deferred remediation costs that
14 would have existed at that time. Table 3 depicts this as follows:

³¹ O’Connell, Exh. ECO-14 at 2 (referring to the sum of all amounts listed above the \$29 million).

**Table 3. Comparison of Tacoma Tar Pits
Unreimbursed Costs to Final Settlement**

<u>Description</u>	<u>in millions</u>
Likely balance of remedial costs for Tacoma Tar Pits at time of final settlement (from page 14 of Exhibit SEF-26)	\$ 34.3
Less: Settlement funds received from pre-trial defendants (from page 2 of Exhibit ECO-14)	<u>(7.60)</u>
Unreimbursed Costs	<u>\$ 26.7</u>
Final Settlement	<u>\$ 29.0</u>

1 **Q. Do you have any other reason to believe that the unreimbursed costs**
2 **referenced in the November 1995 letter were \$27 million?**

3 A. Yes. PSE has a copy of the September 1994 quarterly report that provides some
4 additional information on the status of Tacoma Tar Pits leading up to the final
5 settlement. I have included a copy of the report and transmittal letter in Exhibit
6 SEF-27, wherein PSE reports:

7 The current clean up cost estimate, less recoveries from insurance
8 settlements and third parties, totals \$27 million. This amount does
9 not include attorney fees incurred in the insurance litigation nor
10 interest.

11 Therefore, it is clear, that the \$7.6 million in pre-trial settlement funds was
12 considered when determining the amount of unreimbursed costs referenced in the
13 November 1995 letter. Doing so results in \$29 million of recoveries in
14 comparison to \$27 million (not \$34 million) of unreimbursed costs.

1 **Q. Are there any other reasons PSE continued to carry the Tacoma Tar Pits**
2 **deferred costs on its books separately from the recoveries?**

3 A. Yes. As described in Mr. Secrist's prefiled rebuttal testimony, PSE carries
4 deferred costs separately from its recoveries because, for most of the insurance
5 recoveries it received, the recoveries were not assigned to a particular site. In
6 addition, for many of its remediation sites, the costs for completing the
7 remediation are unknown and therefore allocation would be premature. For
8 example, although PSE anticipated that the Tar Pits site remediation was nearly
9 complete in 1998, the EPA directed PSE to address benzene concentrations in
10 groundwater that exceeded the Record of Decision cleanup criteria at the Tacoma
11 Tar Pits site. PSE was required to install a groundwater capture and treatment
12 system As a result, this EPA required action has required PSE to incur additional
13 remediation costs from the operation, maintenance and monitoring of this system
14 since that time. This is particularly important in insurance litigation because
15 prematurely declaring a site as complete could impair PSE's ability to fully
16 recover from its insurers if future costs turn out to be greater than previously
17 believed. By not allocating recoveries until cleanup costs are fully known, it
18 preserves PSE's ability to fully recover from insurers.

1 **Q. Should the Commission accept parties position to pass back 100 percent of**
2 **the unassigned proceeds to customers now or accept Commission Staff's**
3 **position to write-off net cost of the Tacoma Tar Pits project?**

4 A. No. For all of the reasons stated above, the Commission should reject these
5 positions.

6 **Q. Ms. O'Connell recommends disallowance of approximately \$200,000 for**
7 **certain internal employee costs that were netted against the unassigned**
8 **insurance recoveries account.³² Do you agree with her recommendation?**

9 A. Yes. I agree that the Commission orders were clear that there should not have
10 been internal employee costs charged to the remediation deferrals. Therefore, PSE
11 has accepted Ms. O'Connell's recommendation and has made this adjustment in
12 this rebuttal filing.

13 **Q. Do you agree with Ms. O'Connell's recommendation to treat PSE's net**
14 **deferred costs for gas environmental deferrals as working capital for**
15 **ratemaking purposes?³³**

16 A. Yes. I appreciate Ms. O'Connell's recognition that circumstances have changed
17 since WNG lost the ability to treat its gas net environmental deferrals as working
18 capital in Docket UG-920840 and for the reasons she states in her testimony, I
19 agree that it is appropriate to now include these accounts in working capital,

³² O'Connell, Exh. ECO-1CT at 21:1-12.

³³ *Id.* at 22:5 -23:2.

1 which is consistent with the treatment of PSE's electric net environmental
2 deferrals. Therefore, as is discussed in more detail in the working capital section
3 below, I have incorporated this change into this rebuttal filing.

