Exh. CRM-1T
Docket UG-200568
Witness: Chris R. McGuire

BEFORE THE WASHINGTON
UTILITIES AND TRANSPORTATION COMMISSION

WASHINGTON UTILITIES AND TRANSPORTATION COMMISSION, **Complainant,** **v.** **CASCADE NATURAL GAS CORPORATION,** **Respondent.**	**DOCKET UG-200568**

TESTIMONY OF

Chris R. McGuire

STAFF OF
WASHINGTON UTILITIES AND
TRANSPORTATION COMMISSION

Overview of Staff's Case
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Policy Concerns Regarding Pro Forma Plant

November 19, 2020

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I. INTRODUCTION

Q. Please state your name and business address.

A. My name is Chris R. McGuire, and my business address is 621 Woodland Square Loop SE, Lacey, Washington, 98503. My business mailing address is P.O. Box 47250, Olympia, Washington, 98504-7250. My business email address is chris.mcguire@utc.wa.gov.

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

A. I work in the Regulatory Services Division of the Washington Utilities and Transportation Commission (Commission) as Assistant Director of Energy Regulation. I have worked at the Commission since May 2012, and in my current position since April 2018.

Q. Would you please state your educational and professional background?

A. I graduated from the University of Washington in 2002 with a Bachelor of Science degree in Cell and Molecular Biology. I graduated from the University of Colorado in 2010 with a Master of Business Administration and a Master of Science in Environmental Studies. Prior to my employment with the Commission, I held research positions at various institutions, including the University of Washington, the University of Colorado, and the National Renewable Energy Laboratory.

Q. Have you previously testified before the Commission?

A. Yes. I sponsored testimony on behalf of Commission Staff (Staff) in the following adjudicated proceedings: Pacific Power's 2013 general rate case (GRC), Docket UE-130043; Avista's 2014 GRC, Dockets UE-140188 and UG-140189; Avista's 2015 GRC (including the remand phase), Dockets UE-150204 and UG-150205; PSE's 2017 GRC, Dockets UE-170033 and UG-170034; Avista's 2017 GRC, Dockets UE-170485 and UG-170486; PSE's 2018 expedited rate filing, Dockets UE-180899 and UG-180900; Avista's 2019 GRC, Dockets UE-190334 and UG-190335; PSE's 2019 GRC, Dockets UE-190529 and UG-190530; and PSE's application for the sale of Colstrip Unit 4, Docket UE-200115.

II. SCOPE AND SUMMARY OF TESTIMONY

Q. What is the scope and purpose of your testimony?

A. The purpose of my testimony is to provide an overview of Staff's case. I introduce the witnesses sponsoring testimony on behalf of Staff, and I summarize Staff's recommendations and the basis for those recommendations. I also discuss policy concerns related to Cascade's request on pro forma plant.

Q. What is Staff's overall response to Cascade's request for additional revenues.

A. Staff is somewhat dismayed by Cascade's filing. As its customers continue to struggle due to the economic consequences of COVID-19, Cascade asks for a 5.3 percent rate increase a mere four months after the 2.8 percent rate increase from its just-concluded rate case went into effect,[1] even though those new rates were more than sufficient to cover the Company's costs. Cascade's restated test year (2019) rate of return (ROR) was 8.01 percent,[2] or 77 basis points above its currently authorized ROR of 7.24 percent.

What is even more incredible is what Cascade claims the increase is for. While Cascade purports a revenue deficiency of $12.0 million, that full amount (and then some) – or approximately $12.4 million[3] – is driven by (1) a requested increase in ROR, including a 90-basis point increase in return on equity (ROE) (from 9.4 percent to 10.3 percent), (2) $66.1 million in pro forma plant additions in 2020, nearly all of which failed to materialize, and (3) $1.0 million to fund another three percent wage increase for Cascade's employees for 2021, which would be the third consecutive year of such a wage increase.

Q. What has Staff concluded?

A. Cascade does not need a rate increase. The Company does not need a 90-basis point increase in ROE, it does not need rate payers to fund another three percent wage increase for its employees in 2021, and it has not invested in $66.1 million in new facilities, or anywhere near that amount. Cascade's request for a rate increase is driven almost entirely by non-existent and/or unnecessary costs, and its assertion that it is suffering a revenue deficiency lacks merit.

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[1] *Wash. Utils. & Transp. Comm'n v. Cascade Nat'l Gas Corp.*, Docket UG-190210, Order 05 (Feb. 3, 2020) (2019 Cascade GRC Order). *See* Exhibit A to Order 05, Joint Settlement Agreement, 2, ¶ 7.

[2] *See* Section IV.A., below. The calculation of restated ROR includes restating adjustments proposed by Cascade, including restating revenues to reflect the rate increase the Company implemented on March 1, 2020.

[3] This amount includes $8,964,076 for pro forma plant (*see* Hillstead, Exh. KMH-8 at 9) and $2,145,575 for Cascade's requested increase in ROE and equity percentage (applied to test year EOP rate base).

Q. Please summarize Staff's recommendations.

A. As Staff's case demonstrates, Cascade has a revenue *surplus* of $508,968.[4] Therefore, Staff recommends the Commission decrease Cascade's revenue by $508,968. The components of Staff's revenue requirement are summarized in Section IV.B., below.

Staff also recommends that the Commission require Cascade to complete a load study prior to filing its next general rate case. As described in the testimony of Staff witness Higby, after four and a half years, Cascade still has not complied with the Commission's order requiring the Company to initiate a load study.

Q. Why should the Commission not simply dismiss Cascade's case?

A. It certainly could. RCW 80.28.020 requires that the Commission first find the utility's current rates are insufficient before authorizing an increase. It is entirely possible – if not likely – that the Commission will be unable to make such a finding here, leaving the Commission without the legal basis to increase Cascade's rates. The Commission dismissed Avista's 2016 general rate case for this very reason.[5]

However, the Commission should not dismiss Cascade's case here. First, as Staff's case demonstrates, Cascade's current rates are *more than* sufficient to cover the Company's costs, which supports a finding that the Company's current rates are

[4] Hillstead, Exh. KMH-4, ln. 7.

