

**EXH. MRM-11T
DOCKETS UE-190529/UG-190530
UE-190274/UG-190275
2019 PSE GENERAL RATE CASE
WITNESS: MATTHEW R. MARCELIA**

**BEFORE THE
WASHINGTON UTILITIES AND TRANSPORTATION COMMISSION**

**WASHINGTON UTILITIES AND
TRANSPORTATION COMMISSION,**

Complainant,

v.

PUGET SOUND ENERGY,

Respondent.

**Docket UE-190529
Docket UG-190530 (*Consolidated*)**

In the Matter of the Petition of

PUGET SOUND ENERGY

**For an Order Authorizing Deferral
Accounting and Ratemaking Treatment
for Short-life IT/Technology Investment**

**Docket UE-190274
Docket UG-190275 (*Consolidated*)**

PREFILED REBUTTAL TESTIMONY (NONCONFIDENTIAL) OF

MATTHEW R. MARCELIA

ON BEHALF OF PUGET SOUND ENERGY

JANUARY 15, 2020

PUGET SOUND ENERGY

**PREFILED REBUTTAL TESTIMONY (NONCONFIDENTIAL) OF
MATTHEW R. MARCELIA**

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PUGET SOUND ENERGY

**PREFILED REBUTTAL TESTIMONY (NONCONFIDENTIAL) OF
MATTHEW R. MARCELIA**

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1 **PUGET SOUND ENERGY**

2 **PREFILED REBUTTAL TESTIMONY (NONCONFIDENTIAL) OF**
3 **MATTHEW R. MARCELIA**

4 **I. INTRODUCTION**

5 **Q. Are you the same Matthew R. Marcellia who submitted prefiled direct**
6 **testimony on June 20, 2019, on behalf of Puget Sound Energy (“PSE”) in this**
7 **proceeding?**

8 A. Yes.

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

10 A. The purpose of my rebuttal testimony is to address and clarify the issues raised by
11 Mr. Mullins on behalf of the Alliance of Western Energy Consumers (“AWEC”),
12 Mr. Garrett on behalf of Public Counsel, and Ms. Steward and Mr. McGuire on
13 behalf of Commission Staff.

14 More specifically, I will address Mr. Mullins’ misapplication of deferred taxes
15 and Production Tax Credits (“PTCs”) with respect to Colstrip and respond to the
16 concerns that he raised regarding the treatment of excess deferred income taxes
17 (“EDIT”). Also, with respect to EDIT, I will address Mr. McGuire’s testimony
18 about the rate relief agreed to in PSE’s recent expedited rate filing and
19 demonstrate that customers received the benefit of the reversing EDIT in the
20 historical test year. Regarding Ms. Steward’s testimony, I will clarify a couple of
21 points, including a discussion of IRS Revenue Procedure 2017-47. I will address

1 Mr. Garrett's testimony on the proper treatment of EDIT. Finally, I will point out
2 that no party has objected to the Financial Transparency and Improvement
3 Program ("FTIP"), which I discussed in my direct testimony.

4 II. COLSTRIP UNITS 1 AND 2 RETIREMENT

5 A. Accumulated Deferred Income Taxes ("ADIT")

6 **Q. Please briefly summarize the application of ADIT to the Colstrip Units 1 and**
7 **2 retirements proposed by AWEC witness Bradley Mullins.**

8 A. PSE has recorded ADIT on the Colstrip Units 1 and 2. Included in the ADIT is
9 the excess portion related to Tax Reform (the EDIT). At the retirement of
10 Colstrip Units 1 and 2, PSE will record a regulatory asset for the balance of the
11 unrecovered plant. Mr. Mullins would reduce the balance of the regulatory asset
12 for the unrecovered plant by the ADIT, including EDIT.

13 **Q. Do you agree with Mr. Mullins' application of ADIT with respect to the**
14 **Colstrip Units 1 and 2 retirements?**

15 A. No, Mr. Mullins' application of the ADIT in the treatment of Colstrip Units 1 and
16 2 is misguided and incorrect.

17 **Q. Please explain why his treatment is misguided and incorrect.**

18 A. Mr. Mullins makes several errors that I will discuss later in my testimony. First,
19 he errs in confusing the unrecovered investment with the net rate base. Second,
20 based on PSE's response to a data request, which has since been revised, he
21 portrays the ADIT and the EDIT at opposite signs in his calculation. Third, his

1 calculation of EDIT is illogical. Fourth, he applies the EDIT balance to the
 2 unrecovered plant, contrary to IRS guidance.

3 **Q. Can you begin by providing an example to help explain your concerns with**
 4 **Mr. Mullins' approach?**

5 A. Yes. Consider a simple example of a retirement of an asset with a remaining net
 6 book basis (i.e. unrecovered) of \$100 and a remaining net tax basis of \$25. This
 7 asset would have ADIT of \$15.75 (the net book of \$100 less the net tax of \$25 =
 8 \$75 multiplied by the tax rate of 21%).¹ See Table 1 for a summary of this
 9 example.

TABLE 1							
						-- Rate Making --	
	Book	Tax	Diff (gross)	ADIT	Rate Base	Work Cap	
1 Net Value	100.00	25.00	(75.00)	(15.75)	84.25	-	
2							
3 Sales proceeds	none	none					
4 Cost	(100.00)	(25.00)	75.00				
5 "Loss"	(100.00)	(25.00)	75.00	15.75	(84.25)		
6							
7 Current Tax (bene)	5.25					5.25	
8 DFIT	15.75						
9 "after tax Loss"	(79.00)						
10							
11 Regulatory Asset	100.00	-	(100.00)	(21.00)	79.00		
12							
13 Ending position:	100.00	-	(100.00)	(21.00)	79.00	5.25	

11 At this point, we could summarize the net rate base as \$84.25 (the net book basis
 12 of \$100 less the ADIT of \$15.75). See Line 1.

¹ This example ignores Tax Reform for now to keep the example simple.

1 In this example, I will assume that there will be no sales proceeds. As a result,
2 before considering any regulatory action, we would expect to see a pre-tax book
3 loss of \$100, a tax loss of \$25, and the reversal of the ADIT. See Line 5.

4 If we pause here before considering the Commission's action to establish a
5 regulatory asset, we can see that the net rate base has been brought to zero – the
6 book balance has been removed from plant, the tax loss has been realized, and the
7 ADIT on the difference between the net book and net tax has been reversed.

8 Now assume that the Commission allows for the recovery of the net book balance
9 of \$100 by establishing a regulatory asset. See Line 11. The accounting for that
10 would be as follows: Instead of posting the book loss to the income statement, the
11 loss would be directed to a regulatory asset of \$100. However, this does not
12 happen for tax purposes. The tax laws have no allowance to divert tax loss on the
13 retirement to a future period. As a result, the creation of the regulatory asset will
14 cause the creation of a new ADIT for the new timing difference, in the amount of
15 \$21 (the net book amount of \$100 multiplied by the tax rate of 21%). In addition,
16 the tax loss will create a benefit in current taxes and taxes payable of \$5.25 (tax
17 loss of \$25 multiplied by the tax rate of 21%).

18 This leaves a regulatory asset of \$100, ADIT of \$21, and current tax payable
19 (benefit) of \$5.25 – for a net impact to the balance sheet of \$84.75. See Line 13.

20 This is the essentially the same place that we started before the retirement and is
21 the expected outcome.

1 **Q. What lessons would you draw from this example?**

2 A. There are three important things that this example illustrates: First, it is
3 imperative that the Commission approve the recovery of the net book balance of
4 the plant. In the example, it is \$100. That recovery should never be netted
5 against a tax – either current or deferred. The taxes will be applied *as a result* of
6 the underlying activity (e.g. a retirement followed by a regulatory asset). Focus
7 on the gross activity, and the tax will follow.

8 Second, once the retirement is posted – for tax – the whole balance will have been
9 recovered. There will be no additional or future tax deductions on the tax return
10 for this asset – regardless of the Commission’s decision to allow recovery for the
11 regulatory asset. The regulatory asset will, itself, become a new book/tax timing
12 difference.

13 Third, over time, deferred taxes reverse. This is because they are based on timing
14 differences. They reverse as the underlying timing differences reverse.

15 Consequently, deferred taxes should not be included in the regulatory asset. The
16 regulatory asset needs to capture the net unrecovered book basis of the plant.

17 This is true even though the ADIT is reflected in the net rate base calculation.

18 The net rate base amount should not be confused with the balance of the
19 regulatory asset.

20 **Q. What is the import of this example to the Colstrip retirement?**

21 A. While the Colstrip retirement is not as clean as the example above, the results are
22 very similar. I hope to anchor the expected results back to the simple example to

1 show how this contrasts significantly from what Mr. Mullins proposes in his
2 testimony.

3 The key differences between the example and Colstrip is that the Colstrip ADIT
4 was not recorded at 21% as most of it occurred pre-tax reform. The imbedded,
5 blended ADIT rate is about 35%. As a result, there are some excess deferred
6 income taxes (“EDIT”) to deal with.

7 **Q. How does Mr. Mullins analysis differ from the proper treatment?**

8 A. On Table 3, BGM-1T, Mr. Mullins attempts to calculate the unrecovered
9 investment. He errs in confusing the unrecovered investment with the net rate
10 base. They are not the same thing. As I noted in my example above, the
11 retirement of the plant causes the reversal of the ADIT. However, the reversal of
12 the ADIT does not result in more or less unrecovered plant. At Table 3, line 3,
13 Mr. Mullins shows \$32.2 million less of unrecovered plant due to his application
14 of ADIT.

15 In addition, he portrays the ADIT and the EDIT at opposite signs in his
16 calculation. This was the result of a flipped-sign on PSE’s original Response to
17 AWEC Data Request No. 38, which has since been corrected with a revised
18 response. This is discussed in the rebuttal testimony of Ms. Free and in her Exh.
19 SEF-29. The ADIT and the EDIT are the same sign, and they are deferred tax
20 liabilities (“DTL”).

21 Regardless of the sign of the ADIT (whether it is a deferred tax asset (“DTA”) or
22 a DTL), it needs to be used correctly in determining the regulatory asset and in

1 setting rates. The ADIT should not be included in determining the regulatory
2 asset, but it should be included in rate base.

3 **Q. How did Mr. Mullins calculate his EDIT?**

4 A. The math he used is perplexing. In reviewing the equations in his spreadsheets,
5 he multiplies the ADIT by 0.14. This calculation is illogical. The ADIT balance
6 was amassed over many years based on applying a tax rate (most commonly 35%)
7 to timing differences in the year that they occurred. So, while 0.14 is the
8 mathematical difference between the old tax rate of 35% and the new rate of 21%,
9 it would be incorrect to apply 0.14 to an ADIT that has already been multiplied by
10 a tax rate.

11 The actual EDIT balance is \$11,501,867, as shown in PSE's workpaper.²

12 **Q. How did Mr. Mullins use EDIT in his analysis?**

13 A. This is important, and it highlights a difference between the simple example and
14 how Colstrip Units 1 and 2 EDIT must be treated. The simple example I provided
15 did not have EDIT. The tax regulations lay out the treatment of EDIT when an
16 asset becomes "deregulated", "whether by disposition, deregulation, or otherwise"
17 as follows

18 the reduction in the taxpayer's excess tax reserve [...] is equal to the
19 amount by which the reserve could be reduced under that provision
20 if all such property had remained public utility property of the

² See PSE Response to WUTC Data Request No. 164_Rev-Supp_01_Attach A (C).xlsx", tab "ADIT".

1 taxpayer and the taxpayer had continued use of its normalization
2 method of accounting with respect to such property.³

3 In other words, a taxpayer must continue to reverse its EDIT as if the retirement
4 had not occurred (i.e. as “if all such property had remained public utility property
5 of the taxpayer”). In the case of Colstrip Units 1 and 2, the EDIT will continue to
6 reverse over its remaining life (approximately seven years) as if no retirement had
7 occurred.

8 This is an unusual result and completely contrary to Mr. Mullins desire to apply
9 the EDIT balance to the unrecovered plant.

10 As an additional note, the Treasury Regulation cited above specifically refers to
11 the Tax Reform Act of 1986. This Regulation was issued in 2008. Prior to its
12 issuance, the IRS had disallowed all return of the EDIT balance when a plant
13 became “deregulated”. By adopting the Regulation, the IRS moved the treatment
14 of EDIT on plant balances closer to the treatment of EDIT on investment tax
15 credit (“ITC”) balances. Prior to 2008, they had been treated differently. The IRS
16 adopted the regulation as there is no logical reason for the two to be treated
17 differently.

³ Treasury Regulation 1.168(i)-3(b).

1 **Q. Is it possible that the IRS would not apply this rule to the Tax Cuts and Jobs**
2 **Act (“TCJA”), thus creating a difference in treatment between tax reform in**
3 **1986 and 2017?**

4 A. This result would be highly unlikely. I am not aware of anyone advocating for
5 this result.

6 Whether the IRS extends the Regulation to cover TCJA or revokes it for TCJA,
7 Mr. Mullins’s proposal would not be permitted. Clearly, his approach is not
8 permitted under the Regulation nor was it permitted prior to the Regulation. See
9 for example, Private Letter Ruling 200632017,⁴ where the IRS disallowed the
10 offset of EDIT against the PSE’s loss on the sale of its Centralia Plant in May
11 2000. This PLR was issued to PSE prior to the 2008 regulation.

12 For the correct handling of the EDIT balance, see PSE’s corrections to the
13 Mullins proposal in Exhibit No. SEF-29.

14 **B. The Proper Treatment of Production Tax Credits**

15 **Q. Can you summarize what Mr. Mullins is proposing as it relates to the**
16 **monetization of the PTCs?**

17 A. Mr. Mullins’ proposal with respect to the use of PTCs is inconsistent with prior
18 Commission orders and settlements addressing how and when PTCs may be
19 utilized. The existing approach is clear and was crafted to address issues that

⁴ See Marcelia, Exh. MRM-12.

1 arose in the past and will arise in the future if we deviate from the established
2 policy.

3 **Q. What settled history are you referring to?**

4 A. The treatment of the PTCs has been crafted to specifically address the issues that
5 appeared when PSE tried to pass the benefit of these tax credits to customers
6 before the PTCs could be used on PSE’s tax returns. Here is a quick recap of that
7 history.