4 **Q. Do you agree with Ms. O'Connell's calculation of the working capital**
5 **treatment?**³⁴

6 A. No. Every general rate case adjustment contains a potential impact on working
7 capital, but it is not appropriate to make adjustments to working capital for the
8 pacts of rate case adjustments. It is worthy of noting that Mr. McGuire and Mr.
9 Hancock did not propose adjustments to working capital for the Colstrip 1 and 2
10 regulatory asset or the placement of PSE's Hydro Treasury Grants in an interest
11 bearing account both of which represent changes to PSE's net utility plant in
12 service in rate base to non-operating items. I presume that is because they
13 understand that it is not appropriate to make adjustments to working capital for
14 the impacts of rate case adjustments. For instance, the change to revenues for the
15 temperature normalization adjustment would presumably also change PSE's
16 balance of customer accounts receivable, a working capital item. Even the general
17 rate case surplus or deficiency granted in a rate case could also be construed to
18 require an adjustment to working capital for the change that would occur to
19 retained earnings within average invested capital. However, the Commission does
20 not require that an adjustment be made to a utility's working capital for any of
21 these items as it would be overly complicated and unnecessary. Also, the

³⁴ O'Connell, Exh. ECO-1CT at 23:4-17.

1 additional net revenue PSE will receive in rates from this case to cover the net
2 amortization expense that Ms. O'Connell is using to adjust working capital would
3 also have an impact on working capital that Ms. O'Connell did not consider in her
4 proposed adjustment. In fact, all things being equal, the impact is directly
5 offsetting to Ms. O'Connell's adjustment because the additional revenue would
6 increase accounts receivable or cash balances, both of which are in working
7 capital. Accordingly, because the impacts on working capital of the additional
8 revenue and the additional amortization are offsetting, there is no need for an
9 adjustment. It is this type of example that justifies why there is a long-standing
10 tradition to not make adjustments to working capital and for these reasons, the
11 Commission should reject Ms. O'Connell's proposal to make a pro forma
12 adjustment to working capital related to rate year environmental remediation
13 amortization.

14 **Q. Do you agree with Ms. O'Connell's recommendations for improving the**
15 **quarterly reporting for PSE's environmental remediation program?**³⁵

16 A. I generally agree. However, PSE proposes to change Ms. O'Connell's
17 recommendation 1) (f), which would require PSE to reduce the balance of
18 corresponding project costs with recoveries it receives. PSE continues to believe
19 that directly reducing deferred project costs with recoveries decreases PSE's
20 ability to achieve optimal benefits for customers. Being able to present multiple
21 projects without assigning direct recovery to each project is important as PSE

³⁵ *Id.* at 24 and 25.

1 pursues insurance recoveries as Mr. Secrist discusses in his rebuttal testimony.
2 Reporting of these recoveries can continue to be done at the aggregate level and
3 determination of application of proceeds can be done in the rate proceeding in
4 which the net deferrals are requested for recovery following the process I outlined
5 earlier in my testimony and in my Exhibit SEF-23. Aside from that requested
6 change to Ms. O'Connell's recommendations, PSE can work with Commission
7 Staff to determine the format of the reports that they would like to see that would
8 presumably follow the guidelines outlined in Ms. O'Connell's testimony.

9 **Q. Please explain the differences between PSE's supplemental filing and**
10 **rebuttal filing.**

11 A. Since its supplemental filing, PSE has updated its estimates of the future costs for
12 PSE's environmental remediation sites, based on consultant's recommendations.
13 Therefore, as discussed on page 25 of my prefiled direct testimony, PSE has
14 updated these estimated future costs to the current estimates for this adjustment.
15 Additionally, during preparation of PSE's Response to ICNU Data Request
16 No. 55, it was discovered that when classifying sites for the future cost estimates,
17 the *City of Olympia v. PSE* environmental remediation site was categorized as gas
18 when it should have been categorized as electric. PSE has made this correction in
19 its rebuttal filing.

20 Also in the original filing, PSE had applied insurance recoveries of \$92,940
21 directly to the *City of Olympia v. PSE* Plum St. Station as if it were a third party
22 reimbursement. This amount is more appropriately included in the unapplied

1 insurance recoveries. PSE has also made this correction in this rebuttal filing to be
2 consistent with Ms. O'Connell's treatment of these proceeds.

3 As discussed above, PSE has accepted Commission Staff's recommendation to
4 remove internal employee costs that were booked to offset insurance recoveries in
5 the amount of \$209,796.52 for Tacoma Tar Pits and \$366.95 for Gas Works Park.

6 The impact of making these adjustments results in a decrease in net operating
7 income of \$925,460 for electric and \$5,592,128 for natural gas operations.

