EXHIBIT NO. ___(JAP-1T)
DOCKET NO. UE-13____
WITNESS: JON A. PILIARIS

BEFORE THE
WASHINGTON UTILITIES AND TRANSPORTATION COMMISSION

In the Matter of the Petition of **PUGET SOUND ENERGY, INC.** **For an Accounting Order Approving the Allocation of Proceeds of the Sale of Certain Assets to Public Utility District #1 of Jefferson County.**	**Docket No. UE-13____**

PREFILED DIRECT TESTIMONY (NONCONFIDENTIAL) OF
JON A. PILIARIS
ON BEHALF OF PUGET SOUND ENERGY, INC

OCTOBER 31, 2013

PUGET SOUND ENERGY, INC.

PREFILED DIRECT TESTIMONY (NONCONFIDENTIAL) OF

JON A. PILIARIS

CONTENTS

PUGET SOUND ENERGY, INC.

PREFILED DIRECT TESTIMONY (NONCONFIDENTIAL) OF

JON A. PILIARIS

I. INTRODUCTION

Q. Please state your name, business address, and present position with Puget Sound Energy, Inc.

A. My name is Jon A. Piliaris. I am employed as Manager, Pricing and Cost of Service at Puget Sound Energy, Inc. ("PSE" or the "Company"). My business address is 10885 N.E. Fourth Street, Bellevue, Washington, 98009.

Q. Have you prepared an exhibit describing your professional qualifications?

A. Yes, I have. It is Exhibit No. ___(JAP-2).

Q. What is the purpose of your testimony?

A. My testimony evaluates the financial consequences to PSE's remaining customers associated with the forced sale of PSE's Jefferson County assets ("Assets") to Public Utility District No. 1 of Jefferson County ("JPUD"). I assess the effect on PSE's revenue requirements attributable to the loss of the Company's service area in east Jefferson County (the "Jefferson Service Territory"). I evaluate whether PSE's former customers in the Jefferson Service Territory paid for the accumulated depreciation associated with the Assets. I assess whether PSE's former customers in the Jefferson Service Territory paid their proportionate share of embedded power costs and evaluate the potential impact of the sale upon future power costs. I discuss the short term transaction and transition costs incurred in connection with the sale to JPUD, and the recovery of these costs from JPUD. Finally, I address how the customer share of the gain should be allocated among customer classes and how that gain could be disbursed to customers.

Q. Please summarize your conclusions regarding the impact of the sale to JPUD on the rates of remaining PSE customers.

A I conclude that the rate revenues paid by PSE's former customers covered their cost of distribution service and, as such, their departure will have minimal impact on this component of the rates of remaining customers. At one end of the spectrum, my analysis considers only expenses that can be directly assigned to the Jefferson Service Territory. At the other end of the spectrum, my analysis includes additional expenses that can be fairly allocated to the Jefferson Service Territory consistent with general methods used to allocate such costs within PSE's electric cost of service studies. My analysis therefore establishes what I believe to be the appropriate "bookends" for assessing the impact on PSE's electric delivery system revenue requirements for remaining customers.[1] I also conclude that our former customers paid their share of property taxes within Jefferson County.

---

[1] References to "electric delivery system" revenue requirements are intended to conform with the categories of costs used in the development of PSE's recently-approved Expedited Rate Filing ("ERF") in Docket No. UE-130137. These categories exclude expenses related to PSE's Power Cost Adjustment ("PCA") mechanism and property taxes, the latter of which are now recovered through a separate rate tracker (Schedule 141).

With respect to power costs, I conclude that our former customers in the Jefferson Service Territory were paying their share of embedded power costs. Based upon my analysis of the impact of the loss of the Jefferson County load on projected future power costs, I conclude that remaining customers will benefit from the lower power costs associated with reduced load on PSE’s system over time.

