EXHIBIT NO. _____(SG-1T)
DOCKET NO. UE-060266/UG-060267
2006 PSE RATE CASE
WITNESS: STANLEY GENT

BEFORE THE WASHINGTON UTILITIES AND TRANSPORTATION COMMISSION

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| WASHINGTON UTILITIES AND TRANSPORTATION COMMISSION,<br><br>Complainant,<br><br>v.<br><br>PUGET SOUND ENERGY, INC.,<br><br>Respondent. | ) | Docket No. UE-060266<br>Docket No. UG-060267 |

# PREFILED TESTIMONY OF STANLEY GENT ON BEHALF OF SEATTLE STEAM COMPANY

Date: July 19, 2006

## I. INTRODUCTION

**Q: Please state your name, occupation and business address.**

A: My name is Stanley Gent. I am President and CEO of Seattle Steam Company ("Seattle Steam"), 1440 Puget Sound Plaza, 1325 Fourth Avenue, Seattle, WA 98101.

**Q: Would you describe your education, relevant employment experience, and other professional qualifications.**

A: I am a native of Ireland, and graduated from Queens University in Belfast with a degree in Mechanical Engineering. After immigrating to Canada in the 1970s I started my career in the design and construction of power generation facilities for Ontario Hydro and Edmonton Power. Since then my career has included development of many energy-related projects across North America. During the 1990s I was vice president of engineering and development for Chicago-based Unicom Thermal Technologies, where I became a leader in development of a variety of district cooling systems. Prior to coming to Seattle Steam I was President of Comfort Link, a district cooling company located in Baltimore, Maryland. I joined Seattle Steam in my current position in 2004.

**Q: What is the purpose of your testimony?**

A: I will present Seattle Steam's position, as one of Puget Sound Energy's ("Puget's") largest, if not its largest interruptible gas customer, regarding the role of interruptible customers in Puget's system, gas rate design and rate spread, and concerning the depreciation tracker that Puget proposed.

## II. THE ROLE OF INTERRUPTIBLE CUSTOMERS IN PUGET'S CUSTOMER BASE

**Q: Please describe the business of Seattle Steam Company.**

A: Seattle Steam operates a steam district heating system serving over 175 customers in the downtown and First Hill areas of Seattle. The predecessors of Seattle Steam were founded in 1893. Through a steam distribution piping network under the streets of

Seattle, we serve the space and water heating requirements of many of the office and government buildings in downtown Seattle, as well as hotels, colleges, hospitals and commercial establishments in an area extending from Elliott Bay on the west to Twelfth Avenue on the east, and from Qwest Field on the south to Virginia Street on the north. Because our business is providing heat, our largest business expense is energy. We are concerned in this proceeding not only with the costs to Seattle Steam, but also with the costs that we must pass on to many of the businesses, institutions and non-profit organizations in downtown Seattle.

**Q: Please describe Seattle Steam's plants and their operation.**

A: Seattle Steam operates two steam plants, both of which are capable of burning either natural gas or residual (heavy) fuel oil. The plants are located near the waterfront in Seattle. Historically the predominant fuel for Seattle Steam's operations has been natural gas. The plants could, however, be quickly switched from burning natural gas to residual fuel oil, as Seattle Steam has been required to do a number of times most winters, when there are capacity restrictions on either Northwest Pipeline's ("NWP's") interstate pipeline or Puget's distribution system.

**Q: What does it mean for the functioning of Puget's distribution system for Seattle Steam to be an interruptible customer?**

A: The Puget distribution network that serves Seattle Steam extends north from NWP's South Seattle meter station located southeast of Renton. Our plants are towards the northern end of that network. As a result, we are in a position to assist Puget in maintaining pressure on its system by quickly switching from natural gas to residual fuel oil. This situation occurs several times some heating seasons. As Puget's witnesses have described, Puget's distribution system is sized to allow it to meet the peak demand day of its firm (non-interruptible) customers, which is the coldest expected day in this area. On the peak demand day, when there is the maximum demand reducing the pressure of gas

within Puget's distribution network, Puget needs to still be able to maintain adequate pressure throughout its system to prevent customers at the end of its system from losing the functionality of their gas appliances. During periods of peak demand for natural gas, primarily cold spells when demand for heating peaks, the pipes in Puget's system are simply not large enough to deliver enough gas to all its customers on that system. As a result, if Puget had to continue delivering gas to all its customers, the pressure in its gas lines would drop. That could result not only in customers going cold, as insufficient gas was delivered to work their heating systems properly, but also in a dangerous situation, because pilot lights could be extinguished by the drop in pressure. It is on those occasions, upon notice from Puget, that Seattle Steam switches from natural gas to fuel oil, thereby freeing up the "transportation capacity" that Puget otherwise uses to deliver natural gas to Seattle Steam. That helps Puget maintain the pressure in its delivery system, and helps assure that its non-interruptible customers (i.e. residential and small commercial) continue to receive the natural gas they expect.