8 **G. Working Capital, Adjustment KJB-20.23 and SEF-15.23**

9 **Q. Have you reviewed the working capital calculation prepared by Commission
10 Staff?**

11 A. Yes. Commission Staff utilizes the Investor Supplied Working Capital method
12 ("ISWC"), sometimes referred to as the Balance Sheet approach, which is the
13 same method used by PSE. My understanding of this method is that it calculates
14 working capital by determining how much of PSE's capital ("Average Invested
15 Capital") has been invested in operating and non-operating activities ("Total
16 Average Investments"), and the remainder, if positive, is the amount of working
17 capital experienced by PSE during the test year. This working capital is then
18 allocated between the portion that is required by the utility business (which is split
19 between electric and gas) and the portion that is required by non-utility
20 operations. The portion allocated to utility operations is known as Investor

1 Supplied Working Capital. The electric and gas ISWC is then added to the electric
2 and gas rate base, respectively.

3 **Q. What is another way to think about how to determine ISWC?**

4 A. Fundamentally, Average Invested Capital is either invested in Total Average
5 Investments or in Working Capital. Working Capital is allocated between Utility
6 (electric and gas) and Non-Utility Operations based on the ratio of how Total
7 Average Investments (less Construction Work in Progress or “CWIP”) breaks
8 down between Operating (electric and gas) and Non-Operating.

9 Because the ISWC approach is a balance sheet approach, it can also be thought of
10 as a specific list of balance sheet accounts that total up to working capital. This
11 total is then allocated to electric and gas ISWC or non-utility working capital
12 based on the portion of electric and gas operating and non-operating investment
13 (excluding CWIP) to total investment (excluding CWIP). Working capital plus
14 total investment ties back to PSE’s capital available for investment.

15 And because it is a balanced approach, all of a Company’s balance sheet accounts
16 are included in one of these three categories – Average Invested Capital, Total
17 Average Investments, or Working Capital.

18 **Q. Please further explain each of the three categories.**

19 A. The following provides a more detailed description of each of the three
20 categories:

1
2
3
4
5
6
7
8
9
10
11
12
13
14
15
16
17
18
19
20
21

Average Invested Capital

Average Invested Capital is made up of the funds available for investment and is comprised of all of the balance sheet accounts related to a company’s capital – in other words its debt and equity accounts.

Total Average Investment

Total Average Investment is the amount of the Average Invested Capital that has been invested in items other than working capital and is comprised of all of the balance sheet accounts that are not included in working capital or Average Invested Capital. It is further broken down into three subcategories:

Operating Investment

Operating Investment is made up of investments made in the utility business. In PSE’s presentation in its original filing, this subcategory contained all of PSE’s balance sheet accounts that are included in its electric and gas rate base as well as other accounts that are utility related but that are not in rate base or working capital and do not earn or pay interest. In Commission Staff’s presentation in their response filing, this subcategory only contains the accounts that are included in electric and gas rate base.

Non-Operating Investment

Non-Operating Investment is made up of investment made in non-utility operations, items that specifically earn or pay interest, or items that are not

1 allowed for rate making purposes. Commission Staff's presentation in its
2 response testimony includes CWIP accounts in Non-Operating, while
3 PSE's presentation does not, the reason for which is explained below.

4 **Construction Work in Progress**

5 Since PSE began consistently using the investor supplied working capital
6 calculation in the early 1980s, CWIP accounts have been held separate
7 from Operating and Non-Operating investment when determining the
8 ratios used to allocate working capital. However, Commission Staff's
9 presentation includes CWIP accounts in non-operating for purposes of
10 allocating work capital.

11 **Working Capital**

12 In the aggregate, Working Capital is the difference between Average Invested
13 Capital and Total Average Investments. At a detailed level, it is comprised of
14 balance sheet accounts that are allowed for ratemaking purposes but that are not
15 afforded a separate return through rate base and on which PSE does not earn or
16 pay interest.

17 **Q. Have you prepared an exhibit detailing PSE's proposed working capital for**
18 **this rebuttal filing?**

19 **A.** Yes. I have adopted Ms. Erdahl's proposed presentation and have utilized her
20 format in preparing my updated exhibits. I will detail the changes that have been
21 made between PSE's original and rebuttal filings for working capital and provide

1 a summary for the differences I am aware of between PSE's rebuttal position and
2 Commission Staff's response position as detailed in Commission Staff's
3 Response to PSE Data Request No. 28 that is included in Exhibit SEF-19. Please
4 see Exhibit SEF-28 and SEF-29 for PSE's revised summarized and detailed
5 working capital calculation and the resulting adjustment to the test period that
6 were included in the original filing.