Although there is no way of making a precise allocation of accumulated depreciation over the entire life of the Assets, I conclude that the customers formerly served in the Jefferson Service Territory were fully funding their share of related depreciation expenses at the time the Assets were transferred to JPUD. I also conclude that transaction and transition costs incurred by PSE were fully recovered by monies collected from JPUD under the Asset Purchase Agreement (“APA”) and the Customer Transition Agreement (“CTA”).

Finally, I recommend that any gain going to PSE’s remaining customers be allocated among the rate schedules in a manner consistent with how related costs were allocated to set rates. PSE proposes that the gain be credited to customers over a four-year period. However, PSE does not have a specific proposal regarding how this credit will be implemented. PSE is willing to work with parties to determine their preferred means by which to credit customers for their share of the gain on the sale of the Assets to JPUD.

II. IMPACT OF LOSS OF JEFFERSON SERVICE TERRITORY ON PSE ELECTRIC DELIVERY SYSTEM REVENUE REQUIREMENTS

Q. Have you evaluated the effects of the loss of the Jefferson Service Territory on the electric delivery system revenue requirements recovered from remaining PSE customers?

A. Yes. I have performed an assessment of these effects. My assessment focuses on data and analyses produced in connection with PSE's recently-approved expedited rate filing ("ERF") in Docket No. UE-130137. However, I have also assessed the impacts related to the "non-ERF" expenses.

Q. Briefly explain how you conducted this assessment on the "ERF-related" revenue requirements?

A. I began with the summarized revenues and revenue requirements depicted in the Second Exhibit to the Prefiled Direct Testimony of Katherine J. Barnard, Exhibit No. ___(KJB-3), as it was subsequently updated in the compliance filing in the ERF docket. From there, I subtracted revenues and revenue requirements associated with service to PSE customers formerly served in the Jefferson Service Territory. The remainder reflects the revenue requirements that would have occurred had the Jefferson Service Territory not been appropriated by JPUD. This analysis is summarized in Exhibit No. ___(JAP-3).

Q. What does Exhibit No. ___(JAP-3) show?

A. Exhibit No. ___(JAP-3) illustrates the impact of the loss of the Jefferson Service Territory on the electric delivery revenue requirements of remaining PSE customers. This exhibit shows that this impact ranges from a $3.2 million increase to a $1.1 million reduction in the remaining customers' revenue requirements. With an overall electric revenue requirement (i.e., including power and property tax expenses) of roughly $2 billion, this is essential a neutral result because the overall impact is within +/- 0.15 percent.

Q. Please explain why two sets of results are provided in Exhibit No. ___(JAP-3).

A. There is a certain set of identifiable expenses that can be directly assigned to the Jefferson Service Territory. Page one of Exhibit No. ___(JAP-3) presents the results that would occur if only these directly-assigned costs are considered. That said, it can be argued that these costs do not cover the entire revenue requirement appropriately attributable to the Jefferson Service Territory. However, since many of these costs cannot be directly attributed to the Jefferson Service Territory, they must instead be allocated. Therefore, to provide the corresponding bookend to the result presented on page one, on page two I present the results that would occur when additional costs are allocated to the Jefferson Service Territory. These allocations are consistent with the general methods used to allocate costs within PSE's electric cost of service studies.

Q. Why did you not simply rely on the results on page two of Exhibit No. ___(JAP-3)?

A. As noted earlier, the results on page two of Exhibit No. ___(JAP-3) apply allocations of expenses[2] that are consistent with the methods used in PSE's electric cost of service study. However, it is not at all clear whether all of those allocated costs are truly avoidable as a result of the loss of the Jefferson Service Territory. For example, just because the Jefferson Service Territory is now being served by JPUD does not mean that the transmission system expenses that were allocated to departing customers will go away. The majority of the transmission facilities once used by those customers remain and these costs will continue to be borne by the remaining (and future) customers. Another example is the level of customer-related and administrative costs that will be avoided with the loss of the Jefferson Service Territory. The extent to which these costs can be fully avoided is speculative. Page two was therefore intended to provide one bookend for the range of reasonable results, by including an allocation of these costs.