8 Originally, from about 2005 through 2010, customers were given the benefit of
9 the PTCs at the time the PTCs were generated. However, due to the enactment
10 and continual renewal of bonus depreciation, PSE could not use the PTCs on its
11 tax return because it had tax losses. Thus, PSE was accumulating a large
12 regulatory asset because it was passing along a tax benefit for which it had
13 received no benefit from the IRS. Further, PSE was charging customers for the
14 carrying costs of that regulatory asset.

15 In late 2010, due to the size of the regulatory asset and significant accruals for the
16 carrying charges, the Commission approved the Company’s unopposed request⁵
17 to change the accounting and give customers the benefit of the PTCs once the
18 amount utilized became known. This can only occur once the annual tax return
19 has been filed.

⁵ See Docket UE-050870, Order 06 ¶¶ 2-8 (referencing revisions to Schedule 95A, the PTC tracker that would be granted in a “no action” agenda item on December 30, 2010 in Docket UE-101767 because the proposal was fair and uncontroversial). See also Docket UE-101581; Docket UE-091703, Order 02; Docket UE-101581, Order 01.

1 **Q. What was the result of this policy?**

2 A. The result of the policy was to shift the timing for providing customers the benefit
3 of the PTC from the time the PTCs were generated to the filing of the tax return.

4 **Q. Why did the benefits of the PTCs shift to the filing of the tax return?**

5 A. The timing of the PTC benefit was centered on the filing of the tax return because
6 taxable income is difficult to estimate accurately. But once the tax return is filed,
7 it is known. Taxable income is the basis on which the income tax is calculated.
8 The PTCs are then used to reduce the tax.

9 **Q. Why is taxable income difficult to estimate accurately?**

10 A. Taxable income is difficult to estimate accurately because so many things that
11 occur in the day-to-day operations of a utility can cause significant swings in the
12 amount of taxes that would be currently payable. For example, if a big storm
13 occurs, those costs will be deductible for tax purposes, while those same costs
14 will be recorded to a regulatory asset for regulatory purposes. The large tax
15 deduction could significantly lower the company's estimate of taxes payable for
16 the year, or it could even eliminate that amount of taxes payable. In either case,
17 an unexpected storm would throw the forecasted taxes payable, and the forecast
18 of PTC utilization, into disarray.

19 The other issue is one that occurred on a near-annual basis in the bonus
20 depreciation era – Congress would change the tax laws late in the tax year

1 (sometimes in late December). This nearly always throws the tax forecast into
2 disarray as it is impossible to predict tax law changes with any level of certainty.

3 **Q. How does the current policy regarding the use of PTCs confront these issues?**

4 A. The current policy does not make the underlying issues go away – meaning that
5 storms and other events still happen during the year and Congress still changes
6 the tax laws almost on a whim. But the current PTC policy makes all of this
7 invisible and not impactful to customers. That is why the parties agreed to change
8 the timing of the PTC accounting to provide customers the credits when the PTCs
9 are used on the Company’s annual tax return. This is the definition of “utilized”
10 or “monetized” that has governed when PTC benefits are provided to customers
11 since Schedule 95A was revised in 2010.

12 **Q. How would you sum up Mr. Mullins’ “monetization” scheme?**

13 A. Mr. Mullins wants to change the longstanding meaning of the term “monetized”
14 from (a) the amount of PTC used on PSE’s tax return to (b) the amount of PTC
15 PSE *estimates* that it will use on its tax return. Those can be two very different
16 numbers for the reasons I have explained above.

17 **Q. Does PSE estimate its quarterly tax payments?**

18 A. Yes, each quarter, PSE is required to estimate its quarterly tax payment.

1 **Q. Does PSE make accurate estimates of its quarterly tax payments?**

2 A. PSE tries to be as accurate as possible when it estimates its quarterly tax
3 payments.

4 **Q. Does PSE reduce its quarterly tax payments by the amount of PTCs that it
5 expects to use for the year?**

6 A. Yes, the quarterly tax payment is reduced by the amount of PTCs that PSE thinks
7 it will use.

8 **Q. Should PSE consider the amount of PTCs that it estimates it will use each
9 quarter as if those PTCs were monetized, as Mr. Mullins suggests?**

10 A. No. The fact that (a) PSE makes quarterly estimates and that (b) it thinks those
11 estimates are accurate misses the point. The issue is, in the case of PTCs, that
12 even the best estimate is in jeopardy of significant modification due to operating
13 activities or changes in tax laws. Mr. Mullins would revert to the situation that
14 existing in 2005 through 2010 when PSE was passing back PTCs before it had
15 utilized the PTCs on its tax return (i.e. monetized).

16 **Q. How frequently does PSE update its tax estimates?**

17 A. PSE prepares monthly tax provisions. In each monthly provision, PSE is
18 estimating and changing its forecast of taxable income. The numbers are fluid. In
19 fact, the amount of taxable income continues to change until the tax return is filed.

1 **Q. When does the amount of the PTC become fixed?**

2 A. I would describe the amount of the PTC as “fixed” when the Company files its tax
3 return. The filing of the tax return is the time when the Company knows what its
4 taxable income is and how many PTCs it will use. At that time, the PTCs are
5 “monetized” as credits on its tax return, which is the time when the benefit should
6 be used to offset the unrecovered plant balances.

7 **Q. What would happen if PSE gives back too much of the PTCs to customers
8 because it is relying on the quarterly tax estimates?**

9 A. It might be helpful to consider what would happen if PTCs that were used in the
10 quarterly tax estimate needed to be “reclaimed” because fewer PTCs were used on
11 the tax return. In that situation, accounting entries would increase the cost of the
12 unrecovered regulatory asset, including carrying costs on the monetized PTC
13 balance, because PSE’s taxable income was a lower number on the tax return than
14 estimated. It is counterintuitive to see the lack of taxable income causing an
15 increase in the amount of unrecovered plant – but that is what would happen
16 under the policy Mr. Mullins advocates.

17 **Q. Why does Mr. Mullins try to change the policy?**

18 A. Mr. Mullins wants a different policy because he wants to get the benefit of the
19 PTCs to offset unrecovered plant more quickly than was contemplated in the
20 settlement and more quickly than is currently possible. However, as discussed
21 above, PSE tried that policy once before, and the results were unpalatable for PSE
22 and customers. The prospect of increasing the Colstrip unrecovered regulatory

1 asset for the PTCs and their carrying costs that were prematurely used to offset
2 the plant balance is not an outcome PSE or its customers would want to see.

3 **Q. Do you have any example of other taxes that are effectively treated like you**
4 **treat the benefit of the PTCs?**

5 A. Yes. PSE recovers its property taxes only after the tax bills have been received.

6 **Q. Does PSE make estimates of its property tax bills?**

7 A. Yes. Just like with income taxes, PSE makes monthly estimates of its property
8 taxes. Those estimates are fluid and change throughout the year. The final
9 property tax amount is not final until PSE receives the bills from the assessors.

10 This is parallel to the current process with PTCs – the final amount is not known
11 until the annual tax return is filed.

12 **Q. What does Mr. Mullins propose for PTCs on Colstrip 3 and 4?**

13 A. For Colstrip 3 and 4, his proposal ignores the 2017 general rate case settlement,
14 recycles his pre-settlement testimony from the 2017 general rate case,⁶ and drops
15 all pretense of “monetization.” He would use the entire remaining PTC balance
16 immediately to lower depreciation expense.

17 **Q. What is wrong with this approach?**

18 A. There are two problems with this approach. First, the proposal contravenes the
19 2017 general rate case settlement agreement. Rather than waiting until Colstrip

⁶ Dockets UE-170033 & UG-170034; Mullins, Exh. BGM-1CT at 35:3-11.

1 Units 3 and 4 are retired and there are regulatory assets for unrecovered plant
2 balances, Mr. Mullins would apply the PTCs to lower the depreciation expense
3 for these operating units. Second, he fails to appreciate why “monetization” is
4 required before a benefit is created.

5 **Q. How does Mr. Mullins’ approach contravene the 2017 general rate case**
6 **settlement?**

7 A. The 2017 general rate case settlement agreement, to which AWEC is a party,
8 requires PSE to place PTCs as they are monetized in an account and, among other
9 things, to use these monetized PTCs to offset unrecovered plant balances for
10 Colstrip Units 1 through 4.⁷ The settlement agreement also makes clear, what
11 should otherwise be obvious, that unrecovered plant balances apply to retired
12 plant not to the depreciation on operating plants: “*At closure of Units 1 and 2,*
13 *PSE shall offset all additional unrecovered plant balances for Colstrip Units 1 and*
14 *2 with monetized production tax credits.*”⁸ Mr. Mullins’ proposal ignores this
15 settlement term and recycles his argument from the 2017 general rate case (before
16 the 2017 general rate case settlement was entered into) in which he proposed
17 using PTCs to offset depreciation on Colstrip Units 3 and 4.

18 **Q. Why is monetization required before a benefit is created?**

19 A. As previously discussed, if the PTC is not used on a tax return, there is no benefit
20 to offset the unrecovered plant balance. Under the terms of the 2017 general rate

⁷ Docket UE-170033, Settlement Stipulation and Agreement, Paragraph 117.

⁸ *Id.*, paragraph 25 (emphasis added).

1 case settlement, PSE is at risk for the “monetization” to occur before December
2 31, 2029. In fairness, Mr. Mullins needs to allow PSE the opportunity to achieve
3 that monetization before he creates a benefit out of thin air.

4 **Q. Can you clarify when PTCs should be applied to the balance of unrecovered**
5 **plant?**

6 A. Yes, the monetized PTCs should be applied to the balance of unrecovered plant as
7 soon as there is an amount recorded to a regulatory asset for unrecovered plant.
8 Until that time, the monetized PTCs should remain in their own account,
9 accumulating interest. As discussed by Ms. Free, there is no regulatory asset for
10 unrecovered plant that is known and measurable for purposes of rate setting in
11 this rate case.

12 The benefit for PTCs that have not yet been monetized should remain in a
13 separate account until such time as they are utilized on PSE’s tax return (i.e. they
14 become monetized). Until that time, they do not accrue interest. This is how PSE
15 is accounting for these balances today, consistent with the intent of the 2017
16 general rate case settlement.

17 **Q. How should the PTCs affect book depreciation?**

18 A. Book depreciation should continue at its approved rate until the Colstrip units are
19 retired. Under the 2017 general rate case settlement, the benefit for PTCs will be
20 used to offset unrecovered plant balances. The unrecovered plant balance is
21 determined at the time the plant is retired. The settlement does not allow for the
22 offset of the plant costs prior to its retirement. This means that book depreciation

1 should continue to be recorded into its accumulated reserve and that the
2 monetized PTC should not be applied against the balance until the plant is retired
3 and the regulatory asset for unrecovered plant is recorded.

4 **Q. Can you summarize your testimony on PTCs?**

5 A. Yes, for Colstrip Units 1 and 2, Mr. Mullins proposes to rewrite the definition of
6 “monetized” PTCs. Doing so would be ill-advised for the reasons I offer above.
7 For Colstrip Units 3 and 4, he would drop the concept of monetization entirely in
8 favor of straight amortization. However, without some form of monetization,
9 there is no benefit to amortize. Further, he proposes to apply the PTCs to Colstrip
10 plant before it is retired; he disregards the 2017 general rate case settlement
11 language that requires monetized PTCs to be applied to Colstrip unrecovered
12 plant balances. Both proposals should be rejected.

13 **Q. Is there anything else to point out on Mr. Mullins’ testimony on the PTCs?**

14 A. Yes, it is a small point, but one that bears mentioning. Mr. Mullins states that
15 “Puget [i.e. PSE] reduced the balance for production tax credits utilized in Puget
16 Energy’s September 30, 2019 tax provision”⁹ It is important to point out that
17 PSE calculates its use of PTCs based on its own taxable income. PSE’s estimates
18 do not include the taxable income or loss of any other company. *Puget Energy’s*
19 tax provision has no influence on the PTCs used in *PSE’s* tax provision.

⁹ Mullins, Exh. BGM-1T at 13:7-9.

1 **III. REVERSAL OF EXCESS DEFERRED INCOME TAXES**

2 **A. Overview**

3 **Q. From your perspective, what is causing the difference in treatment of EDIT**
4 **between PSE and the intervenors?**

5 A. I believe there is a fundamental misunderstanding of the rules for EDIT and the
6 associated reversal under the Average Rate Assumption Method (“ARAM”). The
7 ARAM rules represent the maximum speed by which EDIT can be reversed. The
8 speed limit applies to the timing of the debits and credits which must be recorded
9 in order for the reversal to happen. This reversal is an accounting issue. As I
10 mentioned in my original testimony, the normalization rules require the proper
11 accounting.

12 **Q. What is required for the proper accounting?**

13 A. The proper accounting requires that the four components of normalization be in
14 sync (i.e. the normalization consistency rules apply): rate base, ADIT, book
15 depreciation, and tax expense. Book depreciation is of special importance when
16 discussing ARAM as book depreciation causes deferred taxes to reverse. Recall
17 that ADIT (including the EDIT component) does not begin to reverse until book
18 depreciation is greater than tax depreciation.

19 **Q. How does PSE account for the EDIT reversal?**

20 A. The journal entry to reverse the EDIT is to debit the ADIT for the EDIT reversal
21 and to credit (benefit) deferred tax expense.

1 For example, assuming that \$100 represents the ARAM amount:

2 Debit FERC 282 Deferred Tax Liability \$100
3 Credit FERC 411 Deferred Tax Expense (benefit) (\$100)
4

5 However, this entry by itself does not provide the last word on whether or not
6 PSE has complied with the normalization rules.

7 **Q. If the accounting is correct, haven't you met the normalization requirement?**

8 A. No. One of the purposes of the normalization rules is to protect the government's
9 tax revenues.¹⁰ If the normalization rules stop with the proper accounting, they
10 would be entirely ineffective to execute the congressional intent for which they
11 were created.

12 The language in the TCJA states as much: Normalization is required by a utility
13 "in computing its cost of service for ratemaking purposes and reflecting operating
14 results in its regulated books of account".¹¹ Normalization is required both for
15 ratemaking and accounting.

16 Once the balance sheet (ADIT) and the income statement (tax expense)
17 accounting entries have been recorded, those accounts roll into PSE's usual
18 ratemaking structures: Historical test year plus or minus a few pro forma or
19 restating adjustments for cost of service with rate base valued based on either the
20 average of the monthly averages ("AMA") or end of period ("EOP") basis. In the
21 setting of rates, the normalization rules must also apply throughout.