[5] *Wash. Utils. & Transp. Comm'n v. Avista Corp.*, Dockets UE-160228 & UG-160229, Order 06, 34, ¶ 61 (Dec. 15, 2016) (Dismissing Avista's GRC because the company had "failed to carry its burden to show that its existing rates 'are unjust, unreasonable, [or] insufficient to yield a reasonable compensation for the service rendered.'").

unreasonable and unjust. Such a finding provides the legal imperative under RCW 80.28.020 for the Commission to *lower* Cascade's rates.

Second, the Commission should not simply dismiss Cascade's case (leaving Cascade's current rates unchanged) because doing so would send the signal to utilities that there is no downside risk to filing frivolous rate cases and that there are no repercussions for wasting the Commission's time with baseless requests for increased revenue. Simply dismissing the case sends the signal to utilities that the worst that can happen is a revenue change of $0 and, therefore, there is only upside to filing a rate case – no matter how unnecessary.

III. INTRODUCTION OF STAFF WITNESSES

Q. Please introduce the other Staff witnesses testifying in this proceeding and the subjects of their testimony.

A. The following witnesses present testimony and exhibits for Staff:

- Kristen Hillstead presents Staff's calculation of revenue requirement. Staff witness Hillstead also addresses the interest coordination adjustment (Adjustment P-1) and the adjustment reflecting the results of Staff's per-books audit (Adjustment UTC-1).
- Aimee Higby presents the rate spread and bill impact analysis for Staff's recommended revenue requirement. Staff witness Higby also addresses Cascade's use of forecasted 2020 billing determinants as well as the Company's lack of progress on initiating a load study.

- Joanna Huang addresses Cascade's pro forma wage adjustment, Adjustment P-2. Staff witness Huang contests Cascade's wage increase for 2021 as well as a portion of Cascade's wage increase for 2020.
- David Panco addresses Cascade's pro forma plant adjustment, Adjustment P-3. Staff witness Panco contests the projects Cascade includes in Adjustment P-3 that the Company has not (or will not) place in service in 2020.
- David Parcell addresses Cascade's cost of capital. Staff witness Parcell contests Cascade's requested cost of capital, including its requested capital structure and ROE.
- Amy White addresses Adjustment P-4 which is Cascade's adjustment for the amortization of deferral balances related to the Company's maximum allowable operating pressure (MAOP) pipeline investments. Staff witness White contests Cascade's shortening of the amortization period for certain of these investments.

IV. OVERVIEW OF STAFF'S CASE

A. Summary Of Cascade's Case

Q. Please summarize Cascade's request.

A. Cascade alleges a revenue deficiency of $12.0 million. While Cascade initially requested a revenue increase of $13.8 million,[6] which it later updated to $14.1 million,[7] Cascade produced a revised revenue requirement model in response to

[6] Peters, Exh MCP-2 – ROO Summary Sheet, Col. 4, ln. 4.
[7] Peters, Exh MCP-8 – ROO Summary Sheet, Col. 4, ln. 4.

discovery in which it updated the Company's depreciation rates[8] and corrected a calculation error in the model.[9] In this revised model, Cascade calculates a revenue requirement of $12.0 million.

Q. How does Cascade arrive at this revenue requirement?

A. Cascade relies on a modified historical test year approach with pro forma adjustments. Cascade begins with a test year of January 1, 2019, to December 31, 2019, and first modifies that test year by applying six restating adjustments (Adjustments R-1 through R-6). Of particular note, Cascade's restating adjustments restate the test year plant balances on an end-of-period (EOP) basis (Adjustment R-4) and restate test year revenues to reflect the rate increase that went into effect on March 1, 2020 (Adjustment R-3).[10]

Cascade then makes four pro forma adjustments (Adjustments P-1 through P-4) to its restated 2019 results of operations (ROO). These adjustments capture, among other things, what the Company claims are post-test year increases in employee wages (Adjustment P-2) and plant in service (Adjustment P-3).[11]

[8] Cascade filed an accounting petition requesting to update depreciation rates with the Commission in Docket UG-200278. In its updated model, the Company revised depreciation rates to align with its updated deprecation study (reflecting the terms of a settlement the Company reached with parties in Oregon).
[9] *See* Hillstead, Exh. KMH-8.
[10] Restating adjustments also pull CRM balances into base rates (Adjustment R-1), remove promotional advertising expenses (Adjustment R-2), annualize the test year 2019 wage increase (Adjustment R-5), and remove executive incentives (Adjustment R-6).
[11] Cascade's pro forma adjustments also include the interest coordination adjustment (Adjustment P-1) and amortize the MAOP deferral balance (Adjustment P-4).

Q. On what rate of return is Cascade's revenue requirement based?

A. Cascade requests an ROR of 7.54 percent, which includes a requested ROE of 10.3 percent and an equity layer of 50.4 percent.[12] This compares to Cascade's currently authorized ROR of 7.24 percent,[13] which includes an authorized ROE of 9.4 percent and an equity layer of 48.5 percent.

Q. Relative to Cascade's test year (2019) ROO, what is the revenue requirement impact of each of Cascade's *restating* adjustments?

A. Table 1 below shows the impact of each of Cascade's restating adjustments.[14]

Table 1. Impact of Cascade's Proposed Restating Adjustments on Revenue Requirement.

Adjustment Number	Restating Adjustment Description	Rev. Req. Impact ($)
R-1	Annualize CRM Adjustment	2.90 M
R-2	Promotional Advertising Adjustment	(0.03 M)
R-3	Restate Revenue Adjustment	(14.92 M)
R-4	Restate End of Period (EOP) Adjustment	3.29 M*
R-5	Restate Wages	0.09 M
R-6	Executive Incentives	(1.29 M)
	TOTAL restating adjustments	(10.00 M)

*The revenue requirement impact of Cascade's EOP adjustment includes the effect of applying Cascade's proposed ROR to EOP rate base.

[12] Nygard, Exh. TJN-1T at 3:10-11.
[13] 2019 Cascade GRC Order at 3, ¶ 11.
[14] *See* Hillstead, Exh. KMH-8.

Q. After restating adjustments (including restating test year revenues to account for the rate increase effective March 1, 2020), what does Cascade's 2019 test year ROO show?

A. Cascade does not present a restated, test year ROO; Cascade only presents its pro forma ROO after combining its restating and pro forma adjustments. Table 2 below shows Cascade's restated test year ROO prior to pro forma adjustments, with and without Cascade's EOP rate base adjustment.