Q. Getting back to the specific calculations, please explain how revenue associated with the Jefferson Service Territory was calculated in Exhibit No. ___(JAP-3).

A. Revenues for these customers were calculated in the same manner as they were in the ERF case for PSE's entire system. Using this approach, I multiplied the ERF-related unit costs by rate class by the kWh sales of the former customers in each

---

[2] It also includes an allocation of other revenues.

rate class. These calculations are presented in Exhibit No. ___(JAP-4). In addition, a small portion of PSE's other operating revenues were attributed to the former customers. On page one of Exhibit No. ___(JAP-3), these other operating revenues include those specifically identifiable to service in Jefferson County. On page two, they include a fully allocated share of these other revenues.

Q. How did you derive the ERF-related revenue requirements associated with the Jefferson Service Territory in Exhibit No. ___(JAP-3)?

A. As noted earlier, the majority of revenue requirements attributable to the Jefferson Service Territory presented on page one of Exhibit No. ___(JAP-3) was directly assigned. The primary costs that were directly assigned include distribution expense, depreciation expense, gross plant in service, accumulated depreciation and accumulated deferred taxes. In addition, small amounts of network transmission expense, customer accounting expense, and administrative and general expense were identified in PSE's accounting records as being related to service in Jefferson County. Finally, calculated amounts were included for taxes other than income (line 29), which is tied to revenue, and income taxes (line 30), which is tied to rate base.

For the results shown on page two of Exhibit No. ___(JAP-3), directly-assigned distribution expense, depreciation expense, gross plant in service, accumulated depreciation and accumulated deferred taxes were all carried over from page one. Added to these costs were an allocation of network transmission expense, customer-related expense, administrative and general expense, amortization expense and other rate base items. The factors used to allocate these costs are presented in Exhibit No. ___(JAP-5). These allocation factors are generally consistent with those used to allocate similar costs in PSE's general rate cases. Finally, taxes other than income and income taxes were calculated in the same manner as on page one.

Q. What do you conclude from Exhibit No. ___(JAP-3) regarding the effect of the loss of the Jefferson Service Territory on the remaining customers' electric delivery revenue requirements?

A. The results range from a $3.2 million increase to a $1.1 million reduction in the remaining customers' electric delivery revenue requirements. These results can be found on line 57 on each page of the exhibit. Given that this range readily encompasses a neutral result and that the results using only directly assigned costs are a bit less realistic (i.e., I would give slightly more weight to the results on page two of the exhibit), it is reasonable to conclude that there is a negligible effect on the delivery component of remaining customers' overall revenue requirements.

Q. Do you believe that this has generally been the case over the life of the Assets?

A. Yes. There are many variables that affect the cost of service and the revenue received from customers at any point in time. It is unrealistic to think that you can arbitrarily determine the cost of serving any portion of the Company's service area, at any given time, and find a perfect match with the revenues derived from that area. However, given what has been shown for the recent past and absent any evidence to the contrary, it is reasonable to assume that these differences are small and should offset each other over time.

Q. Have PSE's former Jefferson County customers also been paying their share of property taxes?

A. Yes. PSE's ERF-related property tax expense during the period ending June 30, 2012 was $23.4 million. Property taxes are allocated for ratemaking purposes on the basis of relative net plant. For the period ending June 30, 2012, the net plant value of the Assets sold in Jefferson County was $47.9 million, or 1.6 percent, of the $3.0 billion in ERF-related plant. Applying this 1.6 percent to the $23.4 million in total electric ERF-related property taxes shows that customers formerly served in Jefferson County were paying in their rates approximately $370,000 in related taxes. By contrast, the actual property taxes paid by PSE in Jefferson County were approximately $210,000 in 2011 and $249,000 in 2012. Therefore, for the period analyzed, customers served in Jefferson County have been paying their share of these property taxes.