7 **Q. Please describe the fundamental differences between PSE and Commission**
8 **Staff related to working capital.**

9 A. Based on this rebuttal filing and the amounts reflected in Exhibit SEF-19, there
10 remain only two fundamental differences between PSE and Commission Staff on
11 working capital:

12 **1. Account categorization**

13 As mentioned above, Commission Staff argues that there should be no Operating
14 subsection in the Total Average Investments category. In its rebuttal filing, PSE
15 has agreed with this approach. Between PSE's adoption of (i) many of the
16 changes in account treatment that were originally proposed by Commission Staff,
17 (ii) account re-categorizations made by PSE at rebuttal, and (iii) the account re-
18 categorizations made by Commission Staff reflected in Exhibit SEF-19, PSE and
19 Commission Staff are now in alignment related to the working capital treatment
20 for all accounts except three categories.

21 PSE disagrees with all of the below adjustments proposed by Commission Staff
22 for reasons stated earlier and stated by Ms. Barnard in her prefiled rebuttal

1 testimony. However, if the Commission were to accept Commission Staff's
2 adjustments, the following corrections must be considered.

- 3 a. Tacoma Tar Pits accounts – Commission Staff is treating the
4 portion of the Tacoma Tar Pits accounts that it recommends be
5 written off as non-operating investment. PSE treats these amounts
6 as working capital. I discuss more fully below why, given their
7 proposal, Commission Staff's proposed treatment of these balances
8 as non-operating investment is incorrect.
- 9 b. PSE disagrees with the manner in which Commission Staff has
10 adjusted the working capital calculation for its proposed treatment
11 for PSE's storm deferral mechanism. I discuss more fully below
12 why, given the proposal, Commission Staff's proposed treatment
13 of the rate year end of period balances being removed 100 percent
14 from electric working capital is incorrect.
- 15 c. PSE disagrees with the manner in which Commission Staff has
16 made a pro forma adjustment to working capital calculation for its
17 proposed rate year amortization of the environmental deferral
18 accounts. I discuss more fully below why, given its proposal,
19 Commission Staff's proposed pro forma adjustment is
20 inappropriate. If it were to be accepted, it requires a correction to
21 the way in which the working capital adjustment is applied.

22 **2. Calculation of working capital ratios.**

23 For purposes of calculating the working capital ratios, Commission Staff assigns
24 CWIP to non-operating investment, which results in an increase to the portion of
25 working capital assigned to non-utility business. Using the method that can be
26 traced back at least thirty years, PSE removes CWIP from the calculation of the
27 working capital ratios.

1 **Q. Can you please further explain how Commission Staff and PSE differ on**
2 **their treatment of CWIP?**

3 A. Yes. Commission Staff believes that CWIP should be considered as non-operating
4 investment for purposes of calculating the working capital ratios (“allocation
5 calculation”) because it is not used and useful, and it accrues a return through the
6 allowance of funds used during construction (“AFUDC”) calculation.³⁶
7 Commission Staff also states that other Washington utilities treat it this way.
8 While this may be true for some companies, Avista Corporation calculates its
9 allocation of working capital in the same manner as PSE, which is to exclude
10 CWIP from the calculation.³⁷

11 **Q. Why does PSE not include CWIP in the working capital allocation**
12 **calculation?**

13 A. PSE’s exclusion of CWIP in the working capital allocation calculation stems from
14 Cause 83-54.³⁸ In that case, Commission Staff witness Merton Lott recommended
15 this approach in his investor supplied working capital calculation. PSE at that

³⁶ Commission Staff provides their reasoning for including CWIP in the allocation calculation in their Response to PSE Data Request No. 11 which is provided as Exhibit SEF-30.

³⁷ PSE agrees with Commission Staff that there is no express Commission order on this issue, but notes that pages 111 and 79 of Avista’s Electric and Gas Commission Basis Reports in Dockets UE-170325 and UG-170326 show that Avista does not include CWIP in its allocation calculation.

³⁸ Testimony of Merton Lott, WUTC Accounting Analyst, June 1984 at page 13, beginning on Line 6. “It should be noted that I have proposed a slightly different method of allocating working capital than was accepted by the Commission in Cause U-81-41, a prior Puget case. In that case, working capital was allocated to all investments including CWIP. The major reason I excluded CWIP from the allocation process is that I do not believe that construction activities would tend to have positive working capital related to them.” Accepted in the Fourth Supplemental Order in that Cause at page 17, without endorsement.

1 time had filed a lead lag study. Without expressly commenting on the allocation
2 calculation, the Commission's order in that case accepted Commission Staff's
3 investor supplied working capital over PSE's lead lag study.

4 **Q. Does PSE earn AFUDC on all of its CWIP?**

5 A. No. Certain construction projects are short lived and so are not eligible for CWIP.
6 This means roughly 20 percent of PSE's CWIP does not earn AFUDC.