**Q: When and how does Seattle Steam resume receiving natural gas from Puget?**

A: When the demand on Puget's system is reduced to the point that Seattle Steam can resume using gas without any of Puget's other customers experiencing a drop in pressure, Puget notifies Seattle Steam that it can switch back from fuel oil to natural gas.

**Q: Are there similarities between the design and cost of facilities to serve Puget's natural gas customers and the design and cost of facilities to serve Seattle Steam's customers?**

A: Yes. Both systems deliver energy in a vapor form by pipeline.

**Q: Based on your experience as an engineer and as an executive of Seattle Steam, what impact does having an interruptible customer in a situation such as Seattle Steam have on Puget's cost of delivering natural gas to Puget's customers?**

A: Looking at the cost of delivering natural gas ("transportation" as that term is used in Puget's rates), one of the highest marginal costs of providing service is the cost of facilities to meet peak demand and especially serving new demand in an area where the existing infrastructure is at its capacity. When a system is at capacity, the primary way of expanding capacity would be to replace existing pipe with larger pipe or to add new larger pipe to the existing network of pipes. Thus it would be extremely expensive for Puget to meet rising peak demand, or serve the needs of additional customers along its existing network, but for the existence of major interruptible customers such as Seattle Steam. Because we can switch to another fuel source, we can free up significant capacity for Puget during peak periods. Indeed, we only use Puget's system during periods when it has excess capacity that would otherwise go unused, and being unused would produce no revenue. As a result, Seattle Steam generally provides significant revenue to the company at comparatively low marginal cost.

**Q: What impact do Seattle Steam and other interruptible customers have on Puget's need to make capital investments in its system?**

A: As Puget witnesses have described, a significant portion of Puget's capital investment is to enable it to serve a growing residential and commercial customer base. That requires both investment in Puget's transportation capacity and in extending its distribution system. Puget Gas Rule No. 23 provides:

> PSE's gas distribution system and gas supply resource portfolio are designed to meet the needs of firm [not interruptible] customers. Interruptible service is made available as long as, in PSE's sole judgment and discretion, any one of the following conditions exists:
>
> a. distribution capacity and/or contracted gas supply resources are not needed to meet the expected demand of firm customers, or
>
> b. any excess distribution capacity and/or supply resource may be used by interruptible customers without jeopardizing continuous service to firm customers, or
>
> c. maintenance, repair or operational conditions of PSE's gas distribution system do not prevent or limit service to interruptible customers.

In discovery, Seattle Steam asked Puget to list all facilities it anticipates it will be required to build over the next five years in order to be able to continue to provide interruptible service under Schedule 57 (Seattle Steam's current rate schedule). Puget responded in part:

> Pursuant to Rule 23, PSE's facility plan over the next five years is to continue to provide firm service to its firm customers. Rule 23 only allows for continued interruptible service until the firm demand utilizes the capacity of the designed facilities.

Exhibit No._____ (SG-2), p. 1. In short, Puget's policy is to build no facilities to meet the needs of interruptible customers.

**Q: Puget witnesses also say that it has been required to make substantial investments in replacing old cast iron and bare steel mains, which must be replaced to avoid safety issues, but the replacement of which generate no additional revenue. What impact does Seattle Steam have on Puget's need to invest in such replacement of existing mains?**

A: Seattle Steam has created none of that need. It is served through a 6-inch service line connected to a 16-inch diameter wrapped steel gas supply main that runs from Northwest Pipeline's South Seattle meter station in Renton (the place where Puget's system takes over from NWP) north to downtown Seattle. That main was installed in 1956, and has long since been fully depreciated.