Table 2. Cascade's Test Year (2019) ROO, After Restating Adjustments and After Removal of Cascade's EOP Rate Base Adjustment.[15]

	TEST YEAR (2019) ROO	RESTATED 2019 ROO	REMOVE EOP RATE BASE
NOI	$20,804,385	$29,989,434	$29,989,434
RATE BASE	$374,226,392	$395,862,505	$374,226,392
ROR	5.56%	7.58%	8.01%

After incorporating Cascade's restating Adjustments R-1 through R-6, the Company's restated 2019 ROO using EOP rate base produces a test year ROR of 7.58 percent. However, EOP rate base is not as the standard basis for assessing a utility's ROR; the Commission's standard for assessing utility earnings relies on measuring rate base on an average-of-monthly-averages (AMA) basis.[16] On an AMA basis, Cascade's restated, 2019 results of operations produce a test year rate of return of 8.01 percent, which is 77 basis points above Cascade's currently authorized ROR of 7.24 percent.

[15] Test year (2019) ROO amounts from Hillstead, Exh. KMH-8 at 3, col. 1. Restated is 2019 ROO less columns R-1 through R-6 from *Id*. at 9, rows "Net Operating Revenues" and "Total Rate Base."
[16] *See, e.g., Wash. Utils. & Transp. Comm'n v. Pac. Power & Light Co.*, Dockets UE-140762 et al., Order 08, 61-62, ¶ 145 (March 25, 2015) (2014 Pacific Power GRC Order); *see also Wash. Utils. & Transp. Comm'n v. Olympic Pipeline Company*, Docket TO-011472, Twentieth Supp. Order, 44, ¶ 158-160 (Sept. 27, 2002).

Q. Given that Cascade's restated, test year ROR was 8.01 percent (versus the Company's currently authorized ROR of 7.24 percent), how is it that Cascade claims a revenue *deficiency* of $12.0 million?

A. Cascade manufactures a purported revenue need – bringing it from a revenue surplus to a revenue deficiency of $12.0 million – through the following three contortions:

1. Adjusting test year rate base to an EOP basis (Adjustment R-4);
2. Adding costs the Company claims it will incur after the test year (Adjustments P-2 through P-4); and
3. Requesting an ROR of 7.54 percent, which includes increasing ROE from 9.4 percent to 10.3 percent.

Q. Relative to Cascade's restated, test year ROO, what is the revenue requirement impact of each of Cascade's _*pro forma*_ adjustments?

A. Table 3 below shows the impact of each of Cascade's pro forma adjustments.[17]

Table 3. Impact of Cascade's Proposed Pro Forma Adjustments on Revenue Requirement.

Adjustment Number	Pro Forma Adjustment Description	Rev. Req. Impact ($)
P-1	Interest Coordination Adjustment	0.12 M
P-2	Pro Forma Wage Adjustment	2.11 M
P-3	Pro Forma Plant Additions	8.96 M*
P-4	MAOP Deferral Amortization	0.97 M
	TOTAL pro forma adjustments	12.17 M

*The revenue requirement impact of Cascade's pro forma plant adjustment includes the effect of applying Cascade's proposed ROR to incremental rate base.

[17] *See* Hillstead, Exh. KMH-8.

B. Summary Of Staff's Case

Q. Does Staff agree that Cascade has a $12 million revenue deficiency?

A. No. As Staff's case demonstrates, Cascade has a revenue *surplus* of $508,968.[18]

Q. Does Cascade assert that its actual, test year ROR shows that the Company is under-earning?

A. Yes. Cascade complains that its test year (2019) ROR was 5.26 percent (as compared to its authorized ROR of 7.24 percent).[19] Cascade argues that "if rates remain unchanged," the Company will continue to under-earn.[20]

However, Cascade's rates *did change*. On March 1, 2020, after the conclusion of the Company's 2019 general rate case Cascade increased customer base rates by 2.84 percent.[21] Therefore, neither Cascade's test year ROO nor the 5.26 percent the Company claims it achieved in 2019 take into account the rate increase that went into effect on March 1, 2020 (i.e. after the test year Cascade uses for this case). Cascade misleadingly suggests the rates currently in effect are what produced the 5.26 percent ROR in the test year. That is not the case. As I demonstrate in Section IV.A., above, Cascade's restated, test year ROR was 8.01 percent.

[18] Hillstead, Exh. KMH-4, ln. 7.
[19] Peters, Exh. MCP-1T at 2:20-21.
[20] *See Id*.
[21] 2019 Cascade GRC Order, Exhibit A, Joint Settlement Agreement, 2, ¶ 7.

Q. Can you please summarize the elements of Cascade's case that Staff contests?

A. Yes. The elements of Staff's case, in order of their individual impact on revenue requirement relative to Cascade's calculation[22] are as follows:

- Pro forma plant (Adjustment P-3) – $7.7 million decrease[23]
- Cost of Capital – $3.4 million decrease[24]
- Pro forma wages (Adjustment P-2) – $1.3 million decrease
- MAOP amortization (Adjustment P-4) – $0.1 million decrease
- Per books audit (Staff Adjustment UTC-1) – $0.05 million decrease

Q. Are there any other adjustments where Staff's and Cascade's numbers differ?

A. Yes. Although Staff technically does not contest Adjustments R-4 and P-1, those two adjustments are impacted by other elements of the revenue requirement Staff does contest and, therefore, numbers in the adjustments differ between Staff and Cascade:

- Interest coordination adjustment (Adjustment P-1) – $0.3 million increase
- End of period (EOP) adjustment (Adjustment R-4) - $0.2 million decrease

[22] Hillstead, Exh. KMH-8.
[23] This amount reflects the effect of using Staff's Adjustment P-3 in place of Cascade's Adjustment P-3 at Staff's recommended ROR. The $8.1 million amount cited in Panco Exh. DJP-2 at 1, ln 25, col. D, includes the additional effect on Adjustment P-1 of using Staff's recommended ROR in place of Cascade's recommended ROR.
[24] This amount reflects the effect of using Staff's recommended ROR in place of Cascade's recommended ROR, both at Staff's recommended rate base. Applying Staff's ROR to Cascade's proposed rate base results in a reduction to revenue requirement of $3.9 million.

Q. What should the Commission take away from the impacts you list above, in terms of the primary drivers of revenue requirement?

