EXHIBIT NO. ______ (BAL-1T)
DOCKET NO. UE-04____/UG-04____
2004 PSE GENERAL RATE CASE
WITNESS: BARBARA A. LUSCIER

BEFORE THE
WASHINGTON UTILITIES AND TRANSPORTATION COMMISSION

WASHINGTON UTILITIES AND TRANSPORTATION COMMISSION, **Complainant,** **v.** **PUGET SOUND ENERGY, INC.,** **Respondent.**	**Docket No. UE-04____** **Docket No. UG-04____**

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

APRIL 5, 2004

PUGET SOUND ENERGY, INC.

PREFILED DIRECT TESTIMONY OF BARBARA A. LUSCIER

PUGET SOUND ENERGY, INC.

PREFILED DIRECT TESTIMONY OF BARBARA A. LUSCIER

I. INTRODUCTION

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

A: My name is Barbara A. Luscier and I am the Manager of Revenue Requirements at Puget Sound Energy, Inc. ("PSE" or the "Company"). My business address is 10885 N.E. Fourth Street, Bellevue, Washington, 98009.

Q: Would you please provide a brief description of your educational and business experience?

A: Please see Exhibit No.___ (BAL-G2).

Q: What topics will you be covering in your testimony?

A: In this portion of my testimony, I will present the calculation of ratebase, working capital, conversion factor and the overall revenue requirement for the natural gas results of operations. I will also explain some of the various adjustments to the results of operations for the current test year and, after taking into account these adjustments, present the natural gas revenue requirement deficiency of $49,015,476, as shown on Exhibit No.___ (BAL-G3), including municipal additions, based on the adjusted test period.

Q: Please explain your Exhibit No.___ (BAL-G3).

A: The first page of this exhibit, Summary page, presents the unadjusted operating income statement and Average-of-the-Monthly-Averages ratebase for the Company as of September 30, 2003. Each of these items is then adjusted for the summarized proforma and restating adjustments. The revenue deficiency is added to the adjusted income statement and the impact on the operating income statement is presented. The rest of the exhibit is composed of two sections.

Pages G3-A through G3-C present a summary schedule of all the proforma and restating adjustments. The first column of numbers, on page G3-A, is the unadjusted net operating income for the year ended September 30, 2003 and the unadjusted ratebase for the same period. Each column to the right of the first column represents a proforma or restating adjustment to net operating income or ratebase. Each of these adjustments has a supporting schedule, which is referenced by the page number shown in each column title.

Pages 2.01 through 2.16 are the supporting schedules for each of the adjustments shown on the summary schedule.

The last column, shown on page G3-C of the summary schedule, summarizes all of the adjustments and is the adjusted test period results used to calculate the revenue deficiency.

II. NATURAL GAS ADJUSTMENTS

Q: Please describe each adjustment, explain why it is necessary, and identify the effect on operating income or ratebase.

A: I will explain the adjustments that I am testifying to in the same order as they are shown on the summary schedule.

Revenue and Purchased Gas

This restating and proforma adjustment, shown on Exhibit No.___ (BAL-G3), page 2.01, normalizes weather sensitive gas therm sales by eliminating the effect of temperature deviation above or below historical normals. It restates therms sold to reflect the weather normalized therms and then reprices the adjusted therms sold based upon the authorized weighted average cost of gas. Restating adjustments have been made to: remove propane sales and the associated revenue; reflect consumption under normal weather conditions; and reflect the revenue difference between the actual rates and the base rates in effect during the test year. A proforma adjustment has been made to reprice the normalized monthly therms at current base rate levels, effective September 30, 2003.

This adjustment, shown on Exhibit No.___ (BAL-G3), page G3-A, column 2.01, decreases net operating income by $1,423,726.

Federal Income Taxes

This adjustment, shown on Exhibit No.___ (BAL-G3), page G3-A, column 2.02, adjusts actual Federal Income Tax expense to the restated level based on the test year for this case. As our normal tax year ends December 31st, this adjustment recalculates the test year using expenses and tax adjustments for the twelve months ended September 30, 2003 and removes the current tax year estimates from the test period.

The effect of this adjustment, shown on Exhibit No.___ (BAL-G3), page G3-A, column 2.02, is to decrease net operating income by $1,221,100.

Tax Benefit of Proforma Interest

This proforma adjustment, shown on Exhibit No.___ (BAL-G3), page G3-A, column 2.03, uses a ratebase method for calculating the tax benefit of proforma interest. As adopted by this Commission in prior rate cases, the customers receive the tax benefit associated with the interest on debt used to support ratebase and construction work in progress that has associated tax deductible interest.

The effect of this adjustment is to decrease net operating income by $6,061,718.

Depreciation and Amortization

Test year depreciation has been restated based on the Average-of-Monthly-Averages using the rates from the depreciation study performed in 2001 and applied in the Company's last general rate case, Docket No. UE-011570 and UG-011571. This restating and proforma adjustment, shown on Exhibit No.___ (BAL-G3), page G3-A, column 2.04, decreases net operating income by $241,312 and decreases ratebase by $120,656.