¹⁰ Rev. Proc. 2017-47, section 1.01; *see* Steward, Exh. CSS-2 at 2.

¹¹ TCJA, Section 13001(d)(1); Marcelia, Exh. MRM-06.

1 **Q. Are there exceptions to the normalization rules for EDIT?**

2 A. Nothing in the normalization law, regulations, or private letter rulings (“PLRs”)
3 would suggest an exception for the EDIT component in tax expense. Tax expense
4 reflects the usual movement in deferred taxes including EDIT reversals. The
5 normalization rules apply to all tax expense (including the EDIT reversal). The
6 intervenors in this case have incorrectly assumed that once EDIT has been
7 reversed via ARAM, there are no additional normalization rules to follow. That is
8 not the case. The fact that ARAM applies to the reversal of EDIT does not mean
9 that it is the *only* normalization rule that applies to EDIT. All other normalization
10 rules continue to apply. In this way, congressional intent is achieved as it relates
11 to the EDIT.

12 It is interesting to note, and it is not just coincidental, that the effect of ARAM is
13 to reverse the EDIT over the remaining book life of the asset. This is the same
14 period over which the ADIT reverses.

15 **Q. Can you elaborate on your statement that reversals under ARAM are at the**
16 **same speed as non-excess ADIT reverses?**

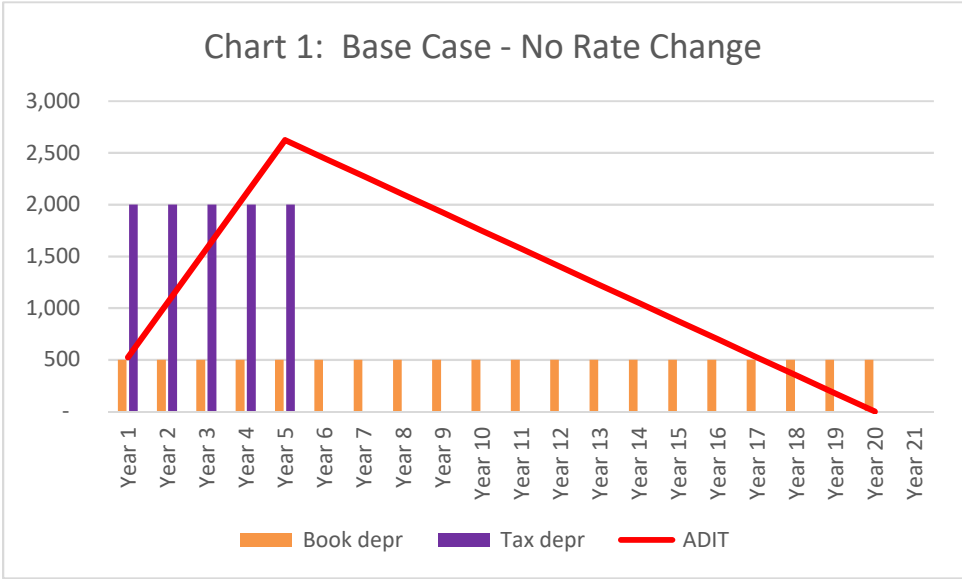
17 A. Yes. ARAM represents the same speed of reversal of EDIT at which the non-
18 excess ADIT will be reversed. This is why Congress developed the ARAM
19 methodology – it preserves the original (pre-tax reform) reversal pattern of the
20 entire ADIT balance whether it is excess or not.

21 I have prepared a chart, below, which demonstrates this point. I have created a
22 very simple example to illustrate how the EDIT and the ARAM are related and

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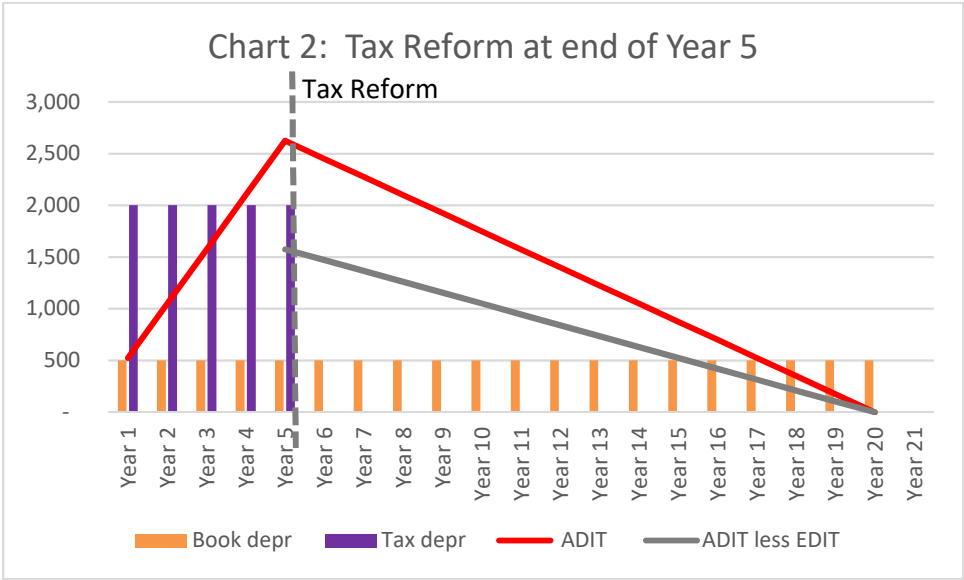
how they result in the same reversal of deferred taxes as if tax reform did not occur. In this example, I'm using an asset with a cost of \$10,000, which has a book life of 20 years with straight-line depreciation and has a tax life of 5 years with straight-line depreciation.

With that foundation, Chart 1 shows the normal, pre-tax reform creation and reversal of the ensuing deferred taxes (ADIT). There is no tax reform and the tax rate remains at 35% throughout the creation and reversal of the ADIT. Observe how the ADIT grows until tax depreciation stops, which is Year 5 in this example. The book depreciation continues and it is the annual book depreciation expense that causes the ADIT to reverse.



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1 In Chart 2, I introduce tax reform just after the asset enters into its reversal
 2 phase¹² in Year 5 which occurs once tax depreciation stops. Notice that the total
 3 ADIT (the red line) is equal to the ADIT from Chart 1 in each period. The EDIT
 4 is the difference between the red line (ADIT) and the grey line (ADIT less EDIT).
 5 When the tax rate changes the EDIT is created, but it is still a part of the deferred
 6 tax balance.



7
 8 In each year after the rate change, the reversing deferred tax expense will have
 9 two components: (a) the reversal of the normal deferred tax balance at 21% and
 10 (b) the reversal of the excess deferred tax at the ARAM rate. The combination of
 11 the two will result in the deferred tax reversing at 35%, as if the tax rate change

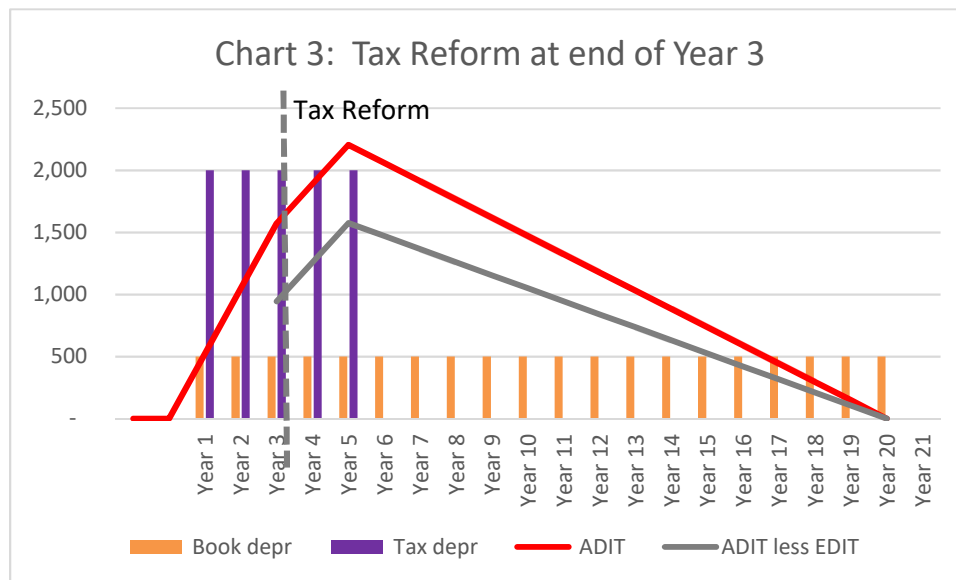
¹² The “reversal phase” of the asset begins when the annual book depreciation of the asset is greater than the annual tax depreciation of the asset. When this happens, the ADIT balance begins to decline (i.e. reverse). Usually, this occurs once the asset becomes fully depreciated for tax purposes. In my example, it occurs when the asset enters Year 6. At the end of Year 5, the asset is fully depreciated for tax, but there are still a number of years to go on the book life.

1 had not occurred. The ADIT in Chart 2 (the red line) has the same downward
2 slope (reversal rate) as the ADIT in Chart 1.

3 These charts visually illustrate one of the key points: The annual book
4 depreciation is causing the ADIT, along with the EDIT to reverse over the
5 identical time period, at the same rate.

6 **Q. Does the result change if the tax rate changes (i.e. tax reform) occurs earlier
7 or later in the life of the asset?**

8 A. In Chart 3, I provide an example which show how the EDIT reversal pattern
9 works when tax reform occurs *before* an asset reaches its reversal point, which is
10 when the book depreciation becomes greater than the tax depreciation.

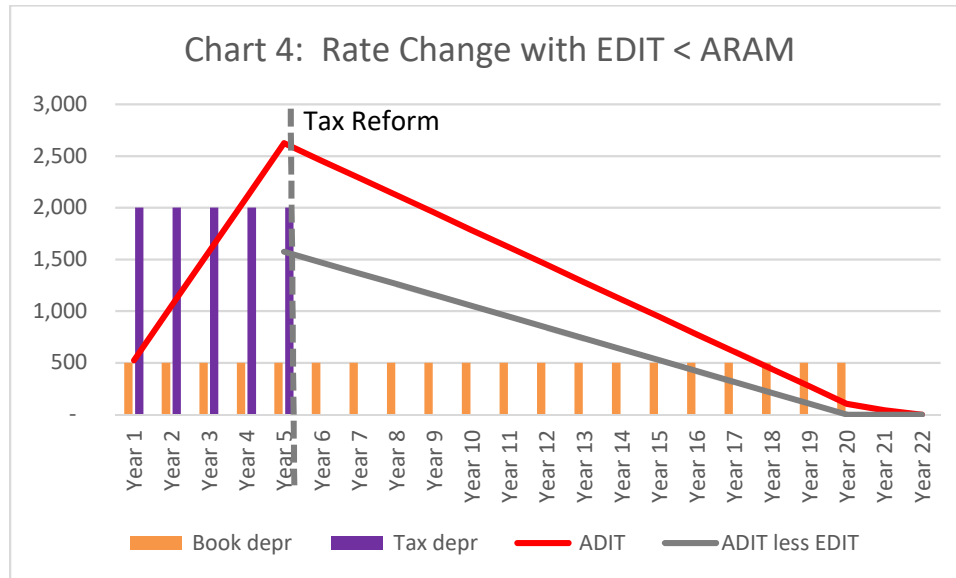


11
12 This example shows tax reform occurring in Year 3 which is two years prior to
13 the asset entering its reversal phase. When tax reform occurs, the amount of
14 “excess” becomes locked – no new “excess” is created in Year 4 or 5 as the ADIT

1 that is recorded in those years is being recorded at the new, lower tax rate. As in
2 the earlier charts, the asset will begin to reverse in Year 6. Whatever “excess”
3 was accumulated before tax reform will be reversed over the remaining book life
4 under ARAM. Thus, that “excess” will reverse in the same future period that it
5 would have reversed in as if tax reform has not happened.

6 **Q. What if the utility is not using the full ARAM rate?**

7 A. In my final chart, Chart 4, I demonstrate the effect of reversing the EDIT more
8 slowly than the ARAM rate as Mr. Mullins and Mr. Garrett seem to prefer. This
9 has the effect of reversing the deferred tax over a period that is *longer* than the
10 book life of the asset. In Chart 4, the ADIT is not fully reversed by the end of
11 Year 20, which is the end of the assets book life, because the EDIT is reversing
12 slower than ARAM allows. This causes the reversal to drag on for an extra year.
13 This is an undesirable consequence. Congress allows this as the result is better
14 for the U.S. Treasury, but it is detrimental to customers. I would not recommend
15 this.



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Q. Can you elaborate on the ARAM “speed limit”?

A. Yes, consider the example of a normal speed limit: If you need to travel 60 miles and the speed limit is 60 miles per hour (“MPH”), the journey will take one hour. Now if you travel for the first half-hour at 45 MPH (slower than the 60 MPH speed limit), you will be unable to complete your journey in one hour. This raises a key point: The 60 MPH speed limit still applies for the second half of the trip. You are NOT given a free pass to travel at, say, 75 MPH for the second half of your trip to “make up” for going slower. The speed limit remains 60 MPH and you do not get to violate that speed limit simply because you did not maximize your speed earlier. This is very important to remember when considering the ARAM speed limit. Underrunning that speed limit in the early years does not create freedom in the later years. The speed limit applies in the later year, just like in the earlier years.

1 **Q. What do these charts illustrate?**

2 A. These charts illustrate a couple of things. First, they show what it looks like when
3 a normalization method of *accounting* is followed. It is actually very
4 unremarkable. Book and tax depreciation are recorded when they occur. The
5 difference is recorded to deferred taxes in the same period.

6 Second, the ratemaking implications are not shown on the charts but we can easily
7 see how it would work. Using Chart 2, assume that Year 6 is the historical test
8 year for ratemaking purposes. The test year has \$500 of book depreciation
9 expense, no tax expense. The deferred tax reversal would be \$105 of normal
10 deferred tax ($\$500 \times 21\%$) and \$70 of excess (because the deferred tax was
11 accrued at 35%) for a total deferred tax reversal of \$175. At the end of Year 6,
12 the net book basis of the asset would be \$7,000, the net tax basis would be zero,
13 and the ADIT would be \$2,450 (liability), which includes the remaining EDIT
14 balance of \$980. Those would be the accounting entries and related balances that
15 would be present in the Year 6 test year.