A. Cascade's case is driven almost entirely by pro forma plant and ROR, together accounting for $11.1 million of the $12.5 million difference between Staff's and Cascade's revenue requirement calculations.

Q. Is Staff contesting Cascade's EOP adjustment?

No. Although Staff decided not to contest Cascade's EOP adjustment (Adjustment R-4), Cascade clearly failed to carry its burden of proving that EOP rate base treatment is warranted.

Q. How has Cascade failed to carry its burden of proving that EOP rate base treatment is warranted?

A. Cascade provided no testimony or evidentiary support for its use of EOP rate base. The Commission has made it clear that utilities must present ample evidence demonstrating that EOP rate base treatment is "an appropriate regulatory mechanism under specific, well documented facts supporting its use."[25] As the Commission has explained, an EOP adjustment is a ratemaking tool that the Commission can use to address regulatory lag "*when a sufficient showing has been made* that, absent the use of EOP rate base, a utility will experience losses."[26] Cascade did none of this.

[25] 2014 Pacific Power GRC Order at 65, ¶ 151.
[26] 2019 PSE GRC Order at 68, ¶ 228 (Emphasis added).

The Commission has rejected EOP adjustments when companies have failed to meet their burden of proof on the issue,[27] as Cascade has done here.

Q. How did Cascade present its EOP rate base adjustment?

A. In its direct case Cascade did not include an EOP adjustment in its presentation at all, choosing instead to use its test year ROO with rate base presented on an EOP-basis as the *starting point* of its revenue requirement calculation.[28]

Cascade ultimately supplemented its case and provided an updated revenue requirement calculation to show the EOP adjustment for test year rate base. However, Cascade continued to offer no rationale for the adjustment. In its supplemental filing, Cascade states that it was now presenting test year rate base on an AMA basis with the EOP adjustment called out separately only because Staff wanted it that way,[29] indicating that Cascade does not agree that such a presentation is necessary.

Nevertheless, in its revised request, filed July 24, 2020, as well as in its response to Staff Data Request No. 127 (which Staff uses as the basis for its revenue requirement calculation),[30] Cascade shows its EOP rate base adjustment in Adjustment R-4.

[27] *See* 2014 Pacific Power GRC Order at 65, ¶ 151.
[28] Peters, Exh. MCP-7T at 1:6-7.
[29] *Id*. at 1:7-9.
[30] *See* Hillstead, Exh. KMH-8.

Q. Has the Commission specified any additional criteria it will use when evaluating a company's request for EOP rate base treatment?

A. Yes. The Commission has indicated it will consider approving EOP rate base if the treatment promises to prevent back-to-back rate cases.[31]

Q. Does Cascade indicate that EOP rate base treatment will allow the Company to avoid filing back-to-back rate cases?

A. No. In fact, Cascade states it will "file an additional rate case shortly after the conclusion of this rate case."[32]

Q. Why then does Staff not contest Cascade's EOP rate base adjustment?

A. A reduction of an additional $2.0 million[33] – which Staff would recommend if it were to contest the EOP adjustment – would reverse nearly a third of the rate increase the Company just implemented in March, and did not strike Staff as a pragmatic position to advance in this case. Although rejection of Cascade's EOP rate base adjustment is justified by the record (or, rather, the lack of one), Staff believes its recommendation on revenue requirement – i.e. a reduction of $0.5 million – fairly reflects the Company's overall cost of service.

Staff's position on Cascade's EOP rate base adjustment should not be construed as Staff supporting the adjustment or the manner in which the Company approached the issue. Cascade's brazen disregard for the Commission's evidentiary

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[31] *See* 2014 Pacific Power GRC Order at 63-64, ¶ 147; 65, ¶ 149.
[32] Parvinen, Exh. MPP-1T, 9:14-17.
[33] Amount is Cascade's EOP rate base adjustment of $21,636,113 multiplied by Staff's ROR of 6.93 percent, divided by the gross-up factor of 0.755.

standards is on its own a valid reason for the Commission to reject Cascade's EOP rate base adjustment, as it has in past cases.[34] Staff also believes the Commission should keep this issue in mind when weighing the merits of a dismissal of Cascade's case versus a rate reduction.

Q. What has Staff determined with respect to Cascade's requested cost of capital?

A. Staff witness Parcell provides the evidentiary basis for lowering the Company's authorized ROR. Staff recommends an overall cost of capital of 6.93 percent.[35] This is based on a capital structure of 48.5 percent common equity and 51.5 percent long-term debt, and an ROE of 9.25 percent. Staff does not contest Cascade's 4.745 percent cost of debt.

Q. What is the impact of Staff's recommendation on cost of capital?

A. Relative to Cascade's requested ROR of 7.54 percent, Staff's recommended rate of return of 6.93 percent reduces revenue requirement by $3.9 million.[36]

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[34] *See* 2014 Pacific Power GRC Order at 65, ¶ 151.
[35] Parcell, Exh. DCP-3.
[36] This amount is calculated using Cascade's requested pro forma rate base. Using Staff's pro forma rate base recommendation (reflecting the effect of Staff's Adjustment P-3), Staff's recommended rate of return of 6.93 percent reduces revenue requirement by $3.4 million.

Q. What if the Commission is inclined to not reduce Cascade's ROE? Would Staff's revenue requirement calculation still show a revenue surplus if ROE were to remain unchanged from 9.4 percent?

A. Yes. If Cascade's authorized ROE were to remain unchanged at 9.4 percent (and its capital structure unchanged at 48.5 percent equity), Staff's analysis indicates that Cascade would continue to operate at a revenue surplus of $0.1 million.[37]

My purpose for noting Cascade's revenue surplus at the currently authorized ROE of 9.4 percent is to further impress upon the Commission that Cascade did not need to file this case. Cascade's current rates are sufficient to cover the Company's cost of service, including its currently authorized 9.4 percent ROE.

Q. What has Staff determined with respect to Cascade's requested pro forma plant adjustment?

A. In its pro forma plant adjustment (Adjustment P-3), Cascade builds into its revenue requirement calculation $66.1 million in post-test year plant. However, as Staff witness Panco shows, as of October 27, 2020, Cascade has confirmed that only $6.9 million of the $66 million request has been placed in service. The remaining portion of Cascade's Adjustment P-3 – $59.1 million – represents projects that are not (and may never be) in service.

