BEFORE THE WASHINGTON

UTILITIES & TRANSPORTATION COMMISSION

WASHINGTON UTILITIES AND TRANSPORTATION COMMISSION,

Complainant,

v.

CASCADE NATURAL GAS CORPORATION,

Respondent.

DOCKET UG-210755

TESTIMONY OF MARK E. GARRETT IN OPPOSITION TO THE MULTIPARTY SETTLEMENT
ON BEHALF OF THE
WASHINGTON STATE OFFICE OF THE ATTORNEY GENERAL
PUBLIC COUNSEL UNIT

EXHIBIT MEG-1T

April 25, 2022

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EXHIBIT MEG-1T
DOCKET UG-210755

TABLE OF CONTENTS

PAGE

TABLES

TESTIMONY OF MARK E. GARRETT IN OPPOSITION TO THE MULTIPARTY SETTLEMENT
EXHIBIT MEG-1T
DOCKET UG-210755

EXHIBITS LIST

Exhibit MEG-2	Qualifications and Curriculum Vitae of Mark E. Garrett
Exhibit MEG-3	Summary of Revenue Requirement Recommendations
Exhibit MEG-4	Results of Operations Summary Sheet
Exhibit MEG-5	Rate Base and Operating Income Update
Exhibit MEG-6	Restate Revenue
Exhibit MEG-7	Restate Payroll
Exhibit MEG-8	Incentive Compensation
Exhibit MEG-9	Director's Fees Adjustment
Exhibit MEG-10	Customer Growth
Exhibit MEG-11	End of Period Rate Base
Exhibit MEG-12	End of Period Depreciation Adjustment
Exhibit MEG-13	Interest Coordination Adjustment
Exhibit MEG-14	Cost of Capital
Exhibit MEG-15	Cascade Natural Gas Corp. Response to Public Counsel Data Request No. 22
Exhibit MEG-16	Cascade Natural Gas Corp. Response to AWEC Data Request No. 65, with Attachment A
Exhibit MEG-17C	Cascade Natural Gas Corp. Response to AWEC Data Request No. 67, with Confidential Attachment A
Exhibit MEG-18	Cascade Natural Gas Corp. Response to Public Counsel Data Request No. 58, with Attachment A

I. WITNESS IDENTIFICATION AND PURPOSE OF TESTIMONY

Q. Please state your name and business address.

A. My name is Mark Garrett. I am the President of Garrett Group Consulting Inc., an Oklahoma based firm specializing in public utility regulation, litigation, and consulting services. My business address is 4028 Oakdale Farm Circle, Edmond, Oklahoma 73013.

Q. Please describe your educational background and your professional experience related to utility regulation.

A. I am an attorney and a certified public accountant. I work as a consultant in the area of public utility regulation. I received my bachelor's degree from the University of Oklahoma and completed postgraduate hours at the Stephen F. Austin State University and at the University of Texas at Arlington and Pan American. I received my Juris Doctorate degree from Oklahoma City University Law School and was admitted to the Oklahoma Bar in 1997. I am a Certified Public Accountant licensed in the States of Texas and Oklahoma with a background in public accounting, private industry, and utility regulation. In public accounting, as a staff auditor for a firm in Dallas, I primarily audited financial institutions in Texas. In private industry, as controller for a mid-sized ($300 million) corporation in Dallas, I managed the corporate accounting function, including general ledger, accounts payable, financial reporting, audits, tax returns, budgets, projections, and supervision of accounting personnel. In utility regulation, I served as an auditor in the Public Utility Division of the Oklahoma Corporation Commission from 1991 to 1995. In that position, I managed the audits of major gas and electric utility companies in Oklahoma. Before leaving the Oklahoma Commission I served as the personal aide to Commissioner Bob Anthony. Since leaving the Oklahoma Corporation Commission, I have worked on rate cases and other regulatory proceedings on behalf of various consumers and consumer groups. I have provided testimony before the commissions in the states of Alaska, Arizona, Arkansas, Colorado, Florida, Indiana, Massachusetts, Nevada, Oklahoma, Texas, Utah, and Washington. My qualifications were accepted in each of those states.