Q: Regarding depreciation, in the settlement of the last general rate case, Docket No. UG-011571, the Company agreed to depreciate rental assets at an annual rate of not less than $8,284,422 until September 1, 2005. Has the Company complied with that settlement agreement?

A: Yes. For the twelve months ended August 31, 2003, twelve months after the effective date of gas rates from the last general rate case, the Company 's depreciation for rental equipment was $8,382,567. Depreciation for the twelve months ended September 30, 2003, the test period in this rate filing, was $8,356,210.

Q: Regarding gas rentals, the UG-011571 settlement agreement provides that the Company would not request an increase in the revenue requirement associated with the program until at least September 1, 2005. Is the Company requesting an increase in the revenue requirement associated with the gas rental program in this case?

A: No. In fact, the revenue requirement for the gas rental program in this filing has declined from the revenue requirement in the 2001 general rate case.

<u>Conservation</u>

This restating and proforma adjustment, shown on Exhibit No.___ (BAL-G3), page G3-A, column 2.05, removes the amortization associated with the conservation tracker.

The effect of this adjustment is to increase net operating income by $754,507.

Bad Debts

This adjustment restates the uncollectible account provision from the estimated loss per books to the actual amount of net bad debt write-off during the test year.

This adjustment, as shown on Exhibit No.___ (BAL-G3), page G3-A, column 2.06, increases net operating income by $42,404.

Miscellaneous Operating Expense and Ratebase

This restating and proforma adjustment, shown on Exhibit No.___ (BAL-G3), page G3-B, column 2.07, adjusts the test year for various items. Incentive plan payments based on a calendar year have been adjusted to the twelve months ended September 30, 2003. Associated payroll taxes have been adjusted accordingly. An adjustment has been made to annualize the effect upon ratebase of utility property that had been transferred from future use to non-utility during the test year. An adjustment has been made to increase ratebase for construction work in progress that was in service but had not been transferred to plant in the test year.

The effect of this adjustment is to increase net operating income by $106,298 and to increase ratebase by $3,267,546.

Property Taxes

This proforma adjustment, shown on Exhibit No.___ (BAL-G3), page G3-B, column 2.08, reflects the estimated property tax levy rates to be paid in 2004 based upon 2003 value. These rates will be adjusted to actual during the course of this proceeding.

The effect of this adjustment is to lower net operating income by $1,321,869.

Excise Tax and Filing Fee

This restating adjustment, shown on Exhibit No.___ (BAL-G3), page G3-B, column 2.09, adjusts the test year estimates to actual expense for the Washington Utility Tax and filing fee.

The effect of this adjustment is to decrease net operating income by $116,245.

Rate Case Expenses

As in prior general rate cases, this proforma adjustment, shown on Exhibit No.___ (BAL-G3), page G3-B, column 2.10, calculates the expected costs for this case and amortizes them over three years. This adjustment also adjusts for the unamortized costs related to the 2001 rate case to be amortized in the rate year. This adjustment will be updated during the course of the proceeding.

The effect of this adjustment is to decrease net operating income by $352,540.

Property and Liability Insurance

This proforma adjustment, shown on Exhibit No.___ (BAL-G3), page G3-B, column 2.11, reflects the expected increases in property and liability insurance since the test year. This adjustment will be updated during the course of the proceeding.

The effect of this adjustment is to reduce net operating income by $424,068.

Pension Plan

This restating adjustment, shown on Exhibit No.___ (BAL-G3), page G3-B, column 2.12, adjusts the test year to reflect only cash contributions to the Company's qualified retirement fund. During 2003 the Company made the maximum tax deductible cash contribution, as determined by its plan actuary, to the Pension Plan to help ensure that the plan remains fully funded. As allowed in prior general cases the Company has averaged the last four years of contributions and is requesting that average amount in current rates. This adjustment also restates the expense associated with the Supplemental Executive Retirement Plan to an average of the last four years expense.

The effect of this adjustment is to reduce net operating income by $3,106,764.

Wage Increase

This proforma adjustment, shown on Exhibit No.___ (BAL-G3), page G3-C, column 2.13, reflects the impact of wage increases and payroll tax changes. For represented (union) employees, the adjustment annualizes the wage increases granted in 2004, 2005, and 2006. The percentage of wage increase for IBEW union employees from the test period through the rate year are 3% effective April 1, 2003, 3% effective April 1, 2004, and 3% effective April 1, 2005. The percentage of wage increase for UA union employees from the test period through the rate year are 4.5% effective October 1, 2002, 4.5% effective October 1, 2003, 3% effective October 1, 2004, and 3% effective October 1, 2005. The percentage of wage increase for management employees from the test period through the rate year are 3% effective March 1, 2003, 3% effective March 1, 2004, and 3% effective March 1, 2005. These management increases have been weighted by prior year actual salary increases, as in prior general rate cases.

