Exh. BAE-1T
Docket UG-170929
Witness: Betty A. Erdahl

BEFORE THE WASHINGTON
UTILITIES AND TRANSPORTATION COMMISSION

WASHINGTON UTILITIES AND TRANSPORTATION COMMISSION, **Complainant,** **v.** **CASCADE NATURAL GAS CORPORATION,** **Respondent.**	**DOCKET UG-170929**

TESTIMONY OF

Betty A. Erdahl

STAFF OF
WASHINGTON UTILITIES AND
TRANSPORTATION COMMISSION

Overview of Staff Testimony
Policy
Investor Supplied Working Capital
Change to Federal Tax Rate
Compliance with Last Rate Case
Maximum Allowable Operating Pressure (MAOP)

February 15, 2018

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I. INTRODUCTION

Q. Please state your name and business address.

A. My name is Betty A. Erdahl and my business address is the Richard Hemstad Building, 1300 S Evergreen Park Drive SW, P.O. Box 47250, Olympia, Washington, 98504. My email address is betty.erdahl@utc.wa.gov.

Q. By whom are you employed and in what capacity?

A. I am employed by the Washington Utilities and Transportation Commission (Commission) as a Regulatory Analyst in the Energy Section of the Regulatory Services Division.

Q. How long have you been employed by the Commission?

A. I have been employed by the Commission since June 1991.

Q. Please describe your education and relevant work experience.

A. I graduated from Washington State University in 1988 with a Bachelor of Arts degree in Accounting. I have also completed relevant coursework such as the "Basics of Regulation" offered by New Mexico State University, Rate Making Process Technical Program, USTA class on Understanding Separations, Access Charges, and Settlements, as well as Utility Ratemaking: The Fundamentals and the Frontier. Before joining the Commission in June 1991, I worked for two years as an accountant in the financial sector.

As a Regulatory Analyst, I am responsible for auditing the books and records of regulated companies, analyzing cost of service studies, and examining affiliated interest transactions. In addition, I participate in the development of Commission Staff's ("Staff") recommendations concerning tariff filings by regulated companies for presentation to the Commission at open public meetings and adjudications. I have also worked on policy recommendations relating to spin-offs and mergers of regulated companies, payphone deregulation, local calling areas, bundling of regulated and nonregulated telecommunications services, implementation of N11 pursuant to the Telecommunications Act of 1996, and numbering resources.

Q. Have you testified before this Commission?

A. Yes. I testified in Docket TG-920090, regarding affiliated interests of Waste Management, Inc.; Docket UT-950200, regarding a general rate case of US WEST Communications, Inc.; Docket UT-970066, regarding payphone access line rates of Toledo Telephone Company; Docket UT-020406, a complaint by AT&T Communications of the Pacific Northwest, Inc. against Verizon Northwest Inc.'s access charge rates; Dockets UE-111048/UG-111049, regarding a general rate case of Puget Sound Energy ("PSE"); and Docket UE-130043, regarding a general rate case of Pacific Power & Light Co. ("Pacific Power"). I also prepared testimony in Dockets UE-170485/UG-170486, regarding investor supplied working capital in a general rate case of Avista Corporation; Dockets UE-170033/ UG-170034, regarding investor supplied working capital in a general rate case of PSE; Dockets UE-140188/UG-140189, regarding a general rate case of Avista Corporation; Docket

UT-040788, regarding a general rate case of Verizon Northwest Inc.; Docket UT-051291, regarding affiliated interest contracts, overall earnings review, and provision of a quality of service guarantee program in the Sprint spin-off of its local exchange companies; Docket UT-082119, regarding retention of pre-merger settlement provisions, a requirement to offer a quality of service guarantee program, and affiliated interest reporting in the CenturyTel/Embarq merger case; and Dockets UE-140762, et al., regarding a general rate case of Pacific Power, including an adjustment to investor supplied working capital ("ISWC").