My clients include large industrial customers, large gaming customers in Nevada, large hospitals and hospital groups, universities, cities, large commercial customers and solar industry interveners. I have also testified on behalf of commission staffs and offices of attorneys general in the states of Indiana, Nevada, Oklahoma, Washington, Florida and Utah. A more complete description of my education and experience is provided in Exhibit MEG-2.

Q. On whose behalf are you testifying?

A. I am testifying on behalf of the Public Counsel Unit of the Washington Attorney General's Office ("Public Counsel").

Q. What exhibits are you sponsoring in this proceeding?

A. I sponsor the following exhibits:

Exhibit MEG-2	Qualifications and Curriculum Vitae of Mark E. Garrett
Exhibit MEG-3	Summary of Revenue Requirement Recommendations
Exhibit MEG-4	Results of Operations Summary Sheet
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Exhibit MEG-7	Restate Payroll
Exhibit MEG-8	Incentive Compensation
Exhibit MEG-9	Director's Fees Adjustment
Exhibit MEG-10	Customer Growth
Exhibit MEG-11	End of Period Rate Base
Exhibit MEG-12	End of Period Depreciation Adjustment
Exhibit MEG-13	Interest Coordination Adjustment
Exhibit MEG-14	Cost of Capital
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Exhibit MEG-16	Cascade Natural Gas Corp. Response to AWEC Data Request No. 65, with Attachment A
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Q. What is the purpose of your testimony in this proceeding?

A. Garrett Group Consulting, Inc. has been engaged to review the general rate case filing of Cascade Natural Gas Corporation ("Cascade" or the "Company"), a wholly owned subsidiary of MDU Resources Group, Inc., and to present recommendations and ratemaking policy considerations related to the Company's proposed revenue requirement adjustments for its natural gas utility. My testimony presents Public Counsel's recommendations regarding the Company's revenue requirement and Public Counsel's opposition to the proposed Full Multiparty Settlement Stipulation (hereinafter "the Settlement").

II. SUMMARY OF RECOMMENDATIONS

Q. Please summarize the Company's requested rate increase, the revisions the Company made after filing its original application, and the proposed settlement.

A. The Company originally proposed a $13,725,286 rate increase, representing an 11.10 percent increase in margin revenue and an overall increase in rates of 5.12 percent.[1] The Company proposed a capital structure of 49.1 percent equity and a return on equity of 9.4 percent.[2] The Company made several adjustments to exclude executive incentives and 50 percent of Board of Directors expenses, adjust operating income and plant to 2020 End of Period (EOP) levels, restate revenues for the rate increase authorized in 2021, and to restate payroll costs for 2021 pay increases. The Company submitted a revised filing in December 2021 that made a minor correction to executive incentives excluded from operating income.[3]

The Company and the Washington Utilities and Transportation Commission Staff ("Staff" or "WUTC Staff") (hereinafter "Settling Parties") entered into the Settlement, which they filed along with joint testimony and

[1] *See* Direct Testimony of Maryalice C. Gresham, Exh. MCG-1Tr at 2:13–14.
[2] *See* Direct Testimony of Mark A. Chiles, Exh. MAC-1Tr at 2:21–3:5.
[3] *See* Motion for Leave to file Revised Testimony and Exhibits of Cascade Natural Gas (filed Dec. 8, 2021).

supporting exhibits on March 22, 2022.[4] The Settlement proposes an overall revenue increase of $10,692,992, which is approximately an 8.64 percent increase in non-gas operating revenue.[5]

Q. What is Public Counsel's position on the Settlement?

A. Public Counsel opposes the Settlement because the revenue increase the Settling Parties propose is not fair, reasonable, or justified by evidence in the record and is therefore contrary to the public interest. The 2020 unadjusted results of operations show a 5.87 percent return on the average of monthly averages ("AMA") rate base, which would indicate a revenue deficiency of $5.9 million. In addition, the Settlement revenue requirement includes selective cost increases that did not materialize. Cascade's actual operating income and utility investment for 2021 shows that the overly large increase proposed in the Settlement is not supported by actual 2021 results.