Q. Have customers formerly served by PSE in Jefferson County also been paying their share of power supply expenses?

A. Exhibit No.___(JAP-6) illustrates that customers in Jefferson County were historically covering their fully allocated share of embedded power costs. Line 9 of Exhibit No.___(JAP-6) shows the total PCA revenue derived from the Jefferson Service Territory for the ERF test period (June ending 2012) was $19.8

million. This revenue is then compared to $1.4 billion in total system PCA revenue, showing that Jefferson PCA revenue was 1.41 percent of the total for the period in question. I then allocated PSE's power costs to the load served in Jefferson County. For many years, PSE has used the "peak credit" methodology to allocate power costs. Using this approach, and the same peak credit energy and demand classifications derived in PSE's last general rate case, loads served in the Jefferson Service Territory would be allocated 1.39 percent of the Company's power supply costs for this time period. Since the estimated share of PCA-related revenue in the Jefferson Service Territory nearly equals the corresponding allocated power costs, we show that customers in this area were paying an amount very similar to their allocated power costs.

Q. Does this analysis reflect a fair allocation of embedded power costs prior to the ERF test period?

A. As with the discussion above of the electric delivery system revenue requirements, these numbers will vary to some degree over time. One cannot reasonably expect a perfect alignment between power costs and the revenues received from a discrete portion of the Company's service area. There will always be differences. However, given what has been shown for the recent past and absent any evidence to the contrary, it is reasonable to assume that these differences are small and should offset each other over time.

Q. Did you assess the financial impact upon future power costs attributable to the loss of the Jefferson Service Area?

A. Yes. I performed an analysis of future power costs to project the effect on PSE's remaining customers of the elimination of the Jefferson County load. This is presented in Exhibit No. ___(JAP-6).

Q. Please describe your analysis.

A. I first forecast an amount of power costs that will be avoided due to the reduction in load from the loss of PSE's customers in Jefferson County. This forecast was performed using the same models and assumptions used to estimate PSE's incremental energy supply costs presented in the prudence case for transmission renewals in PSE's recently settled power cost only rate case ("PCORC"), Docket No. UE-130617.

These projected avoided incremental costs were compared against a projection of the power-related revenues from PSE's former Jefferson County customers over the period in question. The starting point for these projections is the average effective PCA baseline rate for Jefferson County customers reflected in Exhibit No. ___(JAP-6), updated to reflect the PCORC settlement. This adjusted PCA baseline rate is then applied to a forecast of Jefferson County load. The "variable" portion of the PCA baseline rate is assumed to grow at a rate consistent with the forecast of annual market power and gas prices. The "fixed" portion of the PCA baseline rate is held constant through the 20-year period.

The net present value of the difference between the avoided power costs and the lost power-related revenue was then calculated over a period of 20 years. This analysis is summarized in Exhibit No. ___(JAP-7).

Q. Why did you choose to conduct this analysis over 20 years?

A. A sufficient length of time is needed to present a realistic view of the impacts to PSE's remaining customers of this known, measureable and permanent loss of load. Since PSE's standard resource planning analyses of supply-side and demand-side resource alternatives cover a 20-year period, this was considered an appropriate period over which to analyze the impact of PSE's loss of load in Jefferson County. However, the information presented in Exhibit No. ___(JAP-7) does allow you to look at any consecutive period within this twenty-year horizon and determine the net benefit associated with the loss of the Jefferson County load.

Q. What do you conclude from this analysis?

A. Over twenty years, as shown in Exhibit No. ___(JAP-7), the net present value of the net power supply-related benefits associated with PSE's loss of load in Jefferson County is roughly $83 million. This is a significant benefit to remaining PSE customers. In fact, this amount even exceeds the gain on the sale of assets to JPUD that is at issue in this proceeding. During the course of this twenty-year period, the costs and benefits associated with the loss of the Jefferson County load vary from year-to-year as the Company's load grows and new or replacement resources would be expected to come on line. So, for example, in the very near term (the first four years), as you would expect given the current market prices facing the Company, the cost associated with lost revenues exceeds the corresponding power cost benefit. However, by year five, there is a net benefit to remaining customers.