Therefore, Staff recommends that the Commission include in Adjustment P-3 only the $6.9 million in post-test year plant additions that Cascade has confirmed to

[37] Applying a 7.00 percent ROR to the rate base amount of $402,652,193 (Hillstead, Exh. KMH-4, ln. 1) produces a required net income of $28,193,707, which is below Cascade's adjusted net income of $28,283,946 (Hillstead, Exh. KMH-4, ln. 4).

be in service. Relative to the test year ROO, Staff's Adjustment P-3 increases revenue requirement by $829,754. Relative to Cascade's request, Staff's Adjustment P-3 reduces revenue requirement by approximately $8.1 million.[38]

Q. Does Staff have any additional concerns about Cascade's pro forma plant adjustment?

A. Yes. I discuss those concerns separately in Section V, below.

Q. What has Staff determined with respect to Cascade's adjustment for pro forma wages?

A. Through its pro forma adjustment for employee wages (Adjustment P-2), Cascade asks ratepayers to pay for a three-plus percent wage increase for a third consecutive year in 2021. As described by Staff witness Huang, Staff objects to the three percent wage increase in 2021 on the grounds that the wage increase (a) has not happened and, therefore, is not known and measurable, (b) is not necessary, required by contract, or otherwise outside of the Company's ability to control, and (c) is not an appropriate cost to pass onto ratepayers given the circumstances customers currently face.

Staff also objects to the incremental one percent wage increase (from a three percent increase to a four percent increase) for its non-union employees in 2020. This additional one percent represents costs that are at the Company's discretion.

[38] Panco, Exh. DJP-2 at 1, ln. 25, col. D. This amount includes the effect on Adjustment P-1 of using Staff's recommended ROR in place of Cascade's recommended ROR.

Q. What is the impact of Staff's pro forma wage adjustment?

A. Relative to Cascade's test year 2019 ROO, Staff's Adjustment P-2 increases revenue requirement by $860,226. As compared to Cascade's request, Staff's Adjustment P-2 decreases revenue requirement by $1.3 million.

Q. Please summarize the final two adjustments Staff contests (Adjustments P-4 and UTC-1).

A. Staff contests Cascade's MAOP amortization adjustment (Adjustment P-4) and creates a new adjustment (Adjustment UTC-1) to reflect the results of Staff's audit of Cascade's test year (2019) per-books ROO.

Relative to Cascade's case, Staff's MAOP amortization adjustment (Adjustment P-4) decreases revenue requirement by $0.1 million. Staff adjustment UTC-1 decreases revenue requirement by $0.05 million.

Q. Why are these two adjustments important?

A. Staff contests the MAOP amortization adjustment (Adjustment P-4) and the adjustment for Staff's per-books audit (Adjustment UTC-1) because of the longer-term effects of *not* contesting those items.

Regarding MAOP amortization, Cascade's Adjustment P-4 amounts to a proposal to amortize its MAOP investments over progressively shorter periods with each passing year. For example, with Cascade's approach the Company would amortize its year 1 investments over ten years, its year 5 investments over five years, and its year 10 investments over one year. Over a multi-year time horizon, Cascade's approach would result in the cost burden on ratepayers increasing exponentially with each passing year, reaching a crescendo in year 10 where the cost of all incremental investments would be recovered from ratepayers over a single year.

Regarding Staff's per-books audit adjustment (Adjustment UTC-1), Staff contests the inappropriate items Cascade fails to remove from its test year, per-books results of operations (and, accordingly, its revenue requirement) to send the message that find and call out costs that companies include in revenue requirement but for which under no circumstance should ratepayers be required to pay.

V. POLICY CONCERNS RELATED TO CASCADE'S PRO FORMA PLANT ADJUSTMENT

A. Cascade's Pro Forma Plant Adjustment Is Wildly Inconsistent With Cascade's Actual Plant Additions In 2020

Q. Can you please provide a recap of Cascade's pro forma plant adjustment?

A. Sure. In its pro forma plant adjustment (Adjustment P-3), Cascade includes $66.1 million in post-test year plant additions the Company says it will place in service in 2020.[39]

[39] Peters, Exh. MCP-6 at 3.

Q. What is the problem with the plant amount Cascade includes in its pro forma plant adjustment?

A. It only exists on paper. The overwhelming majority of the projects upon which Cascade bases its pro forma plant adjustment are not in service, and it is unclear if they will be by the end of the year, if at all. As Staff witness Panco shows, of the $66.1 million in projects Cascade claims will be in service by December 31, 2020, Cascade has verified that only $6.9 million had been placed in service as of October 27, 2020.[40]

Q. Do you have any other reason to doubt that Cascade's net plant in service will grow by more than $66 million in 2020?

A. Yes. In addition to Cascade verifying that only $6.9 million has been placed in service, Cascade's claim that it will add $66.1 million in plant in 2020 is (a) grossly out of step with the pace of Cascade's investments in reality and (b) inconsistent with Cascade's report that some projects have been delayed or halted altogether.[41]

Q. Can you please explain how Cascade's claim that it will add $66 million of new plant in 2020 is grossly out of step with reality?

A. Yes, though I should first point out that Cascade claims it will add much more than $66 million in new plant; Cascade claims that there is an *additional* $30 million in

[40] *See* Panco, Exh. DJP-2 at 2.
[41] Parvinen, Exh. MPP-1T at 4:7-14.

plant additions that the Company has not included in Adjustment P-3.[42] Effectively Cascade testifies that it will be adding $96 million in post-test year plant.

According to the Company's quarterly actual results of operations filed pursuant to WAC 480-90-275, Cascade is not adding plant at anywhere close to that level. The Company's net plant in service for the first, second, and third quarters of 2020 has grown by $8.6 million,[43] $1.4 million,[44] and $9.6 million,[45] respectively.[46] However, these amounts ($19.6 million total through the first three quarters of 2020), include plant additions related to the Company's high-risk pipeline replacement program, the cost of which Cascade recovers through its Cost Recovery Mechanism (CRM). According to the Company's annual filing to update CRM rates, Cascade has added $9.2 million in CRM plant through September of 2020.[47] After removing amounts Cascade recovers through its CRM (and therefore does not need to recover through this GRC), Cascade's net plant in service has grown by closer to $10 million over the first three quarters of 2020.