The revenue requirement exhibits and recommendations provided in this testimony respond to the Company's revised filing based on the Settlement, which proposes a revenue requirement of $10,692,992, as cited above. This testimony will demonstrate that the revenue requirement proposed in the Settlement is excessive for the test year. Moreover, this testimony will demonstrate that Cascade's more recent operating results for 2021 show that the Company does not require the excessive rate increase proposed by the Settling Parties.

Q. Please summarize the rate impact of Public Counsel's recommendations.

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[4] Full Multiparty Settlement Stipulation of Cascade Natural Gas and WUTC Staff (filed Mar. 22, 2022). *see also* Joint Testimony of Chiles and Joanna Huang, Exh. JT-1T.
[5] *See* Chiles and Huang, Exh. JT-1T at 4:15–16.

A. Public Counsel recommends that the Utilities and Transportation Commission ("Commission") reject the Settlement between Cascade and WUTC Staff. The Settlement fails to incorporate several appropriate adjustments, which result in a much lower rate increase calculation of $2.614 million, compared to the proposed settlement increase of $10.7 million. In total, Public Counsel identifies adjustments totaling $8.079 million that are missing from the Settlement calculation, as shown in the table below, and as set forth in Exhibit MEG-3.

Table 1: Summary of Public Counsel's Adjustments (Millions)[6]

	Total
Total Increase Requested	$10.693
Public Counsel's Total Proposed Adjustments	$(8.079)
Difference	**$2.614**

Public Counsel's adjustments are as follows:

- Account for the impact of 2021 operations on an AMA basis.
- Account for weather normalized 2021 revenue at current authorized rates.
- Annualize payroll to include an entire year's increase for the union pay raise awarded April 1, 2021.[7]
- Remove the 2021 executive incentives.[8]

[6] *See* Garrett, Exh. MEG-4 (Results of Operations Summary Sheet).
[7] *See* Garrett, Exh. MEG-15 (Cascade's Response to Public Counsel Data Request No. 22). The non-union wage increase went into effect in January, so it is already included in our numbers.
[8] *See* Gresham, Exh. MCG-5r. This adjustment was also proposed by Cascade in Restating Adjustment R-5 to be consistent with prior Commission orders. *See* Chiles, Exh. MAC-1Tr at 2:20–3:6; Gresham, Exh. MCG-1Tr at 6:21–7:2.

- Remove 50 percent of 2021 directors' expenses.[9]

The above adjustments result in a revenue requirement of $2.6 million.

For comparison, Public Counsel also presents adjustments to the AMA results to show what the 2021 EOP results would be. These adjustments include restating rate base, revenue, depreciation expense, and income taxes to reflect EOP results.

III. INITIAL REQUEST AND PROPOSED SETTLEMENT

Q. Did you review the settlement proposal and exhibits to ascertain to what extent the proposed increase was reasonable?

A. Yes. A review of Cascade's settlement exhibits shows that it reported net operating income of $24.7 million for its Washington jurisdictional operations in 2020 with a rate of return on its AMA rate base of 5.87 percent.[10] This alone would indicate a revenue deficiency of $5.9 million,[11] not $13.7 million as Cascade initially requested.

Q. How does the Company calculate a requested rate increase of $13.7 million when the test year operations indicate a revenue deficiency of only $5.9 million?

A. Cascade based its request on EOP adjusted rate base and operating income, arguing that rates are to be applied prospectively. It is important with EOP results

[9] *See* Gresham, Exh. MCG-5r. This adjustment was also proposed by Cascade as Restating Adjustment R-6 to be consistent with prior Commission orders. *see* Chiles, Exh. MAC-1Tr at 2:20–3:6; Gresham, Exh. MCG-1Tr at 7:3–5.
[10] *See* Gresham, Exh. MCG-2, column B, lines 22 and 32.
[11] Revenue Deficiency = (Rate Base * Authorized Return less Net Operating Income)/Net of Tax Factor. ($420,487,637*.0693-24,683,915)/.7551 = $5,901,348.

to include known and measurable changes to all the related levels of utility investment, operating expenses, and available revenue.

