

BEFORE THE WASHINGTON UTILITIES AND TRANSPORTATION COMMISSION

KIMBERLY-CLARK TISSUE COMPANY

Complainant

v.

Docket No. UG-990619

PUGET SOUND ENERGY, INC.

Respondent;

DIRECT TESTIMONY OF WILLIAM F. DONAHUE
ON BEHALF OF PUGET SOUND ENERGY, INC.

October 4, 1999

DIRECT TESTIMONY OF WILLIAM F. DONAHUE

Q. Mr. Donahue, please state your name, business address and position.

A. My name is William F. Donahue. I am a Regulatory Consultant employed at Puget Sound Energy ("PSE"). My business address is 411 108th Avenue NE (OBC-03W), Bellevue, Washington, 98004. More detail on my background is contained at Exhibit ____ (WFD-1).

Q. Please summarize your testimony.

A. Kimberly-Clark has been assessed \$346,000 in penalty charges, pursuant to PSE's tariff, because it continued to consume interruptible gas when it had been instructed to curtail. I will explain the mechanics of and the purpose for the penalty provisions in PSE's Rate Schedule 57 tariff. I will present evidence that demonstrates the cost of gas required to provide the over-run volumes used by Kimberly-Clark in violation of PSE's tariff. I will demonstrate why collection of the assessed penalty dollars is required to keep PSE's jurisdictional sales customers from absorbing a loss. I will demonstrate the approximate savings that Kimberly-Clark has enjoyed over the 34 months preceding the December 1998 curtailment by contracting for a lower level of firm service than it required. Finally, I will respond to certain erroneous balancing assertions made by Kimberly-Clark's witness, J.T. Owens.

ASSESSMENT OF PENALTY CHARGES

Q. What is the purpose of the penalty charge under Rate Schedule 57?

A. The over-run penalty charge of \$2 per therm was designed by PSE, along with the Commission Staff and Public Counsel, and approved by the Commission (in Docket Nos. UG-920840 and UG-940814 / 940034) to accomplish two goals: first, to provide sufficient economic incentive to encourage proper behavior by interruptible customers, namely to suspend the use of interruptible gas when curtailed; and second, to keep sales customers whole for the added costs of acquiring the over-run gas used by the non-complying interruptible customers.

Q. What do you mean by economic incentive?

A. At the time it was authorized, it was thought that the \$2 per therm charge, in addition to the charges under Rate Schedule 41, would be a sufficiently high cost to encourage interruptible customers to switch to their alternate fuels or suspend their use of interruptible gas, in order to comply with provisions of curtailment.

Q. What do you mean by keeping sales customers whole?

A. Like most regulated gas utilities, PSE utilizes a gas cost recovery mechanism, known as a Purchased Gas Adjustment ("PGA") clause. Pursuant to the PGA rule in PSE's tariff, the gas cost recovery rate components, such as those within Rate Schedule 41 are set periodically (with the approval of the WUTC) to recover the expected annual average cost of acquiring gas for the Rate Schedule 41 customers. Differences between actual costs and recoveries are placed in a special PGA fund (known as FERC account 191). To the extent that the PGA fund does not balance out over the course of a year, the rate components charged to all sales customers are adjusted appropriately. Thus, over time the customers neither overpay nor underpay for the cost of gas PSE acquires to serve them, and PSE neither over-recovers nor under-recovers its actual cost of gas.

Q. What is the relationship of the PGA fund to penalty charges under Rate Schedule 57?

A. When a customer violates the tariff and is billed a penalty (the \$2 per therm penalty charge is paid) to the PGA fund. The penalty charge is not profit to PSE, but rather it is compensation to PSE's sales customers.

Q. Could you explain?

A. When transportation customers refuse to curtail their use of interruptible gas during a curtailment, they are billed as a Rate Schedule 41 customer for those over-run volumes. If the Rate Schedule 41 gas cost component paid by the non-curtailing interruptible transporter does not exactly equal the cost of the incremental over-run gas acquired, the difference, either positive

or negative, will be absorbed as a benefit or burden, respectively, by sales customers through the PGA fund.