In short, the $66 million in plant additions Cascade includes in its pro forma plant adjustment – let alone its assertion that really the Company will be adding closer to $96 million – does not pass the smell test given the Company's net plant in

[42] *Id*. at 9:14-17.
[43] Report of Actual Results of Washington Operations for the Quarter Ending March 31, 2020, Docket UG-200427 (May 12, 2020).
[44] Report of Actual Results of Washington Operations for the Quarter Ending June 30, 2020, Docket UG-200741 (August 14, 2020)
[45] Report of Actual Results of Washington Operations for the Quarter Ending September 30, 2020, Docket UG-200911 (Nov. 12, 2020).
[46] As compared to the net plant in service presented in Cascade's 2019 Commission Basis Report, Docket UG-200393 (April 30, 2020).
[47] *See* Docket UG-200493, Revised Proposed Revisions to Cascade's Schedule 597 Rates (Oct. 14, 2020).

service in Washington (excluding CRM plant) has grown by about $10 million through Q3 of 2020.

Q. Is Cascade's $10 million in actual net plant additions through Q3 2020 evidence that Adjustment P-3 should include more than the $6.9 million Staff recommends?

A. No. First, Cascade did not request that Adjustment P-3 include plant transfers beyond the projects the Company specifically identifies. Of the projects Cascade identifies, only $6.9 million has been placed in service. If the Commission were to use the net plant additions from Cascade's Q3 ROO for Adjustment P-3, the Commission would be including in the adjustment unknown projects not even identified in Cascade's case. Second, it is impossible to assess the degree to which the costs associated with the net plant additions identified in Cascade's Q3 ROO are offset by other factors. It is entirely possible for a utility's net plant in service to increase while the utility's overall cost of service remains materially unchanged.

B. Cascade's Pro Forma Plant Adjustment Fails To Adhere To Commission Rules

Q. How does Cascade's pro forma plant adjustment fail to adhere to Commission rules?

A. There are both procedural and substantive issues with Cascade's position, which I will address in turn.

Q. What procedural issue does Cascade's position present?

A. Cascade intends to make its case on rebuttal, and it openly acknowledges the fact.[48] Bear in mind that Cascade's pro forma plant adjustment is the primary driver of the Company's request for a rate increase. Staff witness Panco's adjustment to pro forma plant alone reduces Cascade's requested $12 million revenue requirement increase by approximately $8.1 million.[49] In other words, about 2/3rds of the Company's requested increase is based on projects that Cascade says it intends to provide supporting evidence only after parties have completed their reviews and submitted testimony in response to the Company's direct case.

This is inappropriate. As the Commission's procedural rules clearly state, "[t]he company must include in its initial testimony and exhibits, including those addressing accounting adjustments, sufficient detail, calculations, information, and descriptions necessary to meet its burden of proof,"[50] including for pro forma adjustments.[51] Further, the Commission has long held that companies may not present their *prima facie* case on rebuttal.[52] This is not simply a matter of fairness

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[48] Parvinen, Exh. MPP-1T at 9:5-6.
[49] Panco, Exh. DJP-2 at 1, ln. 25, col. D.
[50] WAC 480-07-510(3)(a).
[51] WAC 480-07-510(3)(c).
[52] *Wash. Utils. & Transp. Comm'n v. Avista Corp.*, Dockets UE-160228 and UG- 160229, Order 04, 5, ¶ 12 (Oct. 10, 2016) ("The Commission has consistently given guidance, over many years, that a utility that does not distribute to other parties its updated background material and work papers in time for the parties to present evidence on a major issue, fails to follow acceptable procedure. This being the Commission's practice, it is even less acceptable for a party to present an alternative request for relief for the first time at the rebuttal stage of a proceeding. It remains today a disfavored practice for a utility to limit other parties' opportunity to examine a proposal by waiting until rebuttal to present it. The Commission expects the company to present its proposals in its direct case."); *see also GTE Northwest, Inc. v. Whidbey Telephone Co.*, Docket UT-950277, Fifth Supplemental Order, 6 (April 2, 1996) ("[The Complainant,] GTE chose to bring a complaint case under RCW 80.04.110. In making this choice, GTE assumed the burdens of the moving party in a complaint proceeding. It was the responsibility of GTE to analyze and determine what it believed to be the elements of a prima facie case. It was the responsibility of GTE to determine what proof would establish each of those elements, and to proffer the requisite evidence in its direct case.").

and procedural due process for Staff and other non-company parties, it is a question of whether the Commission will have a record from which it can make a fully informed decision.

Q. Does Cascade's proposed pro forma plant adjustment raise any substantive concerns?

A. Yes. Cascade's request with respect to pro forma plant indicates a misunderstanding of (1) the Commission's rules on pro forma adjustments (as well as the *purpose* of pro forma adjustments), and (2) the Commission's policy guidance on the used and useful standard, especially with respect to property placed in service after parties have completed their review of the Company's direct case.

Q. What are the Commission's rules on pro forma adjustments?

A. The Commission's rules on pro forma adjustments state that "[p]ro forma adjustments give effect for the test period to all known and measurable changes that are not offset by other factors."[53]

Q. What do the Commission's rules tell us about the *purpose* of pro forma adjustments?

A. Pro forma adjustments pertain to "known and measurable **changes**" relative to the test period that "are not offset by other factors."[54] Given the historical test period

[53] WAC 480-07-510(3)(c)(ii).
[54] *Id*.

serves as the basis for ascertaining the utility's overall cost of providing service,[55] it is critically important to recognize that pro forma adjustments are meant to capture <u>changes to the utility's overall cost of service</u>.

This concept is reinforced by the offsetting factors standard embedded in the Commission's rules; i.e. pro forma adjustments capture changes "not offset by other factors." In other words, known and measurable changes that *are* offset by other factors are not appropriate for pro forma treatment because they have not resulted in a change to the utility's overall cost of providing service.

This makes intuitive sense given the Commission's core objective in a general rate case of setting rates sufficient for the utility recover its cost of providing service.

Q. Does Cascade correctly apply these concepts?

A. No. Even if the costs Cascade includes in its pro forma plant adjustment were known and measurable – which they are not, given that only $6.9 million of the $66 million in requested plant additions actually is in service – Cascade has failed to demonstrate the costs have not been offset by other factors. As a result, Cascade's pro forma plant adjustment is not useful for assessing whether the Company's overall cost of providing service has increased since the test year.