The test year of calendar year 2020 included a period with a major business shutdown because of the COVID-19 Pandemic. As a result, it is important to verify that the operating results based on the calendar year 2020 are a reasonable basis for setting prospective rates.[12]

Q. Could you evaluate whether Cascade's use of calendar year 2020 as the test year was reasonable?

A. Yes. In this case, because Cascade chose 2020 as its test year, we have the benefit of being able to look at Cascade's actual operations for calendar year 2021 to evaluate whether Cascade's request is reasonable. Based on my analysis, using 2020 as a test year resulted in an unreasonable rate request.

In this testimony, I look first at actual 2021 results based on an AMA approach to rate base, and then I look at actual 2021 results based on an EOP approach.

IV. 2021 AMA RESULTS

Q. Does the Cascade 2020 test year adjusted revenue requirement provide a basis for just and reasonable rates?

A. No. The adjusted revenue requirement for 2020 supported by Cascade and Staff does not represent the ongoing investment and expense levels of the Company. I stated earlier that, using AMA, the unadjusted 2020 operating results would indicate a revenue increase of $5.9 million, and the Settlement is proposing an

[12] *See* Direct Testimony of Nicole A. Kivisto, Exh. NAK-1T at 4:19–21.

increase of $10.7 million, with the main adjustment being an adjustment for an EOP update.

According to the 2021 operating results and plant investment provided in response to Alliance of Western Energy Consumers ("AWEC") Data Requests 65 and 67,[13] net operating income increased by several million dollars from 2020 to 2021. Moreover, when rate base is updated on an AMA basis from 2020 to 2021, rate base increases from $420 million to $487 million.[14] The combination of these two items–an increase in operating income and an increase in rate base–results in the unadjusted revenue deficiency of only $6.7 million for 2021. This indicates that the Settlement proposed increase of $10.7 million is overstated.

Significantly, the $6.7 million is based on actual *unadjusted* results for 2021. When necessary adjustments are made, the revenue requirement is reduced further to $2.6 million. The necessary adjustments are: (1) removing executive incentives, (2) sharing board of directors' expenses 50/50, (3) restating revenue to reflect a full year of the mid-year rate change, and (4) annualizing union pay to reflect a full year for the April pay raise. This restated result includes all increased costs the Company requested in its application, but it also includes the improved operating results for 2021. To increase costs without also reflecting improved operating results violates the regulatory principle of matching and results in unjust rates.

[13] Garrett, Exh. MEG-16, Attah. A and MEG-17C, Conf. Attach. A (Cascade Response to AWEC Data Requests 65 and 67, with Attachments).
[14] *See* Garrett, Exh. MEG-5.

Q. In what ways do your calculations differ from those of the Settling Parties?

A. I used an AMA approach rather than an EOP approach, and I used actual 2021 results rather than the adjusted 2020 results.

Q. Why is using 2021 actual results a more reasonable approach than relying on 2020 results.

A. Using 2021 results is more reasonable for several reasons. (1) In ratemaking, we adjust the results in one year to predict what the next year will be. In other words, we adjust the test year to predict what the rate-effective year will be. Here, we do not need to adjust the 2020 results to predict what the 2021 results will be because we already have the 2021 results. (2) 2021 is much closer in time to the rate-effective period, making it a much better predictor of what costs will be when prospective rates go into effect. (3) 2020 was an abnormal year because of the COVID-19 pandemic. All of the COVID impacts would have to be adjusted out of 2020 before it could be used to reflect a reasonable level for prospective rates. Cascade failed to normalize 2020 results in the initial filing, and both Cascade and Staff failed to normalize 2020 results in the proposed Settlement. Fortunately, 2021 does not suffer from abnormal COVID results in the same way that 2020 did.

