

Agenda Date: March 31, 2004
Item Number: A1

Docket: UE-031471
Company: Puget Sound Energy
Staff: Merton Lott, Energy Industry Coordinator

Recommendation:

Enter an order denying the request of Puget Sound Energy for deferral of all of the costs for outside services (legal and technical consultants) associated with its Power Cost Only Rate Case (PCORC), Docket UE-031725, but acknowledge that PSE may raise the issue in its next general rate case proceeding.

Discussion:

On September 12, 2003, Puget Sound Energy (PSE or Company) filed a petition requesting that it be allowed to defer costs associated with outside services related to the PCORC filing in FERC Account 182.3, Other Regulatory Assets. In addition, the Company specifically asks that the deferred costs be included in working capital in future rate proceedings. The petition also asks that these costs be reviewed and the amortization set in the next general rate proceeding.

Staff believes that it is appropriate to consider outside regulatory costs incurred between general rate cases when setting rates in a general rate proceeding. However, the treatment of deferring costs and amortizing them over a specific period is not necessarily the best methodology for such inclusion. The legal and consulting fees projected by PSE in the PCORC represent operating expenses of PSE that, absent regulatory authority, would be expensed consistent with generally accepted accounting principles and the uniform system of accounts. Historically, in many rate case proceedings before the Commission, one adjustment to operating expense has been to proform a reasonable level of rate case expense. These amounts, such as the \$767,000 amount included in the settlement of PSE's last electric general rate case, are referred to as amortizations or normalizations. However, rarely if ever are the unamortized portions of these costs proformed into rate base as working capital or any other rate base component, and no adjustment to rate base was made in PSE last electric general rate proceeding for unamortized rate case costs.

At this time, the level of rate case costs incurred by PSE is unknown. However, in response to Staff data requests PSE provided the following information:

Through August 31, 2003, PSE spent \$450,000 on legal fees and nothing on consultants;

The Company estimated an additional \$970,000 for legal costs through post-hearing briefs;

For consulting fees, PSE estimated \$200,000 of which \$77,000 had been incurred prior to November 7, 2004; and

PSE's total estimated costs in November for the PCORC are approximately \$1.6 million.

Concerns with PSE's Petition

Staff has several concerns with the deferral requested by PSE.

- 1 Review of the actual costs incurred by PSE for legal expenses related to the PCORC is extremely difficult to complete. For the most part the costs had not been incurred as of the date of Staff's data request for invoices in November. With respect to the legal costs incurred from March 2003 through October 2003, for which PSE did provide invoices, the invoiced costs attributed to the PCORC include descriptions of several items, many showing direct relationship to the PCORC, but several others appear related to resource acquisition, least cost planning, or other items.
- 2 The level of legal expenses seems high. In UE-921262, a major general rate case, the Commission expressed concern about total legal expenditures of \$500,000. These PCORC legal costs are nearly triple those for a general rate case while the CPI has increased by about 30%. Additionally the UE-921262 legal fees included oversight of several outside consultants, and included significantly more issues, witnesses, hearings, time to process, and data requests to respond to.
- 3 Total legal costs (both expensed and deferred) appear to be substantially higher starting with the test period in UE-011570 than had been experienced in the years preceding that test period.
- 4 The petition asks that amortization not begin until the Commission's decision in PSE's next general rate proceeding. This type of condition, if approved, may allow PSE to carry a cost on its books for a substantial period of time. While this concern may not be important if PSE files its rate case this year, it is important in a general rate case that the Commission not only consider the regulatory costs incurred between rate cases in establishing a proper expense level but also the time over which those costs are incurred.
- 5 The booking of a regulatory asset, on a company's books, that has not been determined prudent and acceptable for rate recovery by the Commission, results in the possibility of negative reactions, of the financial community for one, if the Commission excludes a portion of the costs as inappropriate for the determination of rates.

- 6 Staff opposes including the unamortized portion of these costs in rate base. These costs are operating expenses and provide no ongoing direct benefit or value to the ratepayers. Like bad debts, temperature impacts on revenues, and stream flow impacts, Staff recognizes that these costs do not follow a smooth pattern and it is important to include a “normal” level of cost in a general rate proceeding -- but that does not mean that any portion of the costs should be treated as an investment.

On the issue of when the amortization should commence, Staff believes that the amortization included in the rate case of \$767,000 means that a certain level of legal costs are currently being considered in the calculation of rates. Those rates went into effect in July 2002. That amortization resulted in revenue requirement in the test year ended July 2001. The level of recovery resulting from that inclusion would be dependent on actual sales since rates went into effect July 1, 2002. Thus, depending on when a rate case is filed and processed, some portion of these costs may have already been recovered through continuation of current rates. Therefore, Staff does not believe the Commission should delay the beginning of amortization of these costs as requested, but instead, it should indicate that the recovery included in rates prior to conclusion of that next general rate case will be considered in the determination of how much of these costs should be used in determining rates going forward.

Despite Staff’s concern, Staff believes that it is appropriate to give PSE assurance that the Commission will in fact consider including these costs in the determination of rates in its next general rate proceeding. Whether these costs are reasonable and prudent, whether or not these costs have already been recovered through time, whether these costs actually represent the costs of this rate proceeding, and whether it is appropriate to give rate base consideration for these costs are all issues that can and should be addressed in a subsequent general rate proceeding; the Commission should not decide these issues at this time.

Conclusion:

Staff recommends, that the Commission deny PSE’s request, but acknowledge that PSE has the right to request recovery of these costs in its next general rate proceeding. The order should not establish future rate recovery or the proper rate treatment of these costs. The question of whether PSE can create a regulatory asset on its financial statements is for PSE and its auditors to determine based on their interpretation of the pronouncements of the Financial Accounting Standards Board.