16 **Q. How would rates be set in this example?**

17 A. The end of period rate base would include the plant balance of \$7,000 less the
18 ADIT of \$2,450.

19 The cost of service would show book depreciation expense of \$500 offset by
20 deferred taxes of \$175 – which is the amount of reversing ADIT (inclusive of the
21 EDIT component). Both of these are components of the historical test year.

22 Based on these results and assuming the normal 16-month timeline for the

1 preparation, filing, and completion of a GRC, the new rates based on Year 6 test
2 year would go into effect sometime in Year 8. Those rates would continue until a
3 new GRC is filed.

4 In this way, the normalization rules are followed. The accounting is proper, and
5 the ratemaking is proper.

6 **Q. What happens if a different approach for reversing EDIT is used for**
7 **ratemaking?**

8 A. If we try to do something different with the reversing EDIT (the \$70 in this
9 example) when setting rates, we end up breaking the linkage between each of the
10 items of normalization. For example, if we try to defer the \$70 of EDIT for a
11 later day after accounting for it correctly, there would be a consequence to tax
12 expense, book depreciation, rate base and ADIT. The normalization rules do not
13 stop with good *accounting*. They extend to the rate setting, as well.

14 **Q. Has the IRS applied this approach in the past to differentiate between the**
15 **accounting and the ratemaking of an item?**

16 A. Yes. This approach can be seen in PSE's PLR 200824001, which addresses using
17 AMA rate base versus EOP rate base. PSE had the proper accounting in place.
18 The ADIT balances were reversing (and accruing) according to the proper
19 accounting rules and time periods. They were properly matched to rate base,
20 book depreciation expense, and tax expense (i.e. the consistency rule was met).
21 However, the ratemaking treatment at the time of the PLR was to have only the
22 ADIT component of rate base reflected at EOP values, and everything else

1 (including plant assets and accumulated book depreciation) at AMA. As a result,
2 if proper accounting were the only normalization requirement – without regard to
3 the rate making treatment – PSE would have been free to apply any ratemaking
4 technique available to pass the impact of those accounting entries back to
5 customers – including valuing ADIT in rate base differently than the underlying
6 book plant and depreciation to which it relates. However, that was not the case.

7 The IRS ruled that PSE could not use the EOP ADIT to offset AMA plant related
8 rate base in setting rates. Consistent treatment is required in ratemaking. EOP
9 versus AMA has nothing to do with accounting and is entirely a ratemaking issue.
10 This ratemaking sits on top of the proper accounting. But as I’ve demonstrated,
11 the accounting *and* the ratemaking matter for normalization. You cannot have
12 compliance with normalization if you have only one but not the other. That is one
13 of the lessons from PSE’s PLR 200824001.

14 **Q. How did PSE establish its position on EDIT?**

15 A. In establishing its position on the treatment of EDIT, PSE has been exceedingly
16 careful and diligent to apply the law as it exists today. At each step, PSE has
17 carefully reviewed its approach to ensure conformity with the law, the
18 regulations, its own PLR, and the other PLRs on normalization within the context
19 of Washington regulation. This diligence was especially necessary in light of the
20 additional penalty Congress added with the TCJA.¹³ At each step, PSE has
21 demonstrated how its approach affirmatively complies with the rules.

¹³ See Marcelia, Exh. MRM-1T at 24:3–11.

1 **Q. Does PSE believe that its approach is the only correct approach?**

2 A. No. PSE's approach is tailored to ratemaking in Washington and matches the
3 positions it has taken in other parts of its GRC. Other utilities in other jurisdiction
4 have alternative ratemaking techniques that they would need to reflect in their
5 approach. The normalization rules are common across all utilities and all
6 jurisdictions, and they apply to everyone.

7 What is important is that PSE can (and has) demonstrated that its approach
8 complies with the normalization rules.

9 **Q. Do you agree with Public Counsel witness Mark Garrett that once EDIT has**
10 **been amortized (or reversed) under ARAM, those balances become**
11 **unprotected?**¹⁴

12 A. No. I think his misunderstanding stems from a misreading of the ARAM rule.
13 The ARAM rule speaks to the methodology to reverse the EDIT over the
14 remaining book life of the asset. This only controls the speed with which the
15 reversal can be posted to the balance sheet (ADIT) and the income statement (tax
16 expense). It does not replace all of the normalization rules.

17 As a result, the amortized balances do not become "unprotected". To the
18 contrary, they maintain their character, which is subject to normalization,
19 throughout the ratemaking process.¹⁵

¹⁴ Garrett, Exh. MEG-1T at 55:18-21.

¹⁵ See PLR 8920025 (Feb. 15, 1989). "Accordingly, all amounts previously deferred under corporate tax rates at 46 percent are part of a 'reserve to reflect the deferral of taxes' as

1 **Q. AWEC witness Bradley Mullins makes a distinction between the**
2 **“amortization” of EDIT and the “reversal” of EDIT. Does PSE agree with**
3 **his application of this distinction?**

4 A. Not at all. He uses “amortization” to describe the amounts that have been set in
5 rates (i.e. the ratemaking) and “reversal” to describe the amounts that were
6 recorded in the test period following ARAM (i.e. the accounting). The issue
7 arises with how he treats each item, as he would only apply normalization to the
8 “reversal” (i.e. the accounting). Then, he would switch tracts entirely when
9 setting rates. He would “amortize” the balances produced by ARAM into
10 customer rates. That is not how it works when rates are set using a historical test
11 year, as in the state of Washington. Instead, the EDIT reversal that occurred in
12 the test year and was included in tax expense must be matched with the book
13 depreciation expense that gave rise to it.

14 His approach raises two problems, both relating to consistency: First, the timing
15 becomes a problem. His ratemaking causes a mismatch between the book
16 depreciation that causes the EDIT to reverse in the historical period and the book
17 depreciation that occurs in a later period when he would “amortize” his balance –
18 the amortization of his balance would be recorded in a time period that does not
19 contain the underlying book depreciation that created the reversal, which creates a
20 mismatch in violation of the consistency provisions of the normalization rules.

described in sections 167(l)(2)(G)(ii) and 168(i)(9)(A)(ii), and become inseparable from the assets which initially gave rise to the deferral.” When the IRS says “all amounts previously deferred” that would include EDIT. It remains “inseparable from the asset”.

1 The key is that the reversing EDIT needs to be matched with the book
2 depreciation that is causing the EDIT to reverse in the historical period. Mr.
3 Mullins' approach fails that test.

4 Second, this is a clear instance of applying a unique rate making technique –
5 distinguishing between “amortization” and “reversal” – to EDIT (which is a sub-
6 component of ADIT) and not applying the same technique to book depreciation,
7 which is causing the EDIT to reverse. (It is not much different than the AMA
8 versus EOP issue in PSE’s PLR 200824001.) Further, to properly complete the
9 normalization cycle, Mr. Mullins would need to apply this logic (defer and
10 amortize) to rate base and the ADIT balance, in addition to book depreciation.

11 Consider what would happen if Mr. Mullins' approach is followed, which I do not
12 endorse because it is not how rates are usually set in the state of Washington.

13 However, if we were to apply Mr. Mullins' ratemaking construct to book
14 depreciation, PSE would have “reversals” of book depreciation of \$600.3 million
15 (e.g. the accounting) on its books during the test year, versus \$483.3 million of
16 “amortization” of book depreciation (e.g. in rates) during the test year. Thus, PSE
17 would need to collect that shortcoming of \$117.0 million¹⁶ over some time period
18 – four years in Mr. Mullins example. A similar calculation could be made for the
19 balances in rate base and ADIT. This is the sort of calculation that would be

¹⁶ See Free, Exh. SEF-1T at 9:14, Table 2; “NEW-PSE-WP-SEF-1T-Table-2-Explain-Deficiencies-TY2019GRC-06-2019.xlsx”, tab “Depreciation” (the combined result for electric and gas and workpaper).

1 necessary to implement Mr. Mullins arrangement and pass the consistency
2 provisions of the normalization rules.

3 The implication of this is not desirable and should not be pursued.

4 **B. PSE's Use of PLRs To Support Its Position**

5 **Q. Mr. Mullins and Mr. Garrett challenge PSE's use of PLRs in support of its
6 position. How would you respond?**

7 A. The PLRs I cited in my prefiled direct testimony are relevant and instructive.
8 However, both Mr. Mullins and Mr. Garrett dismiss the guidance in the PLRs that
9 I cited as either not germane to the issues in the TCJA or not applicable to PSE.
10 Clarification of a couple of issues may assist in explaining why and how each
11 PLR is relevant to PSE's GRC filing.

12 I'll start by elaborating on the role that PLRs play in the tax law. Mr. Garrett
13 takes up this issue at Exh. MEG-1T, 54:16-55:5. In theory, a PLR applies only to
14 the taxpayer to whom it was issued. In practice, taxpayers use PLRs as a window
15 through which to view the IRS's thinking on various issues. This is especially
16 true when considering the normalization rules. The existing body of PLRs is the
17 primary way to see how the IRS applies these rules. Further, because all utilities
18 follow FERC accounting, there is an added level of commonality when the IRS
19 issues a PLR to one utility, and utilities routinely use these to better understand
20 how the ruling might apply to a different, but similarly situated, utility.

1 With that background established, the three PLRs that I cite all bear on the issues
2 in this GRC. Each one specifically addresses the consistency component of the
3 normalization rules. I believe that when we boil down the differences between
4 PSE and intervenors, the issues come down to how the consistency rule applies to
5 the reversal of the EDIT in the interim period¹⁷. Each PLR speaks to that issue in
6 one way or another, and each PLR is in harmony with the others – in other words,
7 the message from the IRS on this topic is unwavering.

8 **Q. Please summarize the significance of PLR 8920025.**

9 A. PLR 8920025¹⁸ clarifies that, without doubt or ambiguity, the consistency rules
10 apply to EDIT. That ruling is foundational. The regulator in that ruling took the
11 position that the consistency rule did *not* apply to EDIT. The IRS ruled
12 otherwise. This ruling leaves no room for ambiguity. There is no reason to think
13 that that ruling would not apply to taxpayers today, including PSE in this GRC.

14 **Q. Please summarize the significance of PLR 200824001.**

15 A. PLR 200824001¹⁹ was issued to PSE to address the Company’s former
16 inconsistent use of the AMA rate base and EOP ADIT. This is an intimate
17 example of (a) PSE’s personal experience with the consistency rules and (b) how
18 otherwise valid ratemaking techniques can be deployed in such a way that the

¹⁷ I use the term “interim period” to refer to the period from January 1, 2018 through February 28, 2019 which is the time period for which PSE was recording the reversals of EDIT in its tax expense prior to the implementation of new rates from the 2018 ERF.

¹⁸ Attached as Exh. MRM-3 and discussed at Marcelia, Exh. MRM-1T at 18:21 – 20:5.

¹⁹ Attached as Exh. MRM-4 and discussed at Marcelia, Exh. MRM-1T at 20:17 – 21:4.

1 result is a normalization infraction. No one would dispute the usefulness of the
2 AMA or EOP methodology as either may be considered appropriate or
3 inappropriate depending on the setting. But the deployment of either
4 methodology must apply equally to the book and tax numbers that are subject to
5 the normalization rules.

6 **Q. Please summarize the significance of PLR 201828010.**

7 A. PLR 201828010²⁰ provides an example of the significance of the use of historical
8 test years and the consistent application of ratemaking methodologies. In that
9 case, the taxpayer used a historical test period with AMA for rate base and ADIT,
10 except for the results of an IRS settlement which occurred in the last month of the
11 AMA period that the commission wanted to include in-full. The IRS ruled that
12 the settlement was subject to AMA, just like the rest of the ADIT and rate base
13 balances.

14 **Q. How do you respond to the view of Mr. Mullins and Mr. Garrett that these**
15 **PLRs have no bearing on this case?**

16 A. I disagree with their viewpoint. These PLRs tell us that the consistency rules
17 apply to PSE's EDIT balance²¹, that the same ratemaking methodologies must be
18 applied consistently to the four components of normalization²², and that an

²⁰ Attached as Exh. MRM-5 and discussed at Marcelia, Exh. MRM-1T at 22:1 – 23:4. Note that when I cited this PLR in my initial testimony, I had a typo in the number. The correct reference is PLR 201828010 – there is an “8” in the sixth digit, not a “0”. The correct PLR was included at Exhibit MRM-5 in the original filing.

²¹ See PLR 8920025.

²² See PLR 200824001.

1 attempt to apply a unique ratemaking methodology to a subcomponent of ADIT
2 (whether an IRS settlement or the reversal of EDIT, both of which are
3 subcomponents of ADIT) is not acceptable under the normalization rules²³.

4 **Q. Is Mr. Mullins correct in asserting that you inferred from PLR 8920025 that**
5 **“any pro forma adjustment to EDFIT reversals calculated in the test period**
6 **would constitute a normalization violation”?**²⁴

7 A. No, that is not accurate. EDIT adjustments can be made provided that the
8 consistency rules are applied, and all four normalization factors (book
9 depreciation expense, rate base, ADIT, and tax expense) are addressed – which
10 neither Mr. Mullins or Mr. Garrett propose.

11 **C. Alignment with Commission Policy and Prior Orders**

12 **Q. Mr. Mullins and Mr. Garrett challenge PSE’s approach to reversing EDIT.**
13 **Is PSE’s approach inconsistent with the Commission’s policy?**

14 A. No. The Commission’s policy must be interpreted in light of the normalization
15 rules. From my observations, it is not, and has never been, the Commission’s
16 policy to issue rules or guidance that contravene the IRS normalization rules.
17 Nothing in the Commission press release addressing the implementation of TCJA
18 could be construed as an instruction to circumvent the normalization provisions.

²³ See PLR 201828010.

²⁴ Mullins, Exh. BGM-1T at 23:10-12.

1 In fact, the language of the Commission press release addressing TCJA
2 foreshadows PSE's exact approach:

3 Customers will not see immediate bill credits or reduced rates.
4 The utilities' expected tax savings must be determined and
5 reconciled with commission-set revenue requirements during
6 regular tariff and rate case filings.²⁵

7
8 In fact, that is precisely what has transpired. PSE was the first utility to lower its
9 rates for the change in tax rate from 35% to 21%. Then, in the 2018 expedited
10 rate filing in Dockets UE-180899 and UG-180900 ("2018 ERF"), PSE eliminated
11 what would have otherwise been a rate increase to electric customers and
12 significantly reduced a rate increase for gas customers by reversing EDIT in the
13 historical test year of the ERF, in a manner that complies with the IRS
14 consistency rules while allowing the annualized amount of EDIT reversal to be set
15 in rates.