Q. What was the cost of acquiring the over-run gas delivered to Kimberly-Clark during the period December 24 through 28, 1998?

A. Without attempting to quantify the value of utilizing PSE's scarce distribution capacity, which was needed to ensure service to other higher priority customers, I would conclude the cost of gas was \$.330 per therm. As shown on my Exhibit ___ (WFD-2) the total cost of overrun gas used by Kimberly-Clark was \$57,500.

Q. By paying the Rate Schedule 41 gas cost recovery rates, as required by the tariff, has Kimberly-Clark provided a benefit or burden to sales customers?

A. Kimberly-Clark has placed a \$24,700 burden on PSE's sales customers. The Rate Schedule 41 gas cost recovery rate in December 1998 was only \$.1895 per therm. Kimberly-Clark thus reimbursed PSE's sales customers only \$32,800 for the over-run gas and could leave the sales customers responsible for the balance. We must consider as well the \$2 per therm penalty charge, which was designed, in part, to prevent a transportation customer from placing an economic burden on sales customers.

Q. But if the full \$2 per therm penalty charge is paid by Kimberly-Clark won't that more than cover the shortfall in gas cost recoveries?

A. Yes, at approximately \$346,000 the penalty charges billed to Kimberly-Clark are more than sufficient to cover the \$24,700 shortfall in gas cost recoveries. But the remaining \$321,300 may only begin to compensate sales customers for their other losses. How does one place a value on the inconvenience and potential health and safety risk associated with the loss of heat and hot water by firm sales customers? Especially when you consider those customers pay significantly higher rates in exchange for an expectation that the company will provide firm uninterrupted service to them. Since there is no comparable fund through which to compensate firm customers for the damages caused by the unauthorized use of distribution capacity, the

Commission found that the crediting of penalty charges for the benefit of sales customers, through the PGA fund, was the most appropriate and convenient manner to compensate them for the wrongful behavior of others.

Also consider that, had Kimberly-Clark's oil shipments stopped on December 19, 20 or 21 Kimberly-Clark could have just as easily made the same decision to burn penalty over-run gas. Kimberly-Clark' witnesses Armstrong and Walton have indicated that the Everett plant requires more than its existing level of firm gas volumes for at least 18-36 hours to shut down the plant. The cost of acquiring over-run gas on those days would have averaged \$1.858 per therm and the sum of the Rate Schedule 41 gas cost component and the \$2 per therm penalty would not have even covered the incremental gas cost, much less provided sufficient compensation for the improper use of capacity.

Kimberly-Clark should not be allowed to place a burden on PSE's sales customers by not covering at least the incremental cost of gas it forced PSE to acquire on its behalf. Further, Kimberly-Clark should not be advantaged by paying less than it would have paid its own supplier for gas on the applicable days. PSE has asked Kimberly-Clark to tell us what that gas would have cost (Data Request No. 4 of PSE's Fifth Data Request) and it has not responded. Portions of Kimberly-Clark's gas supply agreement with DETM are confidential, so I can only estimate, but in my opinion the cost of gas under the DETM agreement may well have been more than the cost of the incremental supplies acquired by PSE on the applicable days.

**KIMBERLY-CLARK HAS ELECTED NOT TO CONTRACT FOR A
SECURE FUEL SUPPLY FOR ITS REQUIREMENTS, APPARENTLY IN
THE INTEREST OF COST SAVINGS**

Q. Does Kimberly-Clark have sufficient secure fuel supply to safely conduct its operations?

A. Kimberly-Clark's witnesses Walton and Armstrong both have indicated that firm supplies of fuel, beyond the existing 14,000 therms per day, would be required for 18-36 hours in order to

accomplish a safe shutdown of the plant. However, when requested to provide the specific volume in Data Request No. 9 of PSE's Sixth Data Request, Kimberly-Clark declined to respond.