7 **Q. Do you think it is appropriate to exclude CWIP from the working capital
8 allocation calculation?**

9 A. Yes. CWIP is different than most other accounts because it will eventually be
10 included in PSE's rate base investments as plant in service and is clearly related to
11 utility business. Additionally, it does not all earn AFUDC. Finally, Commission
12 Staff has previously provided this method for excluding it from the allocation
13 calculation in order to recognize the uniqueness of CWIP. For these reasons, the
14 Commission should not change the long-standing method that PSE has followed.

15 **Q. Did you find any errors when reviewing the way Commission Staff included
16 its working capital adjustments in the determination of its revenue
17 requirement?**

18 A. Yes. I found two errors when reviewing Commission Staff's adjustments as
19 presented in Exhibit SEF-19.

1 **Working Capital adjustment for storm and pro forma environmental**
2 **remediation amortization**

3 Mr. Thomas E. Schooley proposes an inappropriate adjustment to working capital
4 and includes his adjustment without following Ms. Erdahl’s recommended
5 working capital allocations between electric, gas and non-utility. In her rebuttal
6 testimony, Ms. Katherine J. Barnard addresses why Mr. Schooley’s storm
7 adjustment, as well as his adjustment to working capital for storm, is
8 inappropriate. However, if the Commission were to decide in favor of this
9 working capital adjustment, there are errors in the way it has been used to adjust
10 the working capital and the revenue requirement in the exhibits of Ms. Melissa C.
11 Cheesman. First, the balances Mr. Schooley uses to adjust working capital are not
12 the same balances that are included in the original working capital calculation.
13 The test year average of monthly averages (“AMA”) balances of the storm
14 deferrals should be used to calculate the adjustment to working capital.
15 Additionally, the amount of working capital that would be adjusted must be
16 allocated to electric, gas and non-utility following the ending working capital
17 ratios that result from the Commission’s decisions related to the contested items
18 in the working capital adjustment as discussed in this section. This allocation
19 should also be followed if Ms. O’Connell’s adjustment is accepted. I have
20 included Exhibit SEF-31, which includes Commission Staff’s Response to PSE
21 Data Request Nos. 8 and 14 and provides Commission Staff’s confirmation that
22 an alternative way, different from the way their adjustment was made, may be
23 more appropriate. Page 3 of Exhibit 31 shows the working capital adjustment for

1 Storm as recommended by Commission Staff and shows the correct way to
2 calculate the adjustment to working capital if the Commission were to accept Mr.
3 Schooley's adjustment. Ultimately, the working capital ratios shown in Column
4 (d) on page 3 of Exhibit SEF-31 need to be applied to the balances being written
5 off and removed from working capital. Although PSE does not agree with Ms.
6 O'Connell's pro forma adjustment to working capital discussed in section IV.F.
7 above, if the Commission were to accept it, the working capital ratios would also
8 have to be applied to the amount of the total working capital adjustment before
9 removing the adjustment from electric and gas working capital.

10 **Treatment of the recommended write-off of Tacoma Tar Pits deferral**

11 I discuss above in section IV.F. why the Commission should not accept
12 Commission Staff's recommendation to write off deferred costs for the Tacoma
13 Tar Pits deferral. However, if the Commission were to accept the
14 recommendation, Commission Staff's adjustment to working capital for this item
15 requires correction. Ms. Erdahl leaves the balances that are being recommended
16 for disallowance in non-operating investments.³⁹ It is inappropriate to have
17 balances that are recommended for a write off included in non-operating
18 investment. Doing so will create a higher working capital ratio for non-operating
19 than is appropriate. Therefore, if Ms. O'Connell's adjustment to the Tacoma Tar
20 Pits deferral is accepted, two things in the way that Commission Staff has

³⁹ See Free, Exh. SEF-19 at 12:1147 (columns (g) and (j)); see *id.* at 15:1152 (columns (g) and (j)); see *id.* at 29:2338 (columns (g) and (j)).

1 presented the working capital impacts would need to change. First, 100 percent of
2 the test year AMA balances of the subject accounts should be treated as working
3 capital in the working capital exhibit. Second, a working capital adjustment
4 should be made outside of the working capital exhibit in the same manner as
5 discussed above and demonstrated on page 3 of Exhibit SEF-31 wherein the final
6 working capital ratios from the working capital exhibit would be applied to the
7 amount of the environmental remediation write-off before using it to adjust the
8 electric and gas working capital.