II. SCOPE AND SUMMARY OF TESTIMONY

Q. What is the purpose of your testimony in this proceeding?

A. I present Staff's policy testimony in this case, covering topics that include compliance with Cascade's 2015 rate case, use of estimates, and compliance with the Commission's order regarding documentation for maximum allowed operating pressure ("MAOP"). I am also responsible for the adjustment to the Company's ISWC, which Cascade includes as a line item in the per books rate base in the test year results of operations.[1] Staff's ISWC adjustment is identified as UTC-3. Staff's adjustment is intended to adjust per books ISWC calculated by the company. And finally, I propose UTC-4, an adjustment to reflect the impact of the Tax Cut and Jobs Act ("TCJA").

[1] *See* Parvinen, Exh. MPP-2 at 1, Row 23.

Q. Please provide a brief overview of your adjustments.

A. I recommend re-categorizing 16 accounts, which in turn changes the overall ISWC amount. The recommended change in the cash account categorization is a result of extraordinary cash amounts in Account 131, which I detail later in my testimony. I make a recommendation to disallow all deferrals related to MAOP documentation that brings the Company into compliance for post-code pipe. The ratepayers should not have to pay for costs that should have already been incurred after the code went into effect in 1971.

Next, I propose an adjustment based on the response to Bench Request No. 1 addressing the decrease to Federal Income Tax ("FIT") from 35 percent down to 21 percent. The per books taxes must be changed to reflect 21 percent and the conversion factor is changed to effect the incremental tax rate for all adjustments and revenue requirement. Staff calculates this estimated tax adjustment similarly to what was provided by the Company in Bench Request No. 1. Ms. Melissa Cheesman addresses the over collection of 2018 federal income taxes embedded in current rates.[2] Staff proposes to pass back this over collection to ratepayers.

Q. Are you sponsoring any exhibits in support of your testimony?

A. Yes, I have nine supporting exhibits.

Exh. BAE-2 depicts Staff's recommended investor supplied working capital amount for inclusion in rate base. Staff is proposing an adjustment to Cascade's working capital to arrive at its ISWC because the Company includes working capital

[2] Over collection is the current federal income tax rate of 21 percent minus the prior rate of 35 percent, which is currently embedded in rates today.

in the per books results of operations. My recommendation is incorporated into Staff witness Ms. Kristen Hillstead's Exh. KMH-2, Summary of Adjustments, as UTC-3.

Exh. BAE-3 shows the detailed account-by-account analysis for calculating Staff's proposed ISWC. Exh. BAE-3 shows each balance sheet account, the associated dollar values, and categorization or re-categorization, as applicable. I used the Company's response to UTC Staff Data Request No. 54 as a beginning point. The Company updated its originally filed ISWC calculation in this data request response.

Exh. BAE-4 is the Company's Response to UTC Staff Data Request No. 54. In responding to Staff's request, the Company discovered that four balance sheet accounts should be re-categorized and updated in the ISWC calculation, those accounts are highlighted green. Cascade's response, which I am including as an exhibit, supports Staff's Adjustment UTC-3 and shows that Staff and Cascade agree on several of the re-categorized accounts.

Exh. BAE-5 is a Staff analysis of cash on hand since 2006 for Cascade and the other three gas utilities the Commission regulates.

Exh. BAE-6 is Cascade's Supplemental Response to UTC Staff Data Request No. 57, which shows the Company's cash balances from 2006-2017 and explanations of use of those funds.

Exh. BAE-7 is Cascade's Response to PC Data Request No. 3 showing cash balances for January–October 2017.

Exh. BAE-8 is Staff's analysis of MAOP Deferrals, from Cascade's Response to UTC Staff Data Request No. 117, calculating pre-code and post-code percentages to apply to the average of monthly average ("AMA") balance sheet amounts.

Exh. BAE-9 is Staff's Estimated Tax Adjustment UTC-4 calculated by making changes to Ms. Kristen Hillstead's Exh. KMH-2 to determine the total impact of Staff's proposed case including the estimated tax adjustment.

III. POLICY

Q. What are the overall results of Staff's proposed case?

A. First, Staff responds to the case that was filed and proposes a <u>decrease</u> to current rates of $3,324,476 as seen on Exh. KMH-2 at 1, Column E. Staff bases its case on a 7.21 percent weighted average cost of capital with the return on equity at 9.35 percent and equity as 47.31 percent of total capital. The largest differences between Staff's proposal and the Company's proposal are changes to weather normalization and related adjustments, removal of incentive pay that is related to financial goals, difference in pro forma plant when determining what is major and by not including estimates in rates, the amount of allowed investor supplied working capital, and cost of capital. The individual adjustments are shown on Exh. KMH-2 at 2.