16 **Q. Is the EDIT treatment in the 2018 ERF relevant to this GRC?**

17 A. Yes, contrary to Mr. Mullins statements²⁶, the EDIT treatment in the 2018 ERF is
18 relevant. In the 2018 ERF, PSE's approach is explained in detail; and its
19 approach in this GRC is nearly identical and just as compliant with the
20 normalization rules. Even though the parties to the 2018 ERF settlement agreed
21 to discuss the reversal of the interim EDIT further, which we are doing presently

²⁵ Press Release, WUTC, State regulators: Utilities must pass federal tax cut savings on to customers, (Jan. 8, 2018).

²⁶ Mullins, Exh. BGM-1T at 25:4-10.

1 in this GRC, the treatment of EDIT in the 2018 ERF is important as it lays the
2 foundation for the approach used in this filing.

3 **Q. Does PSE’s approach differ from what other utilities in Washington have**
4 **requested?**

5 A. Yes. There are two reasons for the difference. First, the fact patterns for PSE and
6 the other utilities are very different. Second, these other utilities do not address
7 the normalization consistency rules in their filings.

8 **Q. How are the fact patterns of these cases different than PSE’s case?**

9 A. In the Cascade Natural Gas (“Cascade”) general rate case, the Commission
10 rejected Cascade’s argument to apply the interim EDIT reversal against future
11 cost increases. Based on my reading of Order 06 in that proceeding, I believe the
12 Commission was correct in its determination on this point. In its general rate
13 case, Cascade was setting rates based on a historical test period that did not
14 include any EDIT reversals. In other words, the Commission was setting rates
15 that were fair, just, reasonable, and sufficient – and those rates did not include any
16 EDIT reversal. Then the TCJA comes along and causes a new benefit that
17 Cascade wanted to use to offset future cost increases. That is a fine theory, but it
18 is not how the Commission sets rates in Washington. It uses a historical test year
19 as its base.

20 Compare this to PSE: PSE’s situation was significantly different. (a) PSE’s rates
21 were not current as they had not just been reset in a rate proceeding which was
22 essentially adjudicated without consideration of tax reform. PSE had not just

1 completed a GRC. (b) In the 2018 ERF, PSE followed all Commission guidelines
2 and procedures to establish that it had actual, measurable, and verifiable costs that
3 would require a rate increase and that those costs were offset by the amount of
4 reversing EDIT (which was calculated using the same ratemaking processes and
5 techniques as required by normalization). The key difference between Cascade
6 and PSE was that PSE had actual, measurable, and verifiable costs that were
7 *historical* – not some future, unknowable, potential cost increase. Those
8 historical costs were offset with the historical EDIT reversal.

9 PSE’s approach in both the ERF and GRC is consistent with the Commission’s
10 general policy for setting rates based on historical activity and its press release on
11 reconciling the benefits of tax reform with the revenue requirement in rate case
12 filings.

13 **Q. How do PSE’s facts differ from Avista?**

14 A. Avista was in almost the same situation as Cascade. Avista was in the midst of a
15 GRC when tax reform was enacted. Based on a historical test year, which did not
16 include the reversal of EDIT, the parties settled on rates that were fair, just,
17 reasonable, and sufficient. They did not address what to do with the interim
18 reversal of EDIT as the EDIT played no role in the historical test year costs. In
19 the order, the Commission decided to have Avista refund it over future periods.
20 In Avista, there were no actual, measurable costs in the historical test year against
21 which the reversal of EDIT could be offset. This is a different situation than that
22 of PSE.

1 **Q. How about the NW Natural Gas order?**

2 A. NW Natural's situation appears to be different from Cascade and Avista. Based
3 on the publicly available information, it appears that NW Natural deferred their
4 reversing EDIT. As a result, the deferred income tax expense that they reported
5 in their test year would have been higher as it included no reversal of EDIT.
6 (Note: It is not possible to defer the EDIT and have it reducing tax expense at the
7 same time. At PSE, the reversing EDIT is reducing tax expense. At NW Natural,
8 it appears that they deferred it.) As a result, in setting rates in their GRC, before
9 considering the interim EDIT, NW Natural would have reported higher tax
10 expense, lower net operating income, and therefore requested a larger rate
11 increase.

12 PSE did not follow this approach. As mentioned above, PSE reduced its tax
13 expense, which increased its net operating income. Had it done so, PSE would
14 have requested a larger rate increases in the ERF. Mr. McGuire references this in
15 his testimony in the ERF.

16 **Q. What do you mean?**

17 A. At Exh. CRM-1T, 24:3-5, Mr. McGuire mischaracterizes the results of the 2018
18 ERF as an electric rate increase of \$25.9 million and a gas increase of \$27.6
19 million. The truth is buried in footnote 29 where he admits that these were not the
20 actual results. Instead, base rates for electric were *unchanged*, and gas rates
21 increased only \$21.5 million.

1 **Q. Why the difference between Mr. McGuire’s characterization versus the**
2 **actual terms of the settlement agreement?**

3 A. The difference is the EDIT reversals that occurred in the ERF. In the settlement,
4 PSE agreed to set the ERF rate change into two tariff schedules – Schedule 141X
5 to show the EDIT reversal separately and the remainder in base rates. PSE was
6 able to agree to this because Schedule 141X is treated in the same manner as base
7 rates – thus maintaining the required level of consistency between the ratemaking
8 treatment of reversing EDIT and the other components of normalization.

9 **Q. What does Mr. McGuire’s characterization prove?**

10 A. Mr. McGuire’s testimony demonstrates that PSE’s customers received the benefit
11 of the reversing EDIT in the historical test year.

12 **Q. You testified that the other Commission orders do not mention the**
13 **normalization consistency rules. Why is that important?**

14 A. Not one of the orders or any of the available testimonies in any of the above
15 general rate cases mention the normalization consistency rules. I only see
16 normalization mentioned in the context of following the ARAM reversal pattern,
17 i.e. the “speed limit”. As I’ve described earlier, there is much more to
18 normalization than ARAM.

19 In my direct testimony in this case, I have laid out in detail how PSE’s approach
20 complies with all of the normalization requirements.

1 **Q. Do the orders in these other general rate cases comply with the normalization**
2 **requirements, including consistency?**

3 A. Based on the available information, I do not believe they comply with the
4 normalization consistency requirement. However, I would also add that each one
5 was the result, in full or in part, of a settlement. It is nearly impossible for an
6 outsider to divine the give and take that goes into a settlement – which is to say
7 that they could comply with normalization, but I cannot see it from my vantage
8 point.

9 **Q. Mr. Mullins has questioned whether your “normalization theory” is**
10 **accurate. How do you respond?**

11 A. No one has suggested that my “normalization theory” violates any provision of
12 the IRC, the Treasury Regulations, or any of the normalization PLRs. Mr.
13 Mullins simply thinks it is wrong because it is different from other approaches he
14 has seen.

15 **Q. Mr. Mullins refers to IRS Notice 2019-33 and the EEI response. Can you**
16 **elaborate on the Notice and EEI response?**

17 A. Prior to issuing any guidance on the TCJA for utilities, the IRS issued Notice
18 2019-33 asking the public for comments on how it should address various issues
19 raised by the TCJA that were unique to utilities. EEI, working in concert with
20 AGA, responded to the Notice on behalf of the electric and gas industries. In
21 developing a response to the IRS notice, EEI discovered that there was a diversity
22 in practice on how companies were treating the reversal of EDIT across the

1 country. I believe that many utilities were surprised to learn that the consistency
2 rule applied to their EDIT reversals. Many had only focused on the distinction
3 between protected versus unprotected balances and the use of ARAM versus
4 Reverse South Georgia methodology. Once they had those issues covered, they
5 thought they were done with normalization. Many had already agreed to
6 settlements or had orders directing them how to treat their reversal of EDIT. As a
7 result, what you see in the EEI response is not a representation of the rules as they
8 exist but is instead a representation of what utilities hope the rule will become.
9 The EEI response is very clear that the industry expects the consistency rules to
10 apply to the EDIT.²⁷ From that premise, they then attempt to accommodate some
11 of the diversity that exists. The EEI request is not an exposition of the rules in
12 place today, and EEI's response does not make that claim.

13 **Q. Is PSE's approach in conflict with the EEI position as Mr. Mullins claims?**

14 A. No. Contrary to Mr. Mullins statement²⁸, PSE's position is not in conflict with the
15 EEI response to the IRS' request for comments on this topic. PSE's position
16 would be upheld under the guidance request by EEI and is consistent with the law
17 and rules as they exist today.

²⁷ IRS Normalization Notice 2019-33, Request for Comments on Necessary Clarifications to Normalization Requirements for Excess Tax Reserves Resulting from the Corporate Tax Rate Decrease, Comment Letter from EEI & AGA, at 12 (July 26, 2019; posted Aug. 5, 2019) ("As an initial matter, we believe it is important for your guidance to recognize that the consistency rules of section 168 of the Code apply to the [EDIT] and that the interim rate adjustments to reflect the reduction in the corporate tax rate are consistent with a normalization method of accounting.").

²⁸ Mullins, Exh. BGM-1T at 28:6-9.

1 **Q. If the IRS adopts the EEI position, would PSE need to change its treatment?**

2 A. No. PSE's treatment of EDIT is proper, and it would continue to be proper even
3 if the IRS issues future guidance.

4 **Q. Do you have any comments on the Commission's submission to IRS Notice**
5 **2019-33?**

6 A. Yes, I read the Commission's response with some interest. Although PSE is not
7 mentioned by name, the reference to PSE's 2018 ERF filing is clear. I was
8 interested to see that the Commission does not pursue any particular solution or
9 offer the IRS any direction, other than asking for guidance. While I agree that
10 guidance would be welcome, PSE and the Commission do not have the luxury of
11 waiting for the guidance. Journal entries must be made, ratemaking must be
12 pursued, and the existing normalization rules must be followed. PSE has been
13 doing this under the IRS normalization and consistency rules in effect today.

1 **D. Further Response to Mr. Mullins from AWEC**

2 **Q. Mr. Mullins claims to have identified “several factual and conceptual**
3 **inaccuracies” on which PSE’s normalization theory is based.²⁹ Could you**
4 **clarify?**

5 A. Yes, I’ll try. First, Mr. Mullins takes issue with my comment that the revenue
6 requirement in Washington is based on a historical test year. I believe my
7 characterization is generally a fair statement, recognizing that Washington also
8 allows limited and specific restating and pro forma adjustments.

9 In addition, he calls out that PSE has proposed an attrition adjustment which
10 would set rates based on a future rate base (which AWEC opposes).

11 If these are considered “factual” or “conceptual” inaccuracies, Mr. Mullins can
12 rest assured that PSE has appropriately and completely made the necessary
13 adjustments so that (a) all of its restating and pro forma adjustments comply with
14 the normalization provisions (including consistency), and (b) its attrition
15 adjustments also reflect full compliance with the normalization provisions
16 (including consistency).

17 Second, Mr. Mullins takes general issue with PSE’s approach to EDIT reversals
18 and their inclusion in rates, stating that “[o]nly the Commission can make that
19 determination”. No one would dispute the Commission’s role in setting rates.

²⁹ See Mullins, Exh. BGM-1T at 24:18 – 25:15.

1 However, no one would dispute the Commission’s desire to comply with the
2 normalization rules. The two should not conflict. In PSE’s case, they do not.

3 **Q. Mr. Mullins states that PSE has “retained” the EDIT reversals between**
4 **January 1, 2018 and February 28, 2019.³⁰ Did PSE “retain” those amounts?**

5 A. No. As mentioned before and in my initial testimony, PSE recorded the reversal
6 of EDIT as a benefit to deferred tax expense, which is a component of net
7 operating income. That benefit was used in setting rates in the 2018 ERF. In fact,
8 that benefit was the sole reason PSE achieved a net zero rate increase for electric
9 operations in the ERF. Had the tax benefit for EDIT reversal not been recorded,
10 electric rates would have increased by the amount of the EDIT reversal.

11 **Q. If PSE’s customers received the benefit of the reversing EDIT in the**
12 **historical test period, what is Mr. Mullins suggesting that PSE amortize to**
13 **customers?**

14 A. It is an undisputed fact that PSE’s customers received the benefit of the reversing
15 EDIT in the 2018 ERF test year. I demonstrated that in the ERF testimony. Mr.
16 McGuire demonstrates the same in his testimony in this filing³¹. In fact, Mr.
17 Mullins demonstrates it in his analysis when he shows reversing EDIT – it is
18 reversing through deferred tax expense in the period in which the book
19 depreciation is causing the reversal.³²

³⁰ Mullins, Exh. BGM-1T at 24.

³¹ See McGuire, Exh. CRM-1T at 24:3-5, n. 29.

³² See Mullins, Exh. BGM-7 at 1, column “Periodic” ARAM Reversal (reversals are occurring in the same period that the book depreciation is occurring including Gas at 2).

1 In this case, as a result of providing customers with the benefit of EDIT reversals
2 in the test year (the twelve months ended December 31, 2018) as well as
3 requesting that the deferral and amortization of the EDIT reversals from the
4 “interim period” (the same test year plus January through February of 2019), Mr.
5 Mullins would have PSE provide that same benefit a second time to ratepayers by
6 setting the test year EDIT reversal in base rates as well as amortizing the test year
7 amounts again in base rates over a four-year period. Here again is a clear
8 normalization issue: Not only is Mr. Mullins approach challenged under the
9 consistency principles, he would give the same deferred tax benefits to customers
10 more than one time.

11 **Q. Do you have any comments on Mr. Mullins computations?**

12 A. Yes, as an overview, I do not believe that his calculations³³ are necessary to
13 provide customers with the benefits of the reversing EDIT between the periods of
14 January 1, 2018 and February 28, 2019. In addition, I believe his calculations as
15 proposed would violate the normalization rules in two ways: (a) he is treating
16 EDIT inconsistently relative to the other components of normalization (rate base,
17 book depreciation, tax expense and ADIT) and (b) he is giving the benefit to
18 customers two times, which makes his return of the EDIT occur more quickly
19 than allowed by the average rate assumption method.