Net incremental energy supply costs can be reasonably predicted using the same models and assumptions used in the PCORC. However, the benefit to remaining customers from a resource acquisition standpoint is absolutely certain. The loss of the Jefferson Service Territory resulted in an immediate and permanent load reduction of approximately 33 aMW.[3] One could compare this to a conservation program where the reduction in demand is immediate and one-hundred percent certain to occur. The decision to acquire this "resource" was compelled by operation of law. Looking forward there is no long term harm to our remaining customers associated with this "investment", and their power cost risk is reduced by 33 aMW.

III. RECOVERY OF ACCUMULATED DEPRECIATION

Q. Have you reviewed the Prefiled Direct Testimony of Matthew R. Marcelia, Exhibit No. ___(MRM-1T)?

A. Yes.

[3] Coincidentally, this is roughly equal to the annual first-year savings targets associated with PSE's conservation programs.

Q According to Mr. Marcelia, what was the total amount of depreciation that was applied to the depreciable Assets?

A. The accumulated depreciation of the Assets was $29,938,735.

Q. Who pays for depreciation?

A. Depreciation is a portion of the cost paid by customers through rates for the service that they receive. The depreciable Assets in question were used and useful for the purpose of providing customers with retail electric service in the Jefferson Service Territory, and the cost of these Assets was reflected in rates. As the depreciation accrues, it is accumulated on the Company's balance sheet as an offset to the rate base used to set rates.

Q. Which customers paid for the accumulated depreciation of the depreciable Assets?

A. The Company's rates are uniform throughout its service area. As such, all customers share in the recovery of PSE's overall depreciation expense. The amount paid by any given customer or group of customers is not tied to specific assets used to provide service within any particular city or county within PSE's service area.

Q. Can it be shown that the Company's former customers in Jefferson County paid their proportionate share of the accumulated depreciation on the depreciable Assets?

A. The data required to calculate a precise allocation of accumulated depreciation over the entire life of the depreciable Assets is not available. We can, however, show that departing customers were currently funding their share of depreciation expenses. This can be seen in the analysis presented in Exhibit No. ___(JAP-3). As shown in this analysis, within a range, the departing customers have generally been covering their share of costs, including their proportionate share of depreciation expense. As with the recovery of the overall revenue requirement, you would not reasonably expect to find a perfect alignment between costs and the revenues received from a discrete portion of the Company's service area each and every year. There will be differences, but it is reasonable to assume that these differences are small and tend to offset each other over time.

Q. What do you conclude from this result?

A. I find it reasonable to conclude that customers formerly served in the Jefferson Service Territory fully contributed to the accumulated depreciation of the Assets.

IV. TRANSACTION COSTS

Q. Were there short term costs incurred by the Company in connection with JPUD's acquisition of the Jefferson Service Territory?

A. There were transaction costs incurred by both parties. Responsibility for these costs is addressed in section 14.7 of the APA:

> Each Party shall bear its own legal, accounting, consulting, regulatory, tax and other professional fees and expenses and other transaction costs, regardless of whether the transactions contemplated under this Agreement are consummated.

As the acquisition moved forward, PSE incurred some costs that it believed were beyond the scope of what was intended in the APA by the term "transaction costs." For example, there were outstanding conservation grants in Jefferson County that were terminated as a result of the transaction. Customers served in Jefferson County were not required to pay back PSE for the conservation savings not realized. The sum of these outstanding grants was $282,999. There were also metering separation costs ($397,000) and other separation costs incurred in connection with transferring the system to JPUD. JPUD vigorously objected to taking responsibility for these costs, seeking to characterize them all as items included in the purchase price. However, pursuant to the CTA, PSE recovered an additional $800,000 from JPUD for transition costs that it believed should be borne directly by JPUD.