Secondly, Staff's proposed decrease of $3,324,476 does not include the impact to revenue requirement related to the TCJA corporate tax rate change from 35 percent to 21 percent. Staff decided to organize its case this way in an attempt to present an apples-to-apples comparison with what was initially filed by the Company, but then to also address the effect of the TCJA that was the subject of

Bench Request No. 1 in this case. Staff's calculation includes the impact of the tax rate change for the per books results as well as each of its proposed adjustments. The result of the tax adjustment, as calculated by Staff, is an additional decrease of $3,482,648. In conjunction with the rest of Staff's adjustments, Staff's **total recommended decrease to current rates is $6,807,124**.

Q. Please identify the members of Staff providing testimony in this case and a brief overview of Staff's recommendation?

A. The following is a list of Staff who provide testimony in this case and what adjustments/issues each person is responsible for:

- Mr. David Parcell proposes an overall rate of return, or weighted cost of capital, of 7.21 percent based on: a return on equity at 9.35 percent, a cost of debt at 5.295 percent, and a capital structure with 47.31 percent common equity and 52.69 percent long-term debt.
- Ms. Kristen Hillstead analyzed the Company's per books results, the Promotional Advertising Adjustment (R-2), the Pro Forma Interest Coordination Adjustment (P-1), the Wage Adjustment (P-2), removes Incentive Pay related to financial goals (UTC-1), removes Supplemental Income Security Plan ("SISP") and Supplemental Executive Retirement Plan ("SERP") expense (UTC-2), separates the wage adjustment into a restating piece (UTC-6), and is responsible for the Revenue Requirement model.
- Ms. Jing Liu analyzed the Weather Normalization Adjustment (R-1), Restate Revenue Adjustment (R-3), the Low-Income Bill Assistance Adjustment (R-

4), the Pro Forma Revenue Adjustment (P-9), and makes a proposal to update the design of the Low Income Program.

- Ms. Amy White analyzed the Company's per books results, the MAOP Deferral Amortization Adjustment (P-6), and the CRM Adjustment (P-8), and proposes UTC-5, removes 2014 arbitration expense included in the Company's per books balance.
- Mr. David Panco analyzed the Company's Pro Forma Plant Additions (P-3), Rate Case Costs Adjustment (P-4), Pro Forma Compliance Department Adjustment (P-5), and Miscellaneous Charge Changes Adjustment (P-7).
- Ms. Melissa Cheesman analyzed the Company's cost of service and rate design. She also testifies that Cascade must complete a load study before increasing basic charges and for any change in rates. Until then, Cascade must apply an equal percentage of margin to each schedule, except for Special Contracts. She also addresses impacts of the TCJA changes related to the pass-back of any over-collection[3] of 2018 federal income taxes embedded in current rates.
- Ms. Jennifer Snyder analyzed the Company's conservation commitments.

[3] Over collection is the current federal income tax rate of 21 percent minus the prior rate of 35 percent, which is currently embedded in rates today.

Q. What principles surface throughout Staff's adjustments and review of Cascade's case?

A. Cascade used estimates in many of its proposed adjustments in this case. Staff proposes only amounts that are known and measurable as prescribed by WAC 480-07-510 (3)(iii). The Company's estimates are rejected by myself and Staff witnesses: Ms. Kristen Hillstead, Ms. Amy White, and Mr. David Panco. Additionally, the Company proposes to update numbers on rebuttal. Staff is not able to address future changes in this case at this time and believes this practice creates a moving target in a limited timeframe.

Staff also discovered examples in the Company's initial filing that indicate it has not followed a number of agreed-upon terms and procedures contained in the Commission-approved settlement of Cascade's last general rate case ("2015 GRC Settlement").[4] First, the Company has not initiated a load study as agreed in the 2015 GRC Settlement. Company witness Mr. Brian Robertson testifies that Cascade does not have the equipment in place to take samples as part of the required load study. He also states that a load study would prove to be expensive and difficult.[5] Staff is unimpressed by the Company's reasons. Staff witness Ms. Melissa Cheesman recommends specific actions until a load study is completed.