9 **Q. Please summarize your position on working capital.**

10 A. I believe that PSE and Commission Staff are close in their proposals on working
11 capital with the clarification of Commission Staff's position in SEF-19. When
12 comparing PSE's calculation of working capital in Exhibit SEF-28 to
13 Commission Staff's determination of working capital in Exhibit SEF-19, there are
14 truly very few fundamental differences. Considering how far apart the respective
15 working capital adjustments were originally, this is quite encouraging. However,
16 there still remain a few fundamental differences between PSE and Commission
17 Staff on working capital, and for the reasons stated above, the Commission should
18 accept PSE's calculation of the adjustment.

1 **H. Liquefied Natural Gas (“LNG”) and Leasing Costs, Commission Staff**
2 **Adjustment 13.24E and 11.24G**

3 **1. Leasing Costs:**

4 **Q. How do you respond to Commission Staff’s recommendation that legal costs**
5 **associated with the Leasing Program in Dockets UE-151871/UG-151872**
6 **should be excluded?⁴⁰**

7 A. Regulatory proceedings by their very nature can be unpredictable and if utilities
8 are not allowed to recover their legal costs associated with these types of
9 adjudicated proceedings, it would impair their ability to adequately protect their
10 legal interests and would have a chilling effect on a utility’s willingness to
11 propose new services. Moreover, as I discuss in more detail below, the
12 Commission ruled in PSE’s favor on several important issues that were contested
13 by Commission Staff in the leasing case and reaffirmed that leasing of equipment
14 can be a tariffed service. As discussed in more detail below, in light of the
15 Commission’s determinations on these contested issues, the costs for PSE’s
16 proposed new leasing tariff should not be disallowed.

17 **Q. What is the basis for Commission Staff’s belief that legal costs associated**
18 **with the Leasing Program should be excluded?**

19 A. Ms. O’Connell supports her recommendation solely on the basis that the
20 Commission determined that the terms and conditions of the Leasing Program
21 were not fair, just, and reasonable and that the proposed Leasing Program was not

⁴⁰ See generally O’Connell, Exh. ECO-1CT.

1 in the public interest.⁴¹ She provides no other reason for disallowing the legal
2 costs associated with the adjudicated proceeding and cites no authority for her
3 proposal.

4 **Q. Is this an accurate summary of the Commission's final order?**

5 A. No. Ms. O'Connell only discusses part of the Commission's final order and
6 ignores the history and context of the proposed Leasing Program.

7 **Q. Why is the history and context of the Leasing Program relevant?**

8 A. As explained in the Prefiled Rebuttal Testimony of Mr. William T. Einstein,
9 Exhibit WTE-1T, PSE and its predecessors have been renting equipment for over
10 fifty years and the legal precedent for doing so is well established by the
11 Commission. In fact, in the Commission's Leasing Order, the Commission
12 affirmed the statutory authority of utilities to lease equipment, despite arguments
13 to the contrary by Commission Staff.⁴² Therefore, there was significant legal
14 precedent for PSE to propose an equipment leasing program and it was a
15 reasonable business decision for PSE to pursue.

16 **Q. What was the Commission's final order regarding the Leasing Program?**

17 A. Despite the Commission's rejection of the leasing tariff in that docket, the
18 Commission made several rulings that were in PSE's favor, holding that PSE's

⁴¹ O'Connell, Exh. ECO-1CT at 5:18-21.

⁴² Leasing Order, ¶¶ 61-73.

1 proposal was a permissible regulatory service, including several that were
2 contrary to Commission Staff's position:

- 3 1. A water heating and HVAC equipment leasing program can
4 be a tariffed utility service subject to Commission
5 jurisdiction.⁴³
- 6 2. Washington utilities are required to develop creative, cost-
7 effective methods to reduce consumption of both electricity
8 and natural gas.⁴⁴
- 9 3. PSE's proposed Leasing Program's purpose and goals
10 satisfied state policy goals for reducing consumption and
11 that there could be an equipment leasing program that
12 encourages conservation.⁴⁵
- 13 4. PSE's proposed Leasing Program satisfied factors the
14 Commission considers to evaluate whether a service is
15 subject to Commission regulation, including whether the
16 service is being offered to the public, the company's market
17 power, and the need for consumer protection.⁴⁶
- 18 5. The service was appropriate under RCW 80.04.270.⁴⁷
- 19 6. The record demonstrated consumer demand for a service
20 that facilitates replacing aging water heating and HVAC
21 equipment with more efficient products.⁴⁸ Indeed, the
22 Commission noted that the fact that 33,000 PSE customers
23 still elect PSE's existing rental service demonstrates "real
24 world" evidence that customers are still interested in a
25 leasing service.⁴⁹

⁴³ Leasing Order at ¶ 61.