20 Although I do not agree with Mr. Mullins’ proposal, the calculation that he uses in
21 Table 9 accurately reflects what he is trying to achieve except there is an

³³ Mullins, Exh. BGM-1T at 30, Table 9; Mullins, Exh. BGM-1T at 33, Table 10.

1 additional adjustment that he should make, which would cure the second
2 normalization issue that I have identified (the double count).

3 **Q. Please elaborate.**

4 A. In Table 9, Mr. Mullins identifies the monthly reversal of EDIT for the 14-month
5 interim period. When PSE recorded that reversal, PSE's accounting entries were
6 as follows (for simplicity I compress the monthly entries into one for electric and
7 one for gas):

8	Debit Deferred Tax Liability – electric (FERC 282)	\$27,034,601
9	Credit DFIT Expense – electric (FERC 411)	(\$27,034,601)
10		
11	Debit Deferred Tax Liability – gas (FERC 282)	\$7,069,749
12	Credit DFIT Expense – gas (FERC 411)	(\$7,069,749)
13		

14 In order to defer these balances for amortization under Mr. Mullins' plan, the
15 reversing EDIT must be restored to the balance sheet (i.e. DTL balance) and
16 removed from the deferred tax expense. Essentially, this plan would require the
17 reversal of both entries above. The impact would be as follows:

	<u>Electric</u>	<u>Gas</u>	
18			
19	DFIT Expense (increase)	<u>\$27,034,601</u>	<u>\$7,069,749</u>
20	Impact to NOI (decrease)	(\$27,034,601)	(\$7,069,749)
21			
22	Impact to DTL rate base	(\$27,034,601)	(\$7,069,749)
23			

1 Mr. Garrett makes a similar suggestion, when he suggests that “the EDIT amount
2 passed through to shareholders be restored.”³⁴ The harmful impact to this case
3 would be the same as I’ve noted above.

4 When the impact of these additional entries is considered for rate making in this
5 case, this would clear the second normalization issue that I identified above.

6 Although, it does not resolve the first issue with consistency.

7 My adjustment above stands in contrast to Mr. Mullins proposal³⁵. He suggests
8 that the DTL balance in rate base for the ADIT needs to be reduced by the amount
9 he would amortize in Schedule 141X. Recall that he uses the term “amortize” to
10 refer to the amounts of EDIT reversal in rates. But also recall that accounting for
11 reversals of EDIT under ARAM already requires the removal of that EDIT from
12 the ADIT balance. In other words, the EDIT that has reversed has already been
13 removed from PSE’s balances (i.e. the ADIT balance has gone down).

14 **Q. Please summarize the significance of the above.**

15 A. The above highlights and affirms my contention earlier that Mr. Mullins’ proposal
16 would actually double count the reversal of the EDIT from the interim period if he
17 amortizes it and reduces the ADIT balance again for it. He has identified the
18 issue, but he has the solution backwards. The solution is not to remove it from the
19 ADIT twice. Instead, the solution is to use the entry I show above and restore the

³⁴ Garrett, Exh. MEG-1T at 56:7-8.

³⁵ Mullins, BGM-1T at 34:14-23. (As a clarification, it appears that Mr. Mullins’ reference to “Table 3” at BCM-1T 34:15, should be “Table 10” on page 33 which is the 2nd Table 10 in his testimony, not to be confused with Table 10 of page 19).

1 reversal of interim EDIT to the DTL balance. Once restored, it would put his
2 EDIT amortization in sync with his ADIT balance, without double counting.

3 Unfortunately, this solution leaves unresolved the more fundamental issue that his
4 approach still falls short of the intent of normalization and the consistency
5 provisions; therefore, his recommendation to amortize the EDIT reversal from the
6 14 month interim period should not be adopted by the Commission.

7 **Q. What do you think of Mr. Mullins' use of Schedule 141X?**

8 A. In general, I agree with his approach on the use of Schedule 141X. I support
9 moving the "day-to-day" reversal of EDIT (i.e. the EDIT reversal that is included
10 in PSE's rate request) into base rates. That has the benefit of forestalling the
11 potential for a consistency issue should Schedule 141X somehow get out of sync
12 with schedules used for base rates. It is presently configured to mirror base rates
13 exactly. If the Commission supports any adjustments associated with the interim
14 period (which would in my opinion violate normalization), I would support using
15 Schedule 141X to capture the cleanup of the EDIT associated with the interim
16 period. Mr. Mullins uses Table 10 on page 33 to illustrate this approach.

17 He further uses Table 10 to analyze his flow back rate to insure that he doesn't
18 exceed the maximum ARAM rate.

1 **Q. How would PSE ensure that it doesn't reverse EDIT more quickly than**
2 **allowed under ARAM?**

3 A. Following PSE's approach, all EDIT is recorded as soon as book depreciation is
4 recorded. They are always in sync. PowerTax, the tax software used by PSE,
5 ensures this. There is no delay between the period in which book depreciation
6 occurs and the period in which the relevant EDIT is reversed. This allows for
7 EDIT to reverse at the maximum rate (ARAM) for as long as there is EDIT. As I
8 have mentioned before, the recovery of EDIT needs to follow the recovery of the
9 plant to which it relates (i.e. book depreciation). From a rate setting perspective,
10 they need to be consistent.

11 **Q. Can you respond to Mr. Mullins' proposed EDIT adjustments?**

12 A. Yes, Mr. Mullins proposed EDIT adjustments would violate the normalization
13 provisions because he has misapplied the normalization guidance by selectively
14 applying it only to the accounting entries (i.e. ARAM) while ignoring the
15 guidance related to ratemaking. As a result, his proposals fail to consider the
16 other components that must be normalized and would result in a normalization
17 violation if adopted.

18 **Q. Changing gears to the *unprotected* EDIT balance for gas operations: How**
19 **would PSE respond to Mr. Mullins proposal to return the unprotected EDIT**
20 **for gas operations to gas customers over a one-year period?**

21 A. PSE does not support this approach. Mr. Mullins suggests using the entire
22 balance as an offset against an increase in gas rates. However, it is unlikely that

1 PSE would be resetting base rates within 12 months and thus under this approach,
2 PSE would likely give back more than its unprotected gas EDIT balance. For this
3 reason, PSE would suggest using four years, as outlined in its original filing.
4 Furthermore, Mr. Mullins preference is not supported by any other party in this
5 case.

6 **E. Response to Commission Staff witness Ms. Steward**

7 **Q. Ms. Steward presents Staff's proposals in her testimony. How do you**
8 **respond to her first proposal which is to "create a separate EDIT account on**
9 **its balance sheet"?³⁶**

10 A. PSE is generally in agreement with this proposal as it seems to mirror PSE's
11 proposal.³⁷ By combining the unprotected EDIT balances from all of the FERC
12 190 and 283 accounts, PSE's ability to administer the amortization of the
13 unprotected EDIT over four years would be greatly improved.

14 To clarify the proposal: It would require four accounts: (a) two for electric with
15 one for the electric 190s and one for the electric 283s and (b) two for gas with one
16 for tax 190s and one for gas 283s. In this way, a very small number of accounts
17 could achieve the desired clarity on the reversal of the unprotected balances.

18 As an additional clarification: PSE would not advise separating out the protected-
19 plus EDIT related to plant. Those balances are maintained in the PowerTax

³⁶ See Steward, Exh. CSS-1T at 6:7.

³⁷ See Marcelia, Exh. MRM-1T at 10:1-6.

1 software. To move those balances into separate EDIT accounts would adversely
2 impact the Company's ability to use the software effectively. PSE would be
3 opposed to this move.

4 **Q. How do you respond to Ms. Steward's second proposal which is to "separate**
5 **EDIT amortization/reversals from the Company's federal tax adjustment"?³⁸**

6 A. PSE is not supportive of this change in that it would add complexity and
7 confusion to the tax calculation instead of achieving the desired clarity. For
8 example, the support for the plant related differences in today's tax adjustment³⁹
9 is the PowerTax report. The activity reconciles precisely. If PSE were to carve
10 out the EDIT and divide it into more than one tax adjustment, it might give the
11 impression of better visibility when in fact, it makes the reviewer's (or
12 intervenor's) work more difficult because the plant related book/tax difference
13 would no longer agree directly to the PowerTax report without manual adjustment
14 and manipulation. This would happen because the non-EDIT part of the plant-
15 related activity would remain in one tax adjustment and the EDIT part would be
16 isolated in a different adjustment. The EDIT reversal can always be segregated
17 within the adjustment which would provide the desired transparency while
18 allowing the ease of reconciliation to PSE's source record, PowerTax.

³⁸ See Steward, Exh. CSS-1T at 6:7-8.

³⁹ Adjustments SEF-6.03ER and GR.

1 **Q. How do you respond to Ms. Steward’s third proposal which is to “continue to**
2 **return EDIT to customers on Schedule 141X”⁴⁰?**

3 A. PSE disagrees with continuing to use Schedule 141X for this purpose and would
4 support Mr. Mullin’s approach, which would use Schedule 141X to address the
5 interim reversal of EDIT should the Commission agree with Mr. Mullins
6 proposal. It is preferable to have the “day-to-day” reversal of EDIT in the base
7 rates as this prevents the possibility of normalization issues between what is
8 included in base rates and what is included in Schedule 141X.

9 **Q. How do you respond to Ms. Steward’s fourth proposal which is to “order**
10 **PSE to update Schedule 141X annually to include the following year’s EDIT**
11 **amortization amount”⁴¹?**

12 A. PSE cannot support this. This creates normalization issues. First, to achieve this,
13 PSE would need to also update book depreciation expense, rate base, ADIT, and
14 tax expense annually to comply with the normalization rules. Second, it appears
15 that there would be an intentional mismatch of “following year’s EDIT
16 amortization amount” (i.e. future looking, probably based on an estimate of future
17 retirements and future book depreciation), which would be recorded in the current
18 year against historical book depreciation and retirements. In fact, the book
19 depreciation, which would be the cause of the “following year’s” EDIT reversal,

⁴⁰ See Steward, Exh. CSS-1T at 6:9.

⁴¹ Id. at 6:9-11.

1 would not have even occurred at the time the entries would be recorded. PSE
2 does not support this and neither should the Commission.

3 **Q. Do you agree with Ms. Steward when she states she does “not believe an**
4 **annual volumetric true-up is necessary”⁴²?**

5 A. PSE agrees with that statement. Volumetric true-ups are not conducted on PSE’s
6 base rates. Thus, in order to be consistent, they should also not be required for a
7 rate schedule in which EDIT reversals are included. The only time that it would
8 be required would be whenever the other components in the normalization quintet
9 are trued up. For example, if there is a true-up to rate base or depreciation, there
10 needs to be a similar calculation on the ADIT and the EDIT.

11 I would suggest that the logic employed by Ms. Steward in regard to the
12 volumetric true-up applies equally well to her proposal to annually update
13 Schedule 141X. Neither should occur and for the same reasons.

14 **Q. Ms. Steward’s final comment on tax reform relates to the IRS Revenue**
15 **Procedure 2017-47 (“Rev. Proc. 2017-47”). How would that guidance apply**
16 **to PSE?**

17 A. Rev. Proc. 2017-47 is helpful guidance when a taxpayer “has inadvertently or
18 unintentionally failed to follow a practice or procedure that is consistent with the
19 Normalization Rules”.⁴³ However, the guidance states that:

20 [A] taxpayer’s Inconsistent Practice or Procedure is neither
21 inadvertent nor unintentional if the Taxpayer’s Regulator

⁴² See Steward, Exh. CSS-1T at 6:14-19.

⁴³ Rev. Proc. 2017-47, Section 3.01(2).

1 specifically considered and specially addressed the application of
2 the Normalization Rules to the Inconsistent Practice or Procedure
3 in establishing or approving the taxpayer's rates even if at the time
4 of such consideration the Taxpayer's Regulator did not believe the
5 practice or procedure was inconsistent with the Normalization
6 Rules.⁴⁴
7

8 PSE believes that this part of the guidance would preclude PSE from taking
9 advantage of Rev. Proc. 2107-47. In this GRC, PSE has specifically addressed
10 the normalization principles and their application to its EDIT in the fullest detail
11 possible in order to explain and support the proper treatment.

12 It is PSE's belief that the fact pattern in this GRC would lack the inadvertent,
13 unintentional element required by Rev. Proc 2017-47. As a result, the Rev. Proc.
14 should not be considered as a part of PSE's or the Commission's path to
15 resolution for this matter.

16 **Q. Do you think the Rev. Proc. could apply to other utilities in Washington?**

17 A. It is possible. To the extent that the official record in their proceedings lacked the
18 specific consideration of some element of normalization that resulted in a
19 violation, the Rev. Proc. could apply in that situation. But that fact pattern is not
20 present in PSE's GRC.

⁴⁴ Rev. Proc. 2017-47, Section 3.02.

1 **F. Response to Public Counsel witness Mr. Garrett**

2 **Q. How does Mr. Garrett characterize the Settlement of PSE’s 2018 ERF as it**
3 **relates to EDIT?**

4 A. Mr. Garrett describes the settlement as providing a rider “to begin the prospective
5 refund of the protected EDIT to customers”.⁴⁵ That is not what Schedule 141X
6 does. What the settlement achieved is the matching of the reversing EDIT with
7 the book depreciation expense (along with rate base and ADIT) for the time
8 period covered in the ERF, given the various adjustments that were allowed in the
9 ERF. It was unequivocally not a “prospective refund” of EDIT. It simply
10 provided for the inclusion of the EDIT reversal in rates because the book
11 depreciation, which was causing the EDIT reversal, was being included in rates.
12 Nothing in the Settlement indicates anything different than that.⁴⁶

13 Specifically, paragraph 14 reads

14 14. The Settling Parties agree that PSE will create separate tariff
15 schedules for the pass back of protected-plus EDIT consistent with the
16 average rate assumption method ("ARAM"). The grossed-up, annualized
17 EDIT reversals consistent with ARAM, are \$25.9 million for electric and
18 \$6.1 million for gas. These amounts are based on EDIT reversals in the
19 2018 period and will be included in a separate rate schedule, Schedule
20 141X as indicated in Settlement Stipulation and Agreement paragraphs 7
21 and 10 above. Schedule 141X rates will be reviewed in PSE's next
22 general rate case. The Settling Parties do not agree on the proper
23 accounting and ratemaking treatment of protected-plus EDIT reversals
24 for the period January 1, 2018 through February 28, 2019. The Settling
25 Parties agree that the disposition of those reversals and the proper
26 ratemaking treatment thereof will be addressed in PSE's next general rate
27 case. Attachment C to this Settlement Agreement includes copies of

⁴⁵ Garrett, Exh. MEG-1T at 49:18

⁴⁶ See Settlement Stipulation and Agreement (“Settlement”), Docket UE-180899 and UG-180900, Jan. 30, 2019, paragraphs 14 and 15.