The transaction and transition costs borne by PSE, net of the amount paid by JPUD under the CTA, was $1,710,407. As noted in the testimony of Mr. Samuel Osborne, the amount paid by JPUD for the Jefferson Service Territory exceeded PSE's estimate of its all-in value. Therefore, the sums received from JPUD under the APA and the CTA were sufficient to fully cover PSE's share of transaction and transition costs.

V. ALLOCATION AND DISTRIBUTION OF GAIN TO CUSTOMERS

Q. What is the nature of Assets sold to JPUD?

A. These assets include a small amount of 115 kV transmission facilities, but are predominately comprised of distribution assets.

Q. How is this class of assets typically allocated in PSE's rate case?

A. PSE's transmission assets have been allocated on the "peak credit" methodology discussed earlier in my testimony. PSE's distribution assets have generally been assigned to specific customer classes, allocated on the basis of some formulation of non-coincident peak loads or allocated on the basis of the number of customers served.

Q. Is it appropriate to allocate the customer share of the gain on sale of Assets to JPUD on the same basis as related plant is allocated for ratemaking purposes?

A. Yes. There may be other equitable ways to allocate the gain on the sale of the Assets among rate groups, but this approach is reasonable as it aligns well with the basis upon which related costs are allocated for ratemaking purposes. For those reasons, I recommend following this approach in allocating the final gain on sale that is ultimately approved by the Commission to be credited to remaining PSE customers. This approach is illustrated in Exhibit No. ___(JAP-8).

Q. Please explain the calculations presented in Exhibit No. ___(JAP-8).

A. Exhibit No. ___(JAP-8) allocates the $15 million proposed in this case to be credited to customers based on the distribution plant used to set rates in PSE's 2011 general rate case ("2011 GRC"), Docket No. UE-111048. Specifically, this amount is first allocated between low-voltage and high-voltage distribution based upon the net book value of plant sold to JPUD at closing. The amounts allocated to low-voltage and high-voltage distribution are then allocated across each class based on the allocation of like plant in the 2011 GRC.

Q. Why are you treating the transmission facilities sold to JPUD as high-voltage distribution?

A. As noted earlier, the transmission assets sold to JPUD delivered power at voltage of 115 kV. At the time of PSE's 2011 GRC, 115 kV facilities were considered high-voltage distribution. These facilities were subsequently reclassified as transmission in Docket No. U-111701. Since the transmission facilities sold to JPUD were treated as high-voltage distribution in the 2011 GRC, PSE considers it more appropriate to align the treatment of the 115 kV facilities sold to JPUD with like 115 kV facilities used in setting PSE's rates.

Q. Why did you distinguish between low-voltage and high-voltage distribution in Exhibit No. ___(JAP-8)?

A. The relative amount of low-voltage versus high-voltage distribution differs between the Assets and PSE's overall system, where the overall system has more relative investment in high-voltage distribution. For example, while high-voltage distribution makes up 12 percent of the net distribution plant sold to JPUD, it made up 18 percent of PSE's overall net distribution plant in its 2011 GRC. As a result, allocating the customer credit on the average distribution investment on PSE's overall system would give inappropriate weight to the allocation of high-voltage distribution costs.

Q. Over what period should the customers' share of the gain be credited?

A. Consistent with the treatment of PSE's comparably sized regulatory assets and liabilities, PSE proposes to credit customers' share of the gain on the sale of the Assets over a four-year period.

Q. Does PSE have a specific proposal for how to credit customers their Commission-approved share of the gain on sale from the sale of Assets to JPUD?

A. No. PSE anticipates that different rate groups may have specific preferences in this regard. As such, PSE is willing to engage in discussions with interested stakeholders in this proceeding regarding the best approach for crediting each rate group's share of the gain on sale.

VI. CONCLUSION

Q. Does this conclude your testimony?

A. Yes, it does.