Second, Cascade calculated but did not use the weather normalization method agreed to in the last settlement.[6] Staff witness Ms. Jing Liu addresses this issue and

[4] *Wash. Utils. & Transp. Comm'n v. Cascade Nat'l Gas Corp.*, Docket UG-152286, Order 04, 2, ¶ 7 (Jul. 7, 2016); *Wash. Utils. & Transp. Comm'n v. Cascade Nat'l Gas Corp.*, Docket UG-152286, Order 04, Exhibit A: Joint Settlement Agreement, 6-7, ¶¶ 15-17 (Jul. 7, 2016) [hereinafter "2015 GRC Settlement"].
[5] Robertson, Exh BR-1T at 8:12-13.
[6] 2015 GRC Settlement at 5, ¶ 13.

why her approach is more appropriate. Also, the Company includes expenditures and deferral amounts that have been rejected by the Commission in another order.[7] Staff's adjustments reflect that order and remove any amounts that relate to post-code pipe compliance from expenditures and from deferral amounts on the balance sheet. Staff recommends the Company be directed to remove any of these expenditures or deferrals in all future reporting to the Commission (Quarterly Reports, Commission Basis Report, any future per book number for a rate case or any other purpose).

IV. INVESTOR SUPPLIED WORKING CAPITAL

Q. What is cash working capital?

A. Cash working capital refers to the funds necessary to sustain a company in its day-to-day operations. The method of determining what amount is reasonable has evolved over time and various measures have been used. What is known as Rule of Thumb allowances is used by FERC and is also called the 1/8th method. This is a calculation applied to operating expenses, with various exclusions, plus an average of material and supplies inventory. As time has passed, the approach and calculation changed to allow other approaches including the Lead Lag Study method, and the Investor Supplied Approach, also known as the Balance Sheet method. The purpose of the Lead Lag Study method, the Balance Sheet method, and the 1/8th method is to determine a reasonable amount of cash that is necessary to meet the day-to-day

[7] *In the Matter of Cascade Nat'l Gas Corp.'s Pipe Replacement Program Plan*, Docket PG-160293, Order 01 (Apr. 7, 2016).

operations of the business. This is to compensate the investors for capital which they have supplied to enable the company to operate efficiently and economically and for which they would not otherwise be compensated.[8] Ultimately, ISWC is calculated by subtracting total investment from total invested capital.

Q. What differentiates Staff's ISWC proposal from Cascade's?

A. Cascade has an excessively large AMA balance of cash on its balance sheet. Staff noted the same concern in Cascade's last rate case, prior to the case's settlement. The problem with Cascade keeping such an enormous balance of cash on its balance sheet is that it receives the benefit of ISWC treatment on that balance, but then it also receives the benefit from using this cash in other ways that receive a ratemaking benefit, such as an allowance for funds used during construction ("AFUDC") when that cash is put towards building plant additions. Through its investigation, Staff has confirmed that the Company is proposing to double-recover on at least some of its cash balance in exactly this way. The Company's proposal for ISWC treatment is unfair, unjust, and unreasonable to ratepayers and Staff cannot support it. I present this in detail later in my testimony.

Q. What is the ratemaking perspective on cash working capital?

A. In rate setting, the goal is to directly measure whether or not investors actually supply working capital. It is only appropriate to allow a return on the amount of working capital the investors supply <u>and</u> for which they would not otherwise be

[8] *Wash .Utils. & Transp. Comm'n v. Pacific Power & Light Co.*, Cause No. U-9097, 2nd Supp. Order, 12, (Mar. 23, 1960).

compensated. But, if the investors otherwise receive a return on the amount they supply, it is inappropriate for those same funds to *also* receive a second return as AFUDC or from other interest-bearing sources. This is fair to both ratepayers and investors. Investors are still compensated for their investment of capital in the business and also are incentivized to continue to make such investments through the ability to earn a return on the capital they contribute into the businesses operations. Ratepayers benefit from a company's ability to utilize on-hand capital for day-to-day business operations in the providing of the utility service. The balance, from the ratepayer perspective, is that ratepayers should not be expected to compensate investors with multiple returns on the same capital contributions. It would not, therefore, be fair, just, or reasonable for investors to be compensated for capital that is earning ISWC treatment and be additionally compensated for that same capital through other sources.