1 proposed Schedule 14IX tariff sheets, as well as copies of proposed
2 Schedule 141 and Schedule 142 tariff sheets.
3

4 There is no mention of “prospective refunds” in the settlement.

5 **Q. Are you advocating for the transfer of the interim EDIT to shareholders as**
6 **Mr. Garrett alleges⁴⁷?**

7 A. No. PSE’s calculation of the EDIT reversal in this case applies the benefit to the
8 costs in this case in the historical test year. It does not transfer the benefit to
9 shareholders. The benefit is offsetting the costs that need to be collected from
10 ratepayers. This has the effect of lowering customer rates, not increasing them.

11 Mr. Garrett appears to be comingling the amounts that were actually over-
12 collected from ratepayers (i.e., amounts collected from January 1 through April
13 30, 2018 which are currently being passed back to customers as a result of the
14 Commission’s order in the 2018 ERF) with the EDIT which was never technically
15 “over-collected”. Different treatment applies to each.

16 The intent behind PSE’s approach is compliance with the normalization rules. In
17 addition, it is looking to achieve the lowest rates possible within the rules.

⁴⁷ See Garrett, Exh. MEG-1T at 50:9-12, 16-17.

1 **Q. Mr. Garrett characterizes the EDIT as a “loan from ratepayers”⁴⁸. Is that**
2 **accurate?**

3 A. No. As I explained in my original testimony, the ADIT represents a tax-free loan
4 from the government, not ratepayers. The government controls all the terms of
5 this “loan”. The government provides two reasons for this loan⁴⁹: (a) to preserve
6 the utility’s incentive to invest and (b) to protect the government’s tax revenues.
7 This is the crux of the normalization rules.

8 **Q. Mr. Garrett has “found no legitimate legal or ratemaking theory articulated**
9 **that would allow for the redirection of these funds to shareholders”⁵⁰. Is that**
10 **accurate?**

11 A. I believe that the normalization rules provide a “legitimate legal [and] ratemaking
12 theory” supporting PSE’s approach in this filing. However, I would not
13 characterize the normalization rules as “redirecting” ADIT or EDIT to
14 shareholders. The rules exist to carry out congressional intent as it relates to the
15 tax incentives Congress has dispensed.

16 When the tax rate is reduced as with TCJA, Congress no longer requires the loan
17 be repaid to the U.S. Treasury. Instead, it permits the loan to be repaid to
18 customers – according to the terms that Congress has provided (i.e. the
19 normalization rules, consistency, ARAM, etc.). But that should not be

⁴⁸ Garrett, Exh. MEG-1T at 51:5.

⁴⁹ Rev. Proc. 2017-46, Section 3.01; Steward, Exh. CSS-2, at 2, “Congressional Intent”.

⁵⁰ Garrett, Exh. MEG-1T at 51:9-11.

1 misconstrued as a “loan from ratepayers” or the “redirection of funds to
2 shareholders”.

3 **Q. Mr. Garrett refers to the Avista order. Do you have anything more to add
4 with respect to that order?**

5 A. Yes, regarding Avista, Mr. Garrett advises the Commission to take some solace in
6 the fact that Avista has not reported a normalization violation and this somehow
7 impugns PSE’s application of the normalization rules.

8 First, I see nothing in the Avista filing or the Commission’s ensuing order that
9 would address the consistency rules of the normalization provisions. Second,
10 Avista’s self-reporting of a normalization violation is not something that Mr.
11 Garrett or I would have any knowledge of until the results became known when
12 the IRS issues a redacted PLR, (assuming we could even infer from the redacted
13 copy who the utility in question was, which we usually cannot do). Third, the
14 lack of self-reporting may only delay the revelation of the issue until it appears in
15 an IRS audit, probably a few years from now. Fourth, PSE’s independent
16 accounting firm, PricewaterhouseCoopers, actually reviewed PSE’s filing position
17 in the ERF and stated that it was correct. I included that as an exhibit in this
18 filing.⁵¹ I did not see similar documentation in the Avista filing.

⁵¹ See Marcelia, Exh. MRM-1T at 34:1-10; Marcelia, Exh. MRM-7.

1 **Q. Mr. Garrett refers to the Cascade order. Do you have anything more to add**
2 **with respect to that order?**

3 A. Yes, regarding Cascade, Mr. Garrett states that “it is another example of a utility
4 in Washington that was required to defer the reversal of protected EDIT for a
5 future amortization to ratepayers – without any normalization rule violation.”⁵²

6 I have already explained how PSE’s approach is consistent with and unique from
7 the order in the Cascade GRC. PSE’s approach complies with the normalization
8 provisions. Mr. Garrett’s assertion of Cascade’s compliance with the
9 normalization rules has no bearing on whether or not it was, in fact, compliant.

10 As with the Avista GRC, I do not see anything in the company’s filing or in the
11 final order addressing the IRS consistency rules. As a result, I do not see
12 evidence to support Mr. Garrett’s assertion. Perhaps he is relying on the lack of
13 evidence (i.e. he has “not heard of any utility incurring a normalization violation
14 from following [his] approach”⁵³) to support his view that no violation exists.

15 That is simply not good enough. There is no reason Mr. Garrett would have any
16 knowledge that any company had a normalization violation on this topic or any
17 other topic. It is imperative that PSE complies with normalization rules,
18 regardless of the approaches other companies have taken.

⁵² Garrett, Exh. MEG-1T at 53:1-3.

⁵³ Garrett, Exh. MEG-1T at 54:1-2.

1 **Q. What evidence does Mr. Garrett point to in support of his position?**

2 A. He dismisses the tax guidance offered by PSE and shifts his attention to six
3 utilities primarily in Oklahoma and Texas. These utilities are using an array of
4 ratemaking methodologies to pass their EDIT to customers.

5 A couple of observations:

6 It appears that none of the utilities has a historical test year covering all of 2018
7 based on Mr. Garrett's cited proceedings.⁵⁴ As a result, none of them could have
8 reflected a full year of EDIT reversal in their rate filing without doing something
9 to bring in the full impact.

10 He notes a number of deferral mechanisms, some with true-ups, some with unique
11 regulatory liability accounts, some with protected balances, some with protected
12 and unprotected balances, and a varying array of amortization particulars (start
13 dates, length, etc.). Some of this was deemed necessary in order to pull in the
14 EDIT reversals which would not have started until 2018, which post-dates the test
15 year in at least a couple of these examples.

16 It is unclear in the examples provided what other mechanisms each utility has in
17 place that would support his proclamation that each utility has no normalization
18 issue. For example, in Oklahoma Gas and Electric ("OGE"), he states that its
19 rider mechanism "will protect the utility and its ratepayers from any tax

⁵⁴ See Garrett, Exh. MEG-1T at 57:5 – 60:6.

1 normalization inconsistencies” and includes a citation. The cited document⁵⁵
2 includes no discussion or reference to normalization or consistency. He simply
3 states it as fact. Now, OGE may or may not have an issue. The relevant question
4 would be what other normalized items are in a similarly constructed rider? If, for
5 example, it is recovering book depreciation via a rider, I would expect the
6 reversing EDIT to be subject to an identical rider. If, on the other hand, only the
7 reversing EDIT is subject to a rider, that would be an issue. The existence of a
8 rider is not evidence that a utility has no normalization issues. It could be that the
9 “protecting” rider may actually be the inconsistency that causes a violation.

10 The same would be true for an annual true-up mechanism. The question to ask is,
11 what else is subject to the annual true-up mechanism. It may be that the true-up
12 mechanism is compliant with consistency, or it may be the cause of non-
13 compliance.

14 **Q. Does Mr. Garrett’s approach comply with normalization?**

15 A. No. In his testimony, Mr. Garrett responds to the following question:

16 If the Commission were to order that the protected EDIT
17 amortization for 2018 through February 2019 be refunded in this
18 case, would you have any concerns with IRS normalization rule
19 violations?⁵⁶

⁵⁵ The citation has a typo, it should be Cause No. PUD 201700496 (rather than
201400496),

⁵⁶ Garrett, Exh. MEG-1T at 60:7-23.

1 He responds in the negative, noting specifically that the statute (IRC
2 §168(i)(9)(B)) does not include EDIT in the list of items to which consistency
3 applies. Mr. Garrett has taken a position diametrically opposed to the IRS
4 position in PLR 8920025, which states that the consistency rules apply to EDIT.
5 It is Mr. Garrett who stands opposed to the IRS rules, not PSE.

6 He then notes that “there are various ratemaking mechanisms available to
7 alleviate any concerns about normalization violations”.⁵⁷ As I have indicated, the
8 mechanisms themselves must comply with the normalization consistency rules.
9 There is no free pass simply because the mechanism is being applied to EDIT.
10 EDIT remains part of the deferred taxes, and all deferred taxes (including the
11 EDIT) remain subject to the normalization rules. Further, any ratemaking
12 mechanism that would violate normalization when applied to the ADIT balance
13 will also violate the normalization when applied to the EDIT balance.

14 All the mechanisms that Mr. Garrett cites (e.g. the deferrals, the true-ups, the
15 special accounts, etc.) would clearly violate the normalization rules if applied
16 only to the ADIT balance (and not the book depreciation, tax expense, and rate
17 base). His defense appears to be (a) the consistency rules don’t apply and (b)
18 other utilities are using these mechanisms. As I have demonstrated, the
19 consistency rules do apply and the fact that others are using these mechanisms
20 does not establish that they are being employed properly under the consistency
21 rules.

⁵⁷ Garrett, Exh. MEG-1T at 60:25 – 61:2.

1 Mr. Garrett refers to the testimony of Mr. Hamlett⁵⁸ from AEP's rates department
2 as an example worth mimicking. According to Mr. Hamlett, AEP is pursuing two
3 tracks to ensure that its EDIT refund scheme will not exceed the ARAM limit.
4 Specifically, he identifies two options: First, he suggests a true-up mechanism
5 attached to a rider. I addressed this type of adjustment above. Provided the same
6 true-up mechanism is applied to all four components of normalization, this could
7 work. If it only applies to the EDIT, it will fail the consistency test. The key
8 would be to ensure the accounting and the ratemaking maintain all items in sync.
9 From the information provided, that does not appear to be the case. Second, he
10 suggests that the commission could "move amortization of excess deferred tax
11 between the 'protected' and 'unprotected' buckets". That's an interesting theory.
12 There is no law, regulation, or PLR that even suggests this is possible. It is
13 unclear how the amortization of one item could be morphed into the amortization
14 of another item when the cause of the reversing EDIT is book depreciation. It
15 either causes the reversal of EDIT or it does not. This is not something that could
16 be decided after the fact.

17 Regardless of these concerns, Mr. Garrett has confidence in Mr. Hamlett's
18 approach because AEP is one of the largest investor-owned utilities in the
19 country.⁵⁹ "AEP is well aware of the normalization rules and how to avoid

⁵⁸ Garrett, Exh. MEG-1T at 61:10 – 18.

⁵⁹ Garrett, Exh. MEG-1T at 62:4.

1 violating them.”⁶⁰ This is extremely poor logic. AEP’s size is not a factor in
2 determining its compliance with the normalization rules.

3 **Q. What else does Mr. Garrett cite in support of his non-compliant approach to**
4 **normalization?**

5 A. In closing, Mr. Garrett offers Exh. MEG-5 with orders from about 12 states. Most
6 of these orders are generic in their expression that commissions across the country
7 are requesting their utilities to pass along the benefits of TCJA as quickly as
8 possible. Most of these are not much different than the press release issues by our
9 own Commission in January 2018. In the few citations actually addressing a
10 utility, most utilities respond along the lines that they are continuing to review the
11 impacts of the TCJA, much like PSE responded initially in Dockets UE-171225
12 and UG-171226. In reviewing Exh. MEG-5, I noted that only one order
13 mentioned normalization – the State of Montana. Not one mentioned the
14 consistency rules nor did any mention ARAM – critical components that could
15 have added something to this proceeding but ultimately do not.

16 **Q. What does Mr. Garrett’s review of these other states’ proceeding tell you?**

17 A. Based on the samples provided by Mr. Garrett, I see no evidence that any other
18 state with which he is familiar has engaged in the careful analysis of the
19 consistency issue as that upon which PSE has embarked.

⁶⁰ Garrett, Exh. MEG-1T at 62:7.

1 **Q. Have you reviewed Mr. Garrett's calculations in Exh. MEG-3?**

2 A. Yes, I have. I will begin by addressing Schedule 6 on Exh. MEG-3, "Interim
3 Amortization of Protected EDIT" for electric.

4 First, let me make a couple of corrections to the math. (a) On line 3 of the Sch. 6
5 of Exh. MEG-3, he calculates the amount of EDIT reversal in January and
6 February 2019. In doing so, he uses the actual number of days (31 for January
7 and 28 for February). This is not how PSE calculates its EDIT reversal. PSE uses
8 whole months, as does Mr. Mullins when he performs his calculations. Mr.
9 Garrett should use whole months on line 3. He does use whole months further
10 down in his determination of the monthly activity, which becomes the basis of his
11 AMA calculation. Line 5 should be \$27,034,600, which would bring it into
12 balance with the ending balance in his monthly activity for his AMA calculation
13 (which appears lower down on Sch. 6).

14 (b) He has an error in his equation for the calculation of AMA. In attempting to
15 include the beginning balance from June 2018 in his equation (which is necessary
16 for the math to work), he points to the wrong cell. The cell he points to is blank.
17 This results in his AMA calculation being incorrect. When corrected, the AMA
18 amount that he is trying to calculate as of June 30, 2019 would be \$23,022,872.
19 This is the value that should appear on Line 6 of Sch. 6.

20 (c) When both of these errors are corrected, the result is that Lines 7 and 8 of Sch.
21 6 would both become \$13,517,300.

1 Shifting now to the gas side and Exh. MEG-4, Schedule 6, also labelled “Interim
2 Amortization of Protected EDIT”:

3 (d) On line 3 of the Sch. 6 of Exh. MEG-4, he calculates the amount of EDIT
4 reversal in January and February 2019, and fails to use whole months, as
5 discussed above. Mr. Garrett should use whole months on line 3. He does use
6 whole months further down in his determination of the monthly activity which
7 becomes the basis of his AMA calculation. Line 5 should be \$7,069,749, which
8 would bring it into balance with the ending balance in his monthly activity for his
9 AMA calculation (which appears lower down on Sch. 6).