Q. What can you conclude about the level of secure fuel supply required for the safe operation of the plant?

A. We know that Kimberly-Clark has testified that it made every effort to minimize the use of natural gas during the curtailment period. Yet without oil, and relying on minimal amounts of wood waste, it still consumed on average over 61,100 therms per day of gas from 10:00 PM December 24 through 5 PM December 28 (see Exhibit ____ (WFD-3)). We also know that Kimberly-Clark has previously contracted for 47,797 therms per day of firm sales service from PSE for the plant site when it appeared that the backup oil fuel system was unavailable in January and February 1996, (see Direct Testimony of PSE witness Mr. Lewis). I would have to conclude from the information available that Kimberly-Clark would require the equivalent of between 47,800 and 61,100 therms per day of natural gas to safely operate its plant.

Q. Does Kimberly-Clark have a firm supply of fuel equivalent to between 47,800 and 61,100 therms per day of natural gas?

A. No. Mr. Armstrong has testified that spent sulfite liquor can "run short in winter" (and there is no other alternative fuel for Boiler No. 10, except natural gas); that "there are no guarantees of wood waste" and that interruptible supplies of natural gas "can be entitled or curtailed." We also know from the record that diesel fuel oil can become unavailable. I would thus conclude that the only reliable supply of fuel for the plant, in fact the "alternate" fuel of last resort for the entire plant, is the natural gas available through Kimberly-Clark's combination of contracts with DETM for 14,000 therms per day of firm gas supply and with PSE for firm gas transportation of that gas supply. As such Kimberly-Clark appears to have concluded that having a secure supply for only 23 % to 29 % of its requirements to safely operate its plant is "safe enough."

Q. What could Kimberly-Clark's motive be for choosing to rely on such a small percentage of firm gas?

A. One factor might be cost. By my calculations (see Exhibit ___ (WFD-3)) Kimberly-Clark saves from \$405,000 to \$566,000 or more per year by only contracting for 14,000 therms per day of firm gas transportation on PSE's system. In addition, while I am not privy to the entire contents of Kimberly-Clark's gas supply agreement with DETM (portions are confidential), I would estimate that Kimberly-Clark could be saving an additional \$123,000 to \$172,000 per year by not contracting for firm gas supply, beyond the 14,000 per day. It appears to me that Kimberly-Clark has chosen to gamble that its interruptible service would not be curtailed at the same time its primary fuels were unavailable.

Further evidence of this "gamble", as it relates to the winter of 1998, is: (a) Kimberly-Clark's choice to only contract with one fuel oil supplier, (b) Kimberly-Clark's election not to negotiate "firm" or "exclusive right" oil deliveries, (c) Kimberly-Clark's failure to more thoroughly test the entire fuel oil delivery system to ensure there was no caustic in the lines, and (d) Kimberly-Clark's apparent decision not to seek an increase in the firm portion of its Rate Schedule 57 contract with PSE and its gas supplier. All of these options would likely have meant additional costs to Kimberly-Clark. For nearly 3 years Kimberly-Clark has benefited from its choice to contract for interruptible transportation by saving approximately \$1,500,000 to \$2,000,000 (or more) in the process. However, on December 24th through 28th, 1998, when its primary fuels were not available, Kimberly-Clark had to rely on its alternate fuel. Due to Kimberly-Clark's own actions (or inactions), the only other fuel available was Kimberly-Clark's chosen alternate fuel: PSE over-run penalty gas. Kimberly-Clark's decision to consume penalty gas cost it \$346,000.

**PSE DID NOT BENEFIT FROM KIMBERLY-CLARK'S OVERSUPPLY
OF GAS**

Q. Kimberly-Clark' witness J.T. Owens has indicated that Kimberly-Clark delivered to PSE over 110,000 therms of supply in excess of its usage in the first few days of the curtailment. Is that entirely correct?