[55] *See Wash. Utils. & Transp. Comm'n v. Avista Corp.*, Dockets UE-090134, UG-090135, and UG-060518 (consolidated), Order 10, 19, ¶ 41 (Dec. 22, 2009) (2009 Avista GRC Order).

Q. Don't incremental plant additions increase a utility's overall cost of service?

A. Not necessarily. Although a utility absolutely will incur new plant-related costs after the test year, those cost increases can be balanced by decreases in costs elsewhere in the business (or by increases in revenues). The core problem with Cascade's pro forma plant adjustment is that it does not account for these offsetting factors; it includes items that increase costs but omits items that decrease costs. As a result, Cascade's pro forma plant adjustment tells us next to nothing about how (or whether) the Company's overall cost of service has changed relative to the test year.

Q. Can you provide some general examples of offsetting factors?

A. Sure. Although utilities will continue to invest in plant (including after the test year used for a rate case), utilities also will (a) remove plant from service which decreases both depreciation expense and rate base, (b) further depreciate test year plant which also decreases rate base, (c) add new customers which increases revenues relative to test year levels, and (d) realize operational efficiencies (such as reductions to O&M expense) due to replacing old facilities with new, which decreases costs relative to test year.

Q. Does Staff cite any examples where Cascade failed to account for offsetting factors?

A. Yes. Staff witness Panco provides examples where Cascade includes the cost of a project but omits cost reductions associated with that same project.[56] Staff witness

[56] Panco, Exh. DJP-1T at 17-18.

Panco discusses Cascade's failure to reflect in revenue requirement (a) the removal of depreciation expense for facilities being replaced, (b) offsetting reductions to operations and maintenance expenses, and (c) other offsetting benefits that the Company itself notes.

In addition to offsetting factors directly related to the specific plant addition in question, offsetting factors also include reductions in cost elsewhere in the business, such that the plant addition does not result in an increase in the company's overall cost of service. For example, while a utility will add plant after the test year, that utility also will remove plant from service after the test year; while post-test year plant additions increase depreciation expense, that increase can be offset by the reduction in depreciation expense related to post-test year plant removals.

Cascade's Adjustment P-3 is plagued by this very flaw; it does not account for plant that was removed from service after the test year. As a result, Cascade's revenue requirement includes depreciation expense that the Company knows it no longer will incur and includes a return on rate base for plant that is no longer in service. These offsetting factors are what the Commission's rules require utilities to account for, yet Cascade did not.

C. Cascade's Proposed Pro Forma Adjustments Are Fundamentally Different From The Adjustments Approved In The 2019 PSE GRC

Q. Please provide some background on the Commission's decision in the 2019 PSE GRC. Were there any recent modifications to the property valuation statute or

the Commission's perspective on the used and useful standard prior to that order?

A. Yes. In 2019, the Washington State Legislature passed the Clean Energy Transformation Act which, among other things, amended RCW 80.04.250, the valuation of public service property statute,[57] to clarify the Commission's authority with respect to how it establishes rate base for ratemaking purposes. The Commission subsequently issued a Policy Statement in which it laid out a process for identifying, reviewing, and approving property that becomes used and useful for service in Washington after the effective date of a proposed rate.[58]

However, the Commission's policy statement pertains to property used and useful *after* the rate effective date. Cascade does not include any such property in its pro forma plant adjustment, so there are no projects in this case to which the Commission's policy statement can be directly applied.

Q. In the 2019 PSE GRC, did the Commission comment on property placed in service *prior to* the rate effective date, but after parties file responsive testimony?

A. To some extent, yes. In its final Order 08 in PSE's recently concluded GRC, the Commission emphasized that while its policy statement pertained to property placed in service *after* the rate effective date, the property valuation statute, and the recent

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[57] LAWS OF 2019, ch. 288 § 20.

[58] *In the Matter of the Commission Inquiry into the Valuation of Public Service Company Property that Becomes Used and Useful after Rate Effective Date*, Docket U-190531, Policy Statement on Property that Becomes Used and Useful After Rate Effective Date (Jan. 31, 2019) (Used and Useful Policy Statement).

modifications thereto, pertain also to property used and useful *by or during* the rate effective period.[59]

Ultimately, the Commission found that costs for certain of the projects PSE identified in its case were appropriate to include in revenue requirement, even though some of those costs were incurred after parties filed responsive testimony.[60]

Q. Of what relevance is the Commission's Final Order 08 to the projects Cascade includes in its pro forma plant adjustment?

A. In Adjustment P-3, Cascade includes a large number of plant transfers (approximately $60 million) that will not be in service as of the drafting of this responsive testimony, but that theoretically *could* be placed in service prior to December 31, 2020. Since in its Final Order 08 the Commission allowed into rates certain costs incurred after parties filed responsive testimony, it is conceivable that the Commission would contemplate doing something similar in this case.

Q. In its review of Cascade's pro forma plant adjustment, did Staff consider the Commission's decision in Order 08 of the PSE rate case?

A. Yes. However, as discussed by Staff witness Panco, in the current Cascade case the projects not yet in service but still included in the Company's pro forma plant

[59] *See* 2019 PSE GRC Order at 37-38, ¶¶ 112-14.

[60] *See Id*. at 9, ¶ 6 (response testimony filed Nov. 22, 2019); 39-42, ¶¶ 121 and 130 (Get to Zero- In service June 30, 2019, pro forma adjustment authorized through Dec. 31, 2019); 49, ¶ 155 (AMI- placed into service on an ongoing basis, pro forma adjustments approved through Dec. 31, 2019, excluding recovery of return on these investments); 63, ¶ 204 (HR TOPS software- placed in service Jan. 2019, adjustment approved through Dec. 31, 2019); 64, ¶ 209 (High Molecular Weight Cable Replacement-placed in service between Jan. and Dec. 2019, adjustment approved through Dec. 31, 2019).

adjustment are distinctly different from those the Commission included in PSE's revenue requirement.[61]

Q. How are the projects not yet in service in the current Cascade case different from those the Commission included in revenue requirement in the PSE case?

Aside from $6.9 million related to projects the Company has verified are in service, Cascade includes in its pro forma plant adjustment a relatively large number of projects with a high degree of uncertainty as to whether they will be in service, leaving Staff and other parties unclear on which projects have a legitimate chance of going into service this year and which do not.