⁴⁴ *Id.* at ¶ 62

⁴⁵ *Id.* at ¶ 63

⁴⁶ *Id.* at ¶¶ 67-70.

⁴⁷ *Id.* ¶ 72.

⁴⁸ *Id.* at ¶ 83.

⁴⁹ *Id.* at ¶¶ 84-85.

1 **Q. Did the Commission reject Commission Staff's positions?**

2 A. Yes, the Commission disagreed with certain of Commission Staff's arguments,
3 including positions taken by Ms. O'Connell, including:

4 1. The customer's meter is not the demarcation line for
5 determining regulatory service and Commission Staff's
6 position otherwise was unsupported in statute or
7 Commission precedent and would harm public policy.⁵⁰

8 2. Commission Staff's standard of review was too
9 constraining when assessing whether a proposed program is
10 subject to Commission regulation.⁵¹

11 **Q. If the program was ultimately not approved, why should the legal costs for
12 the proposed program be allowed?**

13 A. As discussed earlier in my testimony, disallowing legal costs simply because the
14 tariff was not approved would set poor precedent. Additionally, the Commission
15 should review the totality of the record. Ms. O'Connell glosses over the fact that
16 PSE prevailed on several issues that Commission Staff challenged, including that
17 leasing of equipment such as water heaters falls within the jurisdiction of the
18 Commission. PSE was required to expend significant legal expenses to defend its
19 position on these issues and ultimately prevailed on several issues. If utilities are
20 not allowed to recover their legal costs associated with adjudicated proceedings
21 before the Commission, this would impair the ability of utilities to adequately
22 protect their legal interests and also provides a disincentive for utilities to propose
23 new measures before the Commission because if they are not adopted, under

⁵⁰ *Id.* at ¶ 64.

⁵¹ *Id.* at ¶ 65.

1 Commission Staff's theory, PSE would be unable to recover those costs. Such a
2 proposal would harm utilities and ratepayers and should therefore be rejected.

3 **2. LNG Costs:**

4 **Q. Does PSE agree with Ms. O'Connell's suggestion that a portion of the legal**
5 **costs associated with the LNG project should be excluded?**

6 A. No. Ms. O'Connell cites no authority for her suggestion that a portion of the LNG
7 legal costs should be excluded. The LNG project is a prime example of a program
8 proposed by PSE before the Commission that resulted in a complex and lengthy
9 procedural process that required PSE to incur legal costs. The fact that the final
10 settlement resulted in an operational structure where a portion of the LNG
11 business was unregulated should in no way suggest that a portion of the legal
12 costs that led to settlement should be excluded, especially since the structure of
13 the LNG project took months to settle. PSE had no way of knowing at the outset
14 of the case what the final result would be.

15 **Q. Does Ms. O'Connell provide any basis for her apportionment methodology?**

16 A. No. Ms. O'Connell simply argues that the Commission should apportion the legal
17 costs based on the final agreed allocation between the regulated and unregulated
18 sides of the LNG plant. Ms. O'Connell's reasoning is flawed for two reasons.
19 First, the entire settlement required Commission review and approval, even
20 though a portion of the final settlement included an unregulated entity. In fact,
21 Ms. O'Connell even admits that Commission approval was necessary in order to

1 allow the creation of the unregulated entity.⁵² Thus, PSE was required to expend
2 those costs, even though ultimately it was determined that an unregulated entity
3 would be a part owner of the LNG plant. Second, there is no evidence that the
4 final apportionment between the regulated and non-regulated businesses has a
5 direct relationship between the legal costs that were expended on each entity in
6 the case, and Ms. O’Connell has not provided any evidence to demonstrate this is
7 the case. An unregulated business would not require these costs in order to begin
8 operations. Therefore, a direct assignment of these costs to the regulated entity is
9 most appropriate.

10 **Q. Should any of the legal costs for the LNG project be excluded?**

11 A. No. As explained above, utilities must be able to propose new projects before the
12 Commission without the fear that all or a portion of the legal fees will be
13 excluded.

14 **I. Greenwood Incident, NWIGU Adjustment IN-5**

15 **Q. Does PSE agree with NWIGU witness Mullins’s summary of the Greenwood
16 incident and that “the Company admitted to violating both state and federal
17 pipeline safety regulations?”⁵³**

18 A. No. Mr. Mullins oversimplifies the issue. As explained in the Settlement
19 Agreement and supporting narrative between PSE and Commission Staff in

⁵² O’Connell, Exh. ECO-1CT at 32:12-18.

⁵³ Mullins BGM-1CTr at 44:11.