Q. What is the concern for carrying large cash balances on a company's balance sheet?

A. The cash amount on the balance sheet should represent what is needed for day-to-day business operations, so one would expect to see a mildly fluctuating, but relatively constant balance, without any extraordinary peaks or valleys in the account balance. It is fair that ratepayers compensate investors for capital needed to operate the business from day-to-day, but it is not fair to require ratepayers to compensate investors based upon an exceptional, larger than usual cash account balance because that would overcompensate a company at an artificially high level that cannot be shown as fair or reasonable.

In this case, Cascade's cash balances are significantly higher than needed to meet its day-to-day business operations. The evidence of this is provided in Exh. BAE-6, Cascade's Supplemental Response to UTC Staff Data Request No. 57. In that response, the Company states the large cash balances are related to bond issuances to fund capital projects.

Q. What is the basic concept of the ISWC method?

A. Broadly speaking, the Balance Sheet method, which Staff will refer to as the ISWC method, measures the difference between the capital invested in a business and the investments in the business. In other words, ISWC is the amount of invested capital that was provided by investors and available for the company's use, over and above the company's investments in operating plant, non-operating plant, and other specific items of investment. If there is an excess of invested capital over investments, that amount is the working capital supplied by investors, or ISWC.

In summary, the ISWC method directly measures the amount of working capital <u>that investors provide</u> and for which they would not otherwise be compensated. If there is such an amount, it is included in rate base, earns a return, and is allocated to operating and non-operating segments of the business based on the ratio of investments in each segment.

Q. Who provides working capital besides investors?

A. Working capital may be provided by ratepayers or non-investors via various regulatory treatments such as deferred income taxes, unamortized investment tax credits, customer deposits, or trade creditors. A company has use of those funds for a period of time.

Q. In general, how is ISWC allocated to the regulated portion of Cascade's business?

A. Once the amount of investor supplied working capital is calculated for the corporation, there are two basic assumptions applied:

1. ISWC is used for both operating and non-operating investments; and
2. The operating investments and non-operating investments share pro-ratably any excess investor-supplied funds.

V. STAFF ADJUSTMENT UTC-3, ISWC

Q. Please summarize the fundamental flaws you have identified with Cascade's ISWC proposal.

A. More specifically, Staff recommends the Commission reject Cascade's ISWC proposal for the following reasons:

1) The Company uses non-normalized, extraordinary amounts of cash in its ISWC calculation. The Company requests the Commission include an

anomalous $34 million in ISWC in rate base, while the Company's "normal" level of cash is approximately $2 million.

2) Bond issuances made by the Company contribute to the extraordinarily high cash balance. The Company claims the cash received from these bond issuances will be used to pay back money to ratepayers from over-collected purchase gas adjustment ("PGA") revenues. The PGA refund is paid back over 12 months. And, while the Company is required to pay interest on the amount paid back to the customers, the Company pays less interest back to its ratepayers than it receives as a return on the account. This is a financial benefit to the Company, paid for by ratepayers. It is not fair or reasonable that ratepayers pay a full ROR on the extraordinarily high cash balance in return for refunds that are paid back over a 12-month period at a lesser interest rate.

3) The Company includes funds in ISWC that have already been invested in plant and, therefore, is already accumulating interest in the form of AFUDC. The Company is, again, attempting to earn double-recovery on investors' funds that are already receiving a return.

4) The Company is requesting a return on amounts that are disallowed for ratemaking purposes per Commission order related to compliance of post-code MAOP documentation. It is reasonable to hold the Company to compliance with the Commission's orders. And, in this instance, to a Commission order that specifically directs the Company as to what funds are disallowed for ratemaking purposes.

5) The Company requests a return on customer deposits that provide cash for investments, this is cash provided by *customers* not investors. It is unfair, unreasonable, and unjust for the Company to expect to receive ISWC treatment and benefit from capital invested by its customers

Q. How does Staff recommend the Commission resolve these flaws?

A. Staff recommends that the Commission adopt Staff's method of directly allocating the ISWC to the gas utility and non-operating[9] segments based on investment. Staff also recommends modifying the assignments of 16 balance sheet accounts within the ISWC to more appropriate categories. If the ISWC accounts that Staff has identified are not re-categorized, it will result in:

1) Ratepayers paying a full ROR on a cash balance that is extraordinary and far exceeds the amount of cash that Cascade needs in order to operate its day-to-day business. This is evidenced by the consistent history of cash balances that Cascade has kept, which has only coincidentally been extraordinarily high during the test year of this general rate case, and that of the Company's last general rate case.[10]

2) Ratepayers paying a full ROR on the cash used to refund the amounts that ratepayers have overpaid in gas costs, when in fact the Company is required to return interest on any over collections back to ratepayers.