Moreover, the post-testimony costs the Commission included in PSE's revenue requirement largely represented a continuation of costs incurred for projects used and useful <u>*prior to*</u> parties filing responsive testimony.[62] While some of PSE's projects were multi-year projects with a phased roll-out (e.g. PSE's Get To Zero initiative and its investments in Advanced Metering Infrastructure), the Commission also indicated an openness to extending the pro forma period for assets with short book lives.[63] It is critical to recognize that each of the costs the Commission included in revenue requirement in the PSE case were related to projects that were used and useful to ratepayers well before parties filed responsive testimony.[64]

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[61] Panco, Exh. DJP-1T at 18-20.
[62] *See* n.60, *supra*.
[63] 2019 PSE GRC Order at 42, ¶ 130.
[64] *See* n.60, *supra*; *see also Id*. at 65, ¶ 212 (Public Improvement- placed in service between January and June 2019); *compare with, Id*. at 55, ¶ 177 (Tacoma LNG projects not included for immediate recovery in rates, as plant was not yet used and useful to ratepayers).

Q. Does Cascade describe how its request aligns with these criteria?

A. No. Cascade's request does not appear to be informed by these criteria at all. Cascade's pro forma plant adjustment consists mostly of plant that is not in service, and is not limited to (and by and large does not include) projects with short book lives, multi-year projects with a phased roll-out, or a continuation of costs incurred for projects used and useful prior to parties filing responsive testimony.

Q. Are there any other reasons the projects Cascade has yet to place in service do not fit within the Commission's policy guidelines?

A. Yes. For the projects not yet in service, Cascade has not requested approval subject to future review and refund, as contemplated in the Commission's policy statement.[65] Rather, Cascade is asking for immediate inclusion in rates without future review, which requires the projects to be comprehensively reviewed in this proceeding and requiring that the Company's adjustment meet all the traditional pro forma standards. This means that all projects must be verified as in-service and used and useful, and all costs must be known and measurable and proven to have been prudently incurred.[66]

Cascade's case presents an opportunity for the Commission to further expand upon the policy guidance it has recently provided for pro forma plant additions. Here, the Commission can clearly distinguish the costs it allowed in the pro forma plant adjustment in 2019 PSE GRC from the costs Cascade includes in its pro forma plant adjustment. It can also provide additional guidance on when and how utilities

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[65] *See* Used and Useful Policy Statement at 10, ¶ 29; 11-12, ¶ 34.

[66] *Id*. at 6, ¶ 17; 7, ¶ 20.

must demonstrate adherence to Commission rules and standards to those utilities that struggle to understand that they still must meet those rules and standards and that parties still must be given due process.[67]

Q. Does Staff accept the offsetting revenues Cascade includes in its pro forma plant adjustment?

A. No. The fact that growth plant generates new revenues that offset its costs is the very reason growth plant and offsetting growth revenue need not be included in the revenue requirement calculation. The Commission's rules clearly state that pro forma adjustments give effect to the test year of all known and measurable changes <u>*not offset by other factors*</u>. Costs for growth plant are offset by other factors, so there is no need to capture them in a pro forma adjustment.

Additionally, the costs and offsetting revenues for growth plant Cascade includes in its Adjustment P-3 are based on the Company's projections for customer growth which cannot be verified prospectively. As the Commission previously has noted, projections generally do not meet the Commission's standard for pro forma adjustments.[68]

In short, pro forma adjustments for growth plant are both inappropriate and unnecessary. Staff therefore removes from Adjustment P-3 pro forma growth plant

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[67] *See Id*. at 9, ¶ 25.

[68] *See* 2009 Avista GRC Order at 21, ¶ 45 ("Costs that are documented by actual expenditure, invoice, contract, or other specific obligation usually meet this test. Costs that are the product of forecasts, projections, or budgets generally will not qualify."); *see also* 2019 PSE GRC Order at 38, ¶ 114 (Justifying approval of pro forma plant projects in part because "[h]ere, we need not rely on projections or estimates.").

(decreasing revenue requirement) as well as pro forma growth revenue (increasing revenue requirement).

Q. If Cascade can demonstrate by December 31, 2020, that additional projects have been placed in service, does Staff support including the costs for those projects in revenue requirement?

A. No. For any additional projects placed in service, parties will not have had a reasonable opportunity to evaluate whether the actual final project costs were prudently incurred, and parties will not have been given a reasonable opportunity to conduct a focused examination of those projects; it has been frustratingly unclear throughout this case which of the nearly $60 million in projects that were not yet in service when parties filed testimony are likely to be in service by the end of the year. Cascade's responses to discovery indicate that the Company's projected in-service dates are in a constant state of flux, leaving Staff to doubt that the in-service dates the Company initially projected (and has continued to revise) represent Cascade's true and honest expectations for when those projects will be completed.

Additionally, as I describe in further detail in Section V.B., above, Cascade's pro forma plant adjustment fails to account for offsetting factors. As a result, even if Cascade can demonstrate that it has placed additional projects in service, in failing to account for offsetting factors Cascade has deprived the record of the evidence necessary to assess the extent to which – or whether – those projects materially impact the Company's overall cost of service.

Q. Did Staff evaluate the materiality of the projected plant additions Cascade included in its pro forma plant adjustment?

A. Not really. While the Commission has noted that whether or not a project is "major," is a key consideration for pro forma adjustments,[69] the fact that the vast majority of the projects Cascade includes are not yet in service, and that Cascade's projected costs and in service dates appear to lack accuracy, Staff did not feel assessing the materiality of non-existent investments was a worthwhile endeavor, if even possible.

I note here, however, that it is likely that several of the hypothetical costs Cascade includes in its pro forma plant adjustment would not meet the materiality thresholds the Commission previously has employed. Cascade itself does not appear confident that all projects within the adjustment would be considered major.[70]

Q. Does this conclude your testimony?

A. Yes.

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[69] *See e.g., Wash. Utils. & Transp. Comm'n v. Avista Corp.*, Dockets UE-170485 and UG-170486, Order 07, 66, ¶ 196 (April 26, 2018).

[70] *See* Parvinen, Exh. MPP-1T at 9:9-12 ("Cascade's proposes to include as major capital projects all projects for which the budget exceeded $120,000. While $120,000 in and of itself may not seem "major," there are several projects in this cost range that, together, represent significant investment, and therefore warrant inclusion for recovery.").