1 Docket PG-160924, Commission Staff’s investigation concluded that the
2 Greenwood Service Line pipe involved in the incident was structurally sound and
3 the immediate cause of the incident was external damage caused by unauthorized
4 human activity of trespassers. PSE believed the service line had been properly cut
5 and capped by its contractor when in fact it was not. PSE did not contest that
6 violations occurred and, importantly, acknowledged responsibility for its
7 contractors under WAC 480-93-007. PSE did not admit to violating the pipeline
8 safety regulations, but agreed to the Settlement terms to avoid further expense,
9 inconvenience, uncertainty and delay. Both parties recognize that this Agreement
10 represents a compromise of the parties’ positions.

11 **Q. Does PSE agree with Mr. Mullins’ belief that PSE should have treated the**
12 **\$3.2 million⁵⁴ in penalties outlined in the Settlement Agreement as a restating**
13 **adjustment rather than recording it below-the-line?⁵⁵**

14 A. No. The Code of Federal Regulations (“CFR”)⁵⁶ requires utilities to record
15 penalties below the line. FERC Account 426.3 “Penalties,” states:

16 This account shall include payments by the company for penalties
17 or fines for violation of any regulatory statute by the company or
18 its officials.

19 Mr. Mullins’ statement that he is troubled by the below-the-line adjustment
20 because it is not documented or explained is nonsensical. Documentation

⁵⁴ Mullins, Exh. BGM-1CT at page 45:13-15.

⁵⁵ O’Connell, Exh. ECO-1CT at 5:18-21.

⁵⁶ Title 18, Chapter 1, Subchapter C, Part 101.

1 detailing the penalty is provided in the settlement agreement between PSE and the
2 Commission in Docket PG-160924. Were PSE to have recorded this entry the
3 way Mr. Mullins suggests, PSE would be in violation of FERC accounting rules.
4 Additionally, discovery procedures are in place so that interested parties can
5 review PSE's records, including below-the-line entries.

6 **Q. Does PSE agree with witness Mullins' suggestion that \$0.4 million of**
7 **expenditures related to the incident should be excluded?**⁵⁷

8 A. No. The \$366,348 Mr. Mullins is referring to includes costs incurred as part of
9 PSE's response to the gas emergency and the ensuing investigation into the cause
10 as required by state and federal regulations. The total includes costs for the initial
11 response to the reported gas odor, the control of gas to the affected area,
12 restoration of service to customers surrounding the scene, and debris removal and
13 site restoration following the lengthy investigation conducted by PSE and pipeline
14 safety engineers from the Commission. Due to the unique circumstances of this
15 event and the impact to the structures, a significant environmental safety protocol
16 was put in place to protect the workers and the public from airborne contaminants.
17 This extended the time to conduct the investigation.

18 In the settlement, PSE agreed to the monetary penalty of \$2.75 million along with
19 implementation of a Deactivated Gas Line Inspection and Remediation Program,
20 for its part in the Greenwood incident. PSE should not be further penalized for its

⁵⁷ Mullins BGM-1CT at 45:21-23.

1 efforts in response to the reported gas leak and the following investigation into its
2 cause. Accordingly, the Commission should not approve Mr. Mullins'
3 recommended adjustment.

4 **V. CHANGES BY PSE AT REBUTTAL**

5 **Q. PSE had identified adjustments that it would update over the course of the**
6 **proceeding. Has PSE made these updates?**

7 A. No. When PSE made its initial filing it recognized that a number of adjustments
8 could require updating as better information became available over the course of
9 the proceeding. The adjustments for which PSE originally contemplated updates,
10 but that have not changed, are the Property and Liability Insurance Adjustment
11 20.14E and 15.14G, Employee Insurance Adjustment 20.18E and 15.18G and
12 South King Service Center Adjustment 20.21E and 15.21G. All of these
13 adjustments are uncontested and considering the materiality thresholds utilized by
14 Commission Staff, none of the updates originally anticipated by PSE are
15 materially different from the adjustments included in PSE's supplemental filing.
16 Therefore PSE has not proposed updates for these adjustments in this rebuttal
17 filing.

1
2
3
4
5
6
7
8
9
10
11
12

**VI. MATERIALITY AND OTHER
NON-REVENUE REQUIREMENT ISSUES**

Q. How does PSE respond to Commission Staff's proposals related to materiality thresholds and clearer communication?

A. Please see the Prefiled Rebuttal Testimony of Ms. Katherine J. Barnard, Exhibit KJB-17T, for a discussion of PSE's response to issues addressed by Commission Staff related to materiality including whether there is still a need for certain minor rate case adjustments as well as issues raised by Commission Staff related to clearer communication.

VII. CONCLUSION

Q. Does this conclude your testimony?

A. Yes it does.