## III. RATE DESIGN AND RATE SPREAD

**Q: What is Seattle Steam's position regarding Puget's cost of service study?**

A: As Janet Phelps testifies, the fundamental principle of a cost of service study is to allocate costs to the customer or group of customers that causes the utility to incur the cost. In that regard, as more of Puget's costs have been incurred to enable it to meet increased demand, it is important to interruptible customers that the cost of service study reflect the fact that interruptible customers do not cause Puget to make new investment and make no demands on Puget's system except when the system has excess capacity. Puget's description of its cost of service study reflects a detailed effort to assign costs to the

customers that cause the cost to be incurred. To the extent that it differs from the "Commission Basis" methodology determined in Washington Natural Gas Docket Nos. UG-940034 and UG-940814, Seattle Steam asks the Commission to carefully consider the modifications Puget has proposed.

**Q: What is Seattle Steam's position regarding gas rate design and rate spread in this matter ?**

A: A fundamental concept of what makes utility rates "fair, just, reasonable and sufficient" is that individual customer classes should pay the cost of providing service to their class. If they pay less than the cost of their service they are being subsidized by either other customer classes or by the utility stockholders. If they pay more than the cost of their service they are subsidizing other customer classes or the stockholders. In that regard, Seattle Steam finds the table on page 23 of Janet Phelps' testimony, Exhibit No. ____ (JKP-IT), p. 23, reproduced below, troubling.

| Rate Class | Parity Ratio | Rate of Return |
|---|---|---|
| Residential Schedules | 86% | 6.1% |
| Commercial & Industrial (Schedules 31, 36, 51, 61) | 85% | 6.1% |
| Large Volume (Schedule 41) | 114% | 12.7% |
| Interruptible (Schedule 85) | 138% | 19.3% |
| Limited Interruptible (Schedule 86) | 167% | 25.2% |
| Non-exclusive Interruptible (Schedule 87) | 134% | 17.8% |
| Transportation (Schedule 57) | 165% | 25% |
| Transportation Special Contracts | 101% | 9.9% |
| Compressed Natural Gas (Schedule 50) | 2% | -16.2% |
| Rentals (Schedules 71, 72, 74) | 56% | -7.9% |

What that chart shows is that the parity ratio of each of the interruptible classes -- Schedules 85, 86, 87 and 57 -- is significantly higher than the parity ratio of the other schedules. The interruptible customers are currently subsidizing several of the other customer classes based on the cost to provide service. Similarly the rate of return from the four interruptible classes is significantly higher than the rate of return from all other classes.

**Q: What implications does that have for the share of Puget's revenue requirement that should be born by the interruptible classes?**

A: A basic criteria for determining whether rates are "fair, just and reasonable" as to any particular class or group of classes of customers is whether they are paying their share of the costs, but not more than their share of the costs of providing service to them. As described above and as is illustrated by Janet Phelps' testimony, Exhibit No. ____ (JKP-IT), p. 23, Puget's cost of service study shows that the four interruptible classes currently have a higher parity ratio than any of the non-interruptible classes and currently provide Puget with a higher rate of return than any of the other classes. Thus Seattle Steam believes that any share of the increase in the company's revenue requirement that is assigned to the interruptible classes should be significantly less than the share assigned to the other classes. The ultimate rate design should move the interruptible classes towards parity, not further away from parity.

We understand that staff, public counsel and perhaps others contest the amount of Puget's actual revenue requirement, contending that any increase should be substantially less than Puget has requested. Except for noting that it is important to Seattle Steam that Puget have sufficient revenues to be financially healthy and to be able to make long-term commitments in the energy markets, Seattle Steam has no position regarding Puget's total revenue requirement. However, whatever total revenue requirement the Commission establishes should be distributed across the classes so that all share in any reduction over

what Puget has requested. The revenue requirement of some classes should not be fixed, with the benefits of any reduction being assigned solely to other classes.

## IV. THE PROPOSED DEPRECIATION TRACKER

**Q: What is Seattle Steam's position concerning the depreciation tracker that Puget has proposed?**

A: First, Seattle Steam recognizes that when Puget is forced to make investments that do not result in increased revenues, such as replacing cast iron or bare steel mains with wrapped steel or plastic, Puget needs to have a way to recover those costs. Our concern about the depreciation tracker, however, is two-fold. First, it is again critical that such costs be properly attributed to the customer class for which the cost is incurred. From what we could determine, Puget did that appropriately. Second, however, once the depreciation tracker is established, it would be impossible to effectively audit what costs were assigned to it. An alternate that allowed Puget to recover for known and measurable investments it has made over a fairly short period of time would be acceptable.

**Q: Does that complete your testimony?**

A: Yes it does.