This adjustment decreases net operating income by $1,435,634.

Investment Plan

This proforma adjustment, shown on Exhibit No.___ (BAL-G3), page G3-C column 2.14, adjusts the Company portion of investment plan expense to reflect the additional expense associated with the wage increase and is based on the current contribution rates.

Net operating income is decreased by $67,031 as the result of this adjustment.

Employee Insurance

This proforma adjustment updates the test year insurance payments to the amount that will be experienced in the rate year. For represented employees, the estimated cost is based on the average Company contribution amount of $620 (3/03 –6/05) and $682 (7/05-4/06) per eligible employee per month. The amounts are the result of negotiations between PSE and the IBEW union and PSE and the UA union. The same average rate was also applied per salaried employee. This estimate will be updated to actual during the course of these proceedings.

These costs are allocated to expense, construction and other accounts based on the percentage of payroll charged to these accounts during the test year. The portion of the insurance payments associated with expense during the test year has been determined to be 67.73%. This adjustment corrects the amounts actually charged to expense to reflect the appropriate 67.73% allocation.

The effect of this adjustment, shown on Exhibit No.___ (BAL-G3), page G3-C, column 2.15, is to decrease net operating income by $486,489.

Low Income Amortization

This proforma adjustment, shown on Exhibit No.___ (BAL-G3), page G3-C, column 2.16, removes amortization of the Company's Low Income Program. Such costs are recovered through a rider outside of general rates.

The effect of this adjustment is to increase net operating income by $1,792,203.

Working Capital

The purpose of this calculation is to provide a return for the funds the shareholder has invested in the Company, for utility purposes, over and above the investment in plant and other specifically identified ratebase items already earning a rate of return.

The first part of this adjustment calculates the total average invested capital that has been utilized during the test year. From the average invested capital, the operating investment, which is already earning a return, is deducted. A second deduction is made for nonoperating assets and plant not in service. The result is total working capital provided by the shareholder.

This total working capital is then allocated between nonoperating working capital and operating working capital using the method consistent with previous rate cases. The resulting operating working capital represents the shareholder's average investment which is required to provide utility service but which would otherwise not earn a return.

The working capital allowance calculation is shown on Exhibit No.___ (BAL-G3), page 4.01. The result shows that there will be a working capital allowance of $3,808,108 included in ratebase.

Cost of Capital

This schedule, shown on Exhibit No.___ (BAL-G3), page 4.02, reflects the proposed capital structure for the Company during the rate year and the associated costs for each capital category. The capital structure and costs are presented in the testimony of Mr. Donald E. Gaines, Exhibit No.___ (DEG-1T). The rate of return is 9.12%.

Conversion Factor

The conversion factor, shown on Exhibit No.___ (BAL-G3), page 4.03, is used to adjust the net operating income deficiency by revenue sensitive items and Federal income tax to determine the total revenue requirement. The revenue sensitive items are the Washington State utility tax, Washington WUTC filing fee, municipal additions, and bad debts. The conversion factor used in the revenue requirement calculation, taking into consideration the adjustments discussed earlier, is 59.514%.

<u>Allocation Methods</u>

Common Utility Plant is that portion of utility operating plant that is used for providing more than one commodity, i.e., both electricity and gas, to customers. Thus, common plant includes costs associated with land, structures, and equipment which are not charged specifically to electric or gas operations because the assets are used jointly by both departments. The Company allocates its common utility plant in determining ratebase by using the four-factor allocation method as authorized in the merger stipulation. Components of the four-factor allocator include the number of customers, direct labor charged to O & M, Transmission and Distribution O & M, and net classified plant (excluding general plant).

Common operating costs are those costs that are incurred on behalf of both electricity and gas customers. The Company incurs common costs related to: Customer Accounts Expenses; Customer Service Expenses; Administrative and General Expense; Depreciation/Amortization; Taxes Other Than FIT; and FIT. The most appropriate allocation method is applied consistently to each type of common cost. Allocation methods used include: (1) twelve month customer average; (2) joint meter reading customers; (3) non-production plant; (4) four factor allocator; (5) direct labor; (6) current tax.

For purposes of calculating the working capital allowance, the Company applies the most appropriate of the allocation methods to each common balance sheet accounts.

Allocation methods used and the calculations thereof are shown on Exhibit No.___ (BAL-G3), page 4.04.

General Rate Increase

This schedule, shown on Exhibit No.___ (BAL-G3), page 4.05, is a summary of proforma and restated ratebase and net operating income. Based on $1,064,289,530 invested in ratebase and $67,892,302 of net operating income, the Company would have a revenue deficiency of $49,015,476, including municipal additions. This results in an average increase of 4.78%.

Q. Does this conclude your testimony?

A. Yes, it does.

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