Q. Do you have any general conclusions from the information above?

A. Yes. The proposed Settlement should be rejected because the revenue requirement is grossly inflated, as demonstrated by calculating revenue requirement based on actual 2021 results that reflect a more standard year of operations and that is closer in time to the rate effective period and the more appropriate AMA rate base calculation method.

V. 2021 AMA ADJUSTMENTS

Q. Please discuss the adjustments that you made for the 2021 operations and AMA rate base.

A. I adjusted rate base from the 2020 EOP balance requested by the Company to actual 2021 AMA levels. This adjustment increases net plant in service by $8,537,784. Customer advances for construction is increased by $84,833 and accumulated deferred income tax is reduced by $179,972. Customer advances and deferred taxes are used to reduce rate base for cost free capital based on AMA balances from the Company's response to Public Counsel Data Request No. 58.[15] I also adjusted rate base for the change in the working capital allowance. The AMA balance for working capital increased significantly from $13,038,376 to $20,511,946 for 2021. These adjustments combined increase rate base by $16,106,493, as shown at Exhibit MEG-5. Net operating income increased by $4,129,425 million for the unadjusted 2021 operating results based on the information provided in Cascade's response to AWEC Data Request No. 67.[16]

Q. Please discuss the restating adjustments you made for the 2021 operating revenue and expenses.

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[15] Garrett, Exh. MEG-18, Attach A (Cascade Response to Public Counsel Data Request 58, with Attachment A).
[16] Garrett, Exh. MEG-17C, Conf. Attach. A (Cascade Response to AWEC Data Request 67, with Confidential Attachment A).

A. The first 2021 restating adjustment (1) restates revenues for the rates that were set in Docket UG-200568 for normal weather, (2) adjusts the pipeline replacement revenue cost recovery mechanism (CRM) for the rates proposed by the Company, and (3) removes the provision for rate refund that was recorded in 2021. These restating adjustments replicate the adjustments made by Cascade in its filed case and are based on updated billing determinants and weather normalization provided by the Company. Annualizing the rates effective in July of 2021 and normalizing the weather increased operating revenue by $2,307,749. Adjusting to the CRM revenue reduces revenue by $582,702. Removing the rate refund increases operating revenue by $321,121. The combined adjustments are reduced by the impact on revenue taxes, bad debts expense, and income taxes, resulting in a net increase in net income of $1,604,789. This adjustment is found on Exhibit MEG-6.

The second restating adjustment increases payroll costs for the 2021 union pay increase effective April 1 of that year. The adjustment effectively increases payroll costs for the months of January through March to reflect the April pay raises for an entire year.[17] This adjustment increases payroll expenses by $92,863 and payroll taxes by $7,104. When reduced for the impact of income taxes this adjustment reduced net operating income by $78,974. This adjustment is found on Exhibit MEG-7.

[17] The non-union raises were awarded in January, so they are already included in the 2021 numbers.

The third adjustment excludes executive incentives consistent with the order in Docket UG-200568.[18] The adjustment reduces expenses by $1,797,251 for an increase to net operating income of $1,419,828 after the income tax impact is considered. This adjustment is found on Exhibit MEG-8. This adjustment was also proposed by Cascade in its revenue requirement calculations.

The fourth adjustment excludes 50 percent of the Board of Directors' costs consistent with the order in Docket UG-200568.[19] This adjustment reduces Operation and Maintenance expenses by $178,324, for an increase to net operating income of $140,876 after the income tax impact is considered. This adjustment can be found on Exhibit MEG-9. This adjustment was also proposed by Cascade in its revenue requirement calculations.