A. No, the 110,000 therms were delivered to PSE by Kimberly-Clark's supplier, DETM on Kimberly-Clark's instruction. Under Rate Schedule 57 service, a customer is responsible for making a daily order or "nomination" of the gas it plans to use. Often a customer will place this responsibility with its supplier. It is not uncommon for a customer (or its supplier, on behalf of the customer) to make a nomination for gas deliveries for each of several days in advance, especially over a weekend. A volume difference or "imbalance" between a customer's nomination and its actual use (over-supply or under-supply) occurs nearly everyday. The imbalances are tracked by PSE and pursuant to the tariff, must be periodically cleared by the customer. In fact, Kimberly-Clark owed PSE, on average, more than 94,000 therms per day (with a high of 174,000 therms) for each of the first 18 days in December, 1998, (based on my review of page 10 of Exhibit ___ (DJF-5)).

For such a significant imbalance to occur during a period of curtailment, especially when gas supply costs are so high, someone at Kimberly-Clark or its supplier must have been "asleep at the wheel". According to the testimony of Mr. Armstrong, Kimberly-Clark learned of the "strong potential" of entitlement from DETM early on December 18. According to the testimony of Mr. Walton, Kimberly-Clark was directly notified of curtailment by PSE at 7:30 PM on December 19, 1998. From the moment Kimberly-Clark and DETM learned of the curtailment, both parties had numerous opportunities to reduce nominations for deliveries of gas to PSE for gas days December 20 and 21. Had either party contacted PSE and reduced the nomination down to Kimberly-Clark's firm contracted volume, nearly 102,000 therms of the imbalance could have been avoided. Kimberly-Clark and its supplier, by their inaction, chose to have excess

volumes delivered at no charge to PSE on gas days December 20 and 21.

Q. Was PSE's gas supply position assisted by Kimberly-Clark's excess supply during the curtailment period?

A. No. The fact that Kimberly-Clark's excess gas may have been a benefit to PSE is irrelevant, since PSE had more than sufficient supplies available to serve all of the needs of its firm customers. To the best of my knowledge the majority of PSE's available supplies were priced below the estimated cost of Kimberly-Clark's supply during the "price peak." In fact, in certain situations, the presence of Kimberly-Clark's excess gas on PSE's system might be a hindrance to PSE's ability to exercise cost-efficient gas supply management by preventing PSE from utilizing an optimal blend of storage, peaking resources or other contract volumes from its supply portfolio.

Q. Does this conclude your testimony?

A. Yes, it does.

Background of Witness:
William F. Donahue

Education & Professional Degree

Bachelor of Science in Accounting, Marquette University (Milwaukee, Wisconsin)

Certified Public Accountant.

Employment Experience

Arthur Andersen & Co. (Milwaukee, Wisconsin) from 1976-1981.

conducted financial statement audits and special projects primarily for regulated utilities.

Northwest Pipeline Corporation (Salt Lake City, Utah) from 1981 through 1991.

roles of increasing responsibility in the Rates, Regulatory Affairs and Planning organizations.

responsible for all Purchased Gas Adjustment filings for a 5 year period.

member of the open-access industry transition team which led the company's conversion from merchant to transporter.

I. testified before the U.S. Federal Energy Regulatory Commission ("FERC") as an expert witness on rate design matters, storage utilization and pipeline capacity, including preparation and sponsorship of the pipeline's mileage study.

Washington Natural Gas Company (Seattle, Washington) from 1991 to merger, AND

Puget Sound Energy, Inc. (Bellevue, Washington) from merger in early 1997 to current

management of gas-related U.S. Federal and Canadian regulatory matters and policy,

administration of Purchased Gas Adjustment (PGA) mechanism and PGA Incentive Mechanism and special projects relating to these matters,

advisor to the utility's corporate strategic and Least Cost planning efforts related to gas supply, gas storage and capacity resource planning

advisor on tariff and contract matters to the Jackson Prairie Storage Project.

co-author of several regulatory settlements of major policy and rate issues associated with the gas industry transition. (1991-1994)

management of gas supply planning and gas cost accounting functions (1993-1995).