10 (e) While Line 6 is calculated correctly, Line 7 is incorrect due to the changes to
11 Line 5. Line 7 should be \$3,522,854.

12 If left uncorrected, these mistakes in Exh. MEG-3 and Exh. MEG-4 would be an
13 additional normalization violation, albeit a small one, due to the inconsistencies in
14 the calculations. At a minimum they are math errors that need to be cleaned up if
15 the Commission were to accept Mr. Garrett’s proposal.

16 **Q. Changing gears to the *unprotected* EDIT balance for electric and gas
17 operations: How would PSE respond to Mr. Garrett’s proposal to return the
18 unprotected EDIT for electric and gas operations to customers over a two-
19 year period?**

20 A. Mr. Garrett’s preference for electric operations is not supported by any other party
21 in this case. Mr. Mullins agrees with PSE on the use of a four-year amortization.
22 His preference for gas operations conflicts with Mr. Mullins’ one-year

1 amortization. PSE does not support this approach for the reason mentioned
2 above. In addition, Mr. Garrett provides no rational supporting a two-year
3 amortization period. For this reason, PSE would suggest using four years, as
4 outlined in its original filing for amortizing the unprotected EDIT.

5 **G. Summary on EDIT**

6 **Q. Can you summarize the EDIT issues in this case?**

7 A. Yes, I would divide the issues between the interim period and the continuing
8 period.

9 Interim period

10 Mr. Mullins and Mr. Garrett dispute PSE's treatment of the EDIT reversals in the
11 interim period. PSE has substantiated that the IRS consistency rules apply
12 throughout the process, from the accounting entries for the reversal and
13 continuing through the ratemaking process and the mechanisms used in that
14 process. At heart, Mr. Mullins and Mr. Garrett would only apply the
15 normalization rules throughout the accounting process. If their position were
16 correct, PSE's 2008 PLR would not have been ruled a violation, as the accounting
17 was correct. It was the ratemaking mechanism that caused the problem. Their
18 approach presents the same type of challenge to consistency when they employ
19 unique processes to the EDIT reversal, which are not applied to the other
20 components of normalization.

21 Continuing Period

1 I do not detect much disagreement amongst the parties on the treatment of the
2 period following the interim period (the continuing period). The reversal of EDIT
3 is reflected in the historical period and is factored into the setting of rates. As it
4 relates to PSE's proposed attrition adjustment, care has been taken to ensure that
5 all of the normalization rules have been followed. None of the parties propose
6 any specific modification to PSE's handling of EDIT reversals in the attrition
7 model.

8 In addition, whenever pro forma or restating adjustments have been made, PSE
9 has also made adjustments to its EDIT reversals, as appropriate. Most
10 adjustments to the historical test year do not require adjustment, but some do. An
11 example of one that requires adjustment would be the change to Colstrip
12 depreciation rates. None of the parties have proposed any modification to PSE's
13 EDIT treatment in the restating or pro forma items.

14 Accounting and Tracking

15 Mr. Mullins, Ms. Steward, and Mr. Garrett disagree on some of the particulars of
16 the accounting and the use of Schedule 141X. Mr. Garrett would prefer to see the
17 EDIT in a separate account and reversals in Schedule 141X. Mr. Mullins
18 approach is closest to PSE's in that he supports PSE's accounting and would
19 change the use of Schedule 141X to deal with only the interim period. For the
20 reasons stated above, PSE wants to maintain its present accounting – its
21 protected-plus EDIT is located in its three FERC 282 accounts and those accounts
22 are controlled and the detail is maintained within the company's PowerTax

1 software. Tracking and reporting are easily maintained therein and would become
2 much more complex were it to pursue an alternate tracking/reporting scheme. As
3 for the use of Schedule 141X, PSE believes that including EDIT reversals in base
4 rates is the best way to ensure and preserve compliance with the normalization
5 provisions (to which Mr. Mullins does not object). As for Mr. Mullins use of
6 Schedule 141X to address issues in the Interim Period, that would be a good
7 approach – but PSE doesn't believe any adjustment is necessary.

8 **Q. What is the benefit to using the PSE's approach?**

9 A. There are many. First, this approach complies with the normalization rules and
10 the alternatives presented in this case do not. Second, it matches the benefit of the
11 EDIT reversals to those customers who are bearing the burden of the book
12 depreciation expense, which is causing the reversal. No other proposal can make
13 this claim. Third, PSE's approach is simple. It does not require the creation of
14 additional accounts or rate schedules. It uses PSE's software in the manner in
15 which it is appropriately designed. Fourth, PSE's approach is transparent. PSE is
16 able to monitor and report on EDIT activity.

17 **Q. Even so, PSE's approach appears to be an outlier.**

18 A. I would agree with that observation. However, I would also point out, in PSE's
19 defense, that PSE has a history of being an outlier when it comes to normalization
20 issues.

21 PSE was the only utility to raise the issue of AMA rate base versus EOP ADIT
22 back in 2007. All utilities in Washington were faced with the same issue and

1 anyone of them could have raised the issue. None did. In fact, any utility around
2 the country with a similar issue could have raised it. None did. Apparently only
3 PSE understood the import of the normalization rules well enough to raise the
4 issue.

5 I can only imagine if that issue had come before Mr. Mullins and Mr. Garrett back
6 then. It is likely that they would have presented testimony not dissimilar from
7 what they have offered in this case. They would have pointed out how Avista,
8 Cascade, and NW Natural report their rate base and ADIT on AMA and EOP,
9 respectively – so should PSE. They would point out that neither Avista, Cascade,
10 nor NW Natural have self-reported normalization violations – believing,
11 incorrectly, that this is evidence that all is well on the normalization front.

12 Then again when the Treasury issued guidance on the newly created §1603
13 Treasury Grants (“T. Grants”), it was PSE who secured the initial flexibility in the
14 IRS’ application of the normalization rules to the T. Grants – allowing the flow
15 through of the benefit over 10 years versus the usual 25 years for T. Grants on
16 wind farms. PSE followed up this effort by pursuing a change to the
17 normalization laws that would exclude T. Grants from the rules, which allowed
18 the pass back of interest on the T. Grants to customers. Not all utilities were
19 supportive of this approach. Had EEI been polled, I would expect to see a broad
20 diversity of opinion and practice, not unlike what we see today with EDIT.

21 I raise these points as a counter to Mr. Mullins’ and Mr. Garrett’s assertions that
22 PSE is out-of-bounds because it is not following other utilities or their

1 presumption that other utilities know the rules better. I would suggest that PSE's
2 history and the evidence presented in this case indicate otherwise.

3 So when it comes to normalization, PSE may be an outlier – only until other
4 utilities are brought in-line behind it.

5 **Q. What will PSE do if the Commission rules against PSE on this issue?**

6 A. If the Commission were to conclude that PSE's approach is deficient, PSE would
7 need to respectfully challenge that conclusion. If the Commission is unrelenting,
8 it is possible for PSE to pursue a PLR on this topic. This is not the preferred
9 approach as it would result in considerable time before the issue would be
10 concluded. By way of reference, PSE's 2008 PLR took two years to obtain.
11 PSE's 2006 PLR on the 2000 Centralia sale took five years to obtain.

12 **IV. ATTRITION MODIFICATIONS**

13 **Q. Please summarize the changes you made to the attrition workpapers for**
14 **electric attrition calculation.**

15 A. The changes PSE made to its electric attrition analysis resulted in minor changes
16 to the result. Rate base had a net decrease of \$11.7 million, net operating income
17 declined by \$0.7 million, and the revenue requirement had a corresponding
18 decrease of \$1.8 million⁶¹.

⁶¹ See workpaper "190529-30-PSE-WP-SEF-18.00E-ELECTRIC-MODEL-REBUTTAL-19GRC-01-2020.xlsx", "Impacts" tab.

1 Workpaper “NEW-PSE-WP-MRM-1T-Attrition-Study-Tax-19GRC-06-
2 2019.xlsx” has been updated. See “NEW-PSE-WP-MRM-11T-Attrition-Study-
3 Tax-19GRC-06-2019.xlsx”. Specifically, the “electric activity” tab was updated
4 as follows: (a) Minor changes were made to the Escalation Factors for
5 Transmission which moved from 5.32% to 5.77% and Distribution which moved
6 from 3.44% to 3.09%. Those changes tracked through the calculation of book
7 depreciation and accumulated reserve, as well as tax depreciation and the ADIT
8 balances. (b) In addition, on the same tab, the presentation of tax depreciation
9 and ADIT related to GTZ was altered so that it would display in a manner
10 consistent with the AMI presentation. No change was made to the amounts in
11 total, only the display was changed to pull all GTZ amounts out of the Intangible
12 Plant balance. In the original presentation, some GTZ balances remained in
13 Intangible Plant.

14 Changes in the workpaper then rolled into the electric attrition model, Exhibit No.
15 RJA-8. PSE cleaned up its presentation of rate base and its components amounts,
16 starting on rows 33 and below, for AMI and GTZ, in columns h and i. In its
17 initial filing, amounts specific to AMI and GTZ were not fully separated out of
18 column g (“Trended Costs”). This led to some confusion as the balances reported
19 in columns h (“AMI”) and i (“GTZ”) did not visually agree to the supporting tabs.
20 Upon further review, PSE determined that the amounts did, in fact, agree as any
21 variation was buried in column g.

1 The changes to the presentation did not cause a change in the amounts in column
2 j, the “Rate Year Revenue & Costs”.

3 In conclusion, for electric attrition, the only update that had any impact on the
4 attrition results was the update to the Escalation Factors.

5 **Q. Please summarize the changes you made to the attrition workpapers for the**
6 **gas attrition calculation.**

7 A. The changes PSE made to its gas attrition analysis resulted in small changes to the
8 result. Rate base had a net decrease of \$4.8 million, net operating income
9 decreased \$1.2 million, and the revenue requirement had a corresponding
10 decrease of \$2.1 million⁶².

11 Workpaper “NEW-PSE-WP-MRM-1T-Attrition-Study-Tax-19GRC-06-
12 2019.xlsx” has been updated. See “NEW-PSE-WP-MRM-11T-Attrition-Study-
13 Tax-19GRC-06-2019.xlsx”. Specifically, the “gas activity” tab was updated as
14 follows: (a) PSE determined that the amounts reflected for the cost recovery
15 mechanism (“CRM”) were off slightly due to a formula issue which prevented the
16 proper rollforward of the book reserve for accumulated depreciation – thus
17 throwing off the rate base calculation by \$4.8 million. This has been corrected.
18 This issue did not impact depreciation expense or ADIT. (b) In addition, as was
19 the case with the electric side, the presentation of tax depreciation and ADIT
20 related to GTZ was altered so that it would display in a manner consistent with

⁶² See workpaper “190529-30-PSE-WP-SEF-18.00G-GAS-MODEL-19GRC-01-2020.xlsx”, “Impacts” tab.

1 the AMI presentation. No change was made to the amounts in total, only the
2 display was changed to pull all GTZ amounts out of the Intangible Plant balance.

3 Finally, the “ETR” tab was updated, as well. PSE discovered that the pre-tax NOI
4 on the “ETR” tab did not get updated for all of the attrition-related changes that
5 were submitted in PSE’s Response to AWEC Data Request No. 20. This update
6 caused NOI to decline by \$1.2 million.

7 Changes in the workpaper then rolled into the gas attrition model, Exhibit No.
8 RJA-9. PSE updated its presentation of the rate base components, starting at row
9 29 and below, for CRM, AMI, and GTZ, in columns h, i, and j. In its initial
10 filing, amounts specific to these items were not fully separated out from column g
11 (“Trended Costs”). This led to some confusion as the balances reported in
12 columns h (“CRM”), i (“AMI”), and j (“GTZ”) did not visually agree to the
13 supporting tabs. PSE’s review of AMI and GTZ confirmed that the amounts did,
14 in fact, agree as any variation was in column g.

15 PSE has corrected the CRM balances and improved the presentation for CRM so
16 that it ties back to the SEF-8.02GP.

17 In conclusion, for gas attrition, PSE made two updates which impacted the
18 attrition results: one for the CRM book reserve for accumulated depreciation,
19 which impacted rate base, and one to include the missing items in gas pre-tax NOI
20 as identified in PSE’s Response to AWEC Data Request No. 20.

1 **Q. Have you reviewed Staff witness Lui's adjustment to gas attrition adjustment**
2 **for CRM?**

3 A. Yes, I have. In her adjustment, she proposes to change the ADIT displayed in
4 column h of Exh. RJA-9 to the amount that appears on Ms. Free's adjustment
5 SEF-8.02GP. Ms. Lui has the correct theory. The numbers on Exh. RJA-9 and
6 adjustment SEF-8.02G should agree. Unfortunately, PSE's original presentation
7 of the CRM attrition adjustment lacked a certain level of clarity, as I have
8 discussed above. The "missing" balance that Ms. Lui was correctly trying to
9 display was actually imbedded in the "Trended Costs" balances in column g. As
10 a result, the adjustment she proposes to column h needs to also apply to column g
11 at the opposite sign, such that the ending balance in column k would remain
12 unchanged.

13 Based on this confusion, PSE has updated its presentation so that the balances in
14 Exh. RJA-9 agree to those in SEF-8.02GP and adjusted columns h and g
15 accordingly. This adjustment when considered by itself results in no change.

16 In researching this issue, PSE discovered this issue mentioned above where the
17 book reserve for accumulated depreciation was not rolling forward correctly.

18 PSE's revised attrition analysis reflects this change, and it does have an impact on
19 the results, as mentioned above.

20 In summary, the Commission should not accept Ms. Lui's adjustment to the CRM
21 as it was ultimately a presentation issue only.

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V. FINANCIAL TRANSPARENCY AND IMPROVEMENT PROGRAM

Q. Did any party propose any adjustment or modification to the Financial Transparency and Improvement Project (“FTIP”) that you discussed in your prefiled direct testimony?

A. No. It is my understanding that all of the parties in this case have accepted PSE’s position on FTIP. No one has proposed any adjustment or modification.

VI. CONCLUSION

Q. Does this conclude your prefiled rebuttal testimony?

A. Yes, it does.