Q. What is the result of your adjustments for the restated 2021 operations?

A. The 2021 restated operations results in a revenue shortfall of $2,613,851 as found on Exhibit MEG-4.

Q. What are your recommendations regarding the increase in rates proposed in the Settlement?

A. My analysis shows that any increase should be no more than $2,613,851. This calculation is based on the 2021 AMA adjusted results of operations and allows the Company 100 percent of its 2020 year end plant, depreciation expense, and payroll expense, plus an average of another 12 months of plant and expense increases. This calculation results in a revenue shortfall that is less than one

[18] Wash. Utils. & Transp. Comm'n. v. Cascade Natural Gas, Docket UG-200568, Final Order 05, ¶¶ 17, 181, 400, 430 (May 18, 2021).
[19] *Id* ¶¶ 30, 31.

quarter of the increase proposed in the Settlement, rendering the Settlement rate increase unfair, unjust, and unreasonable. The Settlement allows rates that are excessive by over $8 million. In summary, the Settlement results in rates that are harmful to ratepayers and are not in the public interest. As a result, the Commission should reject the Settlement.

VI. 2021 END OF PERIOD RESULTS

Q. Please discuss the adjustments that would be appropriate to update Cascade's investment and operating income to December 2021.

A. The adjustments to update the 2021 AMA results to EOP include adjustments for EOP revenue, EOP rate base, EOP depreciation expense, and synchronized interest.

Q. Please discuss the End of Period revenue adjustment.

A. Cascade gained customers during 2021, and it is appropriate to recognize the increase in revenue that is available to cover any increase in costs. A restatement of revenue to December 2021 increases rate revenue by $848,778, and a similar adjustment increases the CRM revenue by $11,724.[20] Together these adjustments result in an increase in net operating income of $674,883 after being offset by a related increases in revenue taxes, bad debt expense, and income taxes. This adjustment is found on Exhibit MEG-10.

[20] Garrett, Exh. MEG-10.

Q. Please discuss the End of Period rate base.

A. The EOP adjustment increases plant by $37,533,948 which is offset by an increase in accumulated depreciation of $11,771,885 for a net increase in plant of $25,762,063.[21] Customer advances for construction increased by $483,864 and accumulated deferred income taxes decreased by $447,644 from the AMA levels to the EOP levels.[22] Working capital is not adjusted to EOP. The 2021 EOP adjustment increases rate base by $25,725,843. This adjustment is found on Exhibit MEG-11.

Q. Please discuss the End of Period depreciation expense adjustment.

A. The depreciation expense is calculated by applying the depreciation rates approved in Docket UG-200278 to the December 2021 plant balances.[23] The resulting adjustment increases depreciation expense by $1,090,731, which is offset by a reduction in income tax expense of $229,054, for a net reduction to net operating income of $861,678. This adjustment is found on Exhibit MEG-12.

Q. Please discuss the End of Period interest coordination adjustment.

A. The increase in rate base results in an increase in debt for 2021, which reduces income tax expense. The interest coordination adjustment reduces income tax expense by $14,910 and increases net operating income by an equal amount. This adjustment is found on Exhibit MEG-13.

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[21] *See* Garrett, Exh. MEG-16, Attach. A (Cascade's Response to AWEC Data Request No. 65, Attachment A).

[22] *See* Garrett, Exh. MEG-18, Attach. A (Cascade's Response to Public Counsel Data Request No. 58, Attachment A) (The Attachment A title page states that it is the "ATTACHMENT A to Cascade's Response to WUTC Staff Data Request No. 58." It appears that the title page should state "ATTACHMENT A to Cascade's Response to Public Counsel Data Request No. 58.).

[23] In re Cascade Natural Gas, Docket UG-200278, Order 01, ¶ 17 (Dec. 11, 2020).

Q. What is the result of the End of Period adjustments to the 2021 adjustments?

A. The PC 2021 EOP adjustments result in a rate base of $512,244,642, net income of $31,553,251, and a revenue deficiency of $5,198,006. This amount is still less than half of the proposed Settlement.

Q. What do you recommend?

A. I recommend that the Commission reject the settlement, because it is four times higher than the actual results from 2021 using an AMA approach and it is more than two times higher than the actual results from 2021 using an EOP approach. Cascade and Staff base the Settlement on an unreasonable test year which reflected abnormal pandemic operations. Actual results from 2021 demonstrate just how far from reality 2020 was in terms of normal utility operations. Setting rates based on the Settlement would result in rates that are overstated and unfair to ratepayers.

Q. Does this conclude your testimony?

A. Yes, it does.