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[9] Non-operating refers to the company operations outside of the regulated utility, construction work in progress ("CWIP"), accounts not allowed for ratemaking, and to investments that earn interest on their own accord.
[10] Erdahl, Exh. BAE-5.

3) Double-recovery by the Company in two ways. First, any cash assigned to the asset category that the Company uses to make investments in plant will, by the time rates go into effect, receive a full ROR in ISWC and be receiving AFUDC treatment in addition to ISWC treatment. Second, any cash assigned to the asset category in ISWC that the Company puts into an interest bearing account would receive that benefit in addition to ISWC treatment. Later in my testimony, I identify where Staff has discovered that the Company has used, and intends to continue using, cash for both of these purposes.

Staff recommends that the Commission reduce Cascade's regulated utility ISWC for Washington operations by approximately $13 million, from $25.6 million to $12.6 million.

Q. How does Cascade calculate the ISWC for Washington's operations?

A. Like Staff, Cascade uses the balance sheet method, but it allocates the result by dividing ISWC by total average investments (Cascade's ISWC ratio), then multiplies that percentage by total Washington investment. The Company's approach is confusing. Staff's approach is clear and straight-forward.

Q. Which exhibits show the differences between Staff's ISWC proposal and the Company's?

A. All of the exhibits are relevant and support Staff's proposal. But, specifically, Exh. BAE-2 provides a comparison of what the Company filed versus Staff's proposal, and Exh. BAE-3 documents the account-level calculation of Staff's methodology.

Exh. BAE-3 is a complete ISWC calculation, with all accounts listed, each account categorized, and allocations of ISWC to the Washington and Oregon regulated operations of the Company's business and to the non-operating segment of the business.

B. Details of Staff's Analysis

1. Specific calculation and Total dollar impact

Q. Please explain the foundations of Staff's analysis.

A. The starting point for my analysis is Cascade's total company trial balance as of December 31, 2016, on an AMA basis. The Company provided this information to Staff in response to a data request.[11]

Q. How did Staff calculate the total ISWC?

A. Staff reviewed the underlying balance sheet accounts, as shown in Exh. BAE-3. The amounts of each account (Column A) are put into one of four categories:

- Current Assets (Column B);
- Current Liabilities (Column C);
- Average Invested Capital (Column D); and
- Total Investments (Column E).

[11] Cascade's Response to UTC Staff Data Request No. 54.

Next, Exh. BAE-3 documents the "Total Investments" as sub-categorized into WA operating (Column F), OR operating (Column G), and non-operating (Column H). Next, the "Total Investments" are assigned or allocated as Washington Operating Investment-Rate Base, Oregon Operating Investment-Rate Base, and Non-Operating Investments. Staff then independently calculated ISWC by subtracting the total investments (Line 598, Column E) from the total invested capital (Line 598, Column D).

The resulting ISWC is $19,745,534. In other words, investors are supplying capital of about $19.7 million for Cascade's cash flow and day-to-day business needs. I provide a detailed, column-by-column explanation of Exh. BAE-3 later in my testimony.

Q. How did Staff allocate the $19,745,534?

A. As noted above, Staff allocated the $19.7 million of ISWC to three categories: WA operating, OR operating, and non-operating segments of Cascade's business: 64.3 percent is WA operating, 22.2 percent is OR operating, and 13.6 percent for non-operating based on investments. Therefore, investors supply the utility with about $17 million of the $19.7 million total ISWC for utility operations. Non-operating investments receive the balance of $2.7 million of working capital as calculated on Lines 597-602, Column H.

2. Rationale for re-categorizing accounts to non-operating; removing accounts from utility-related operations.

Q. What types of accounts did Staff assign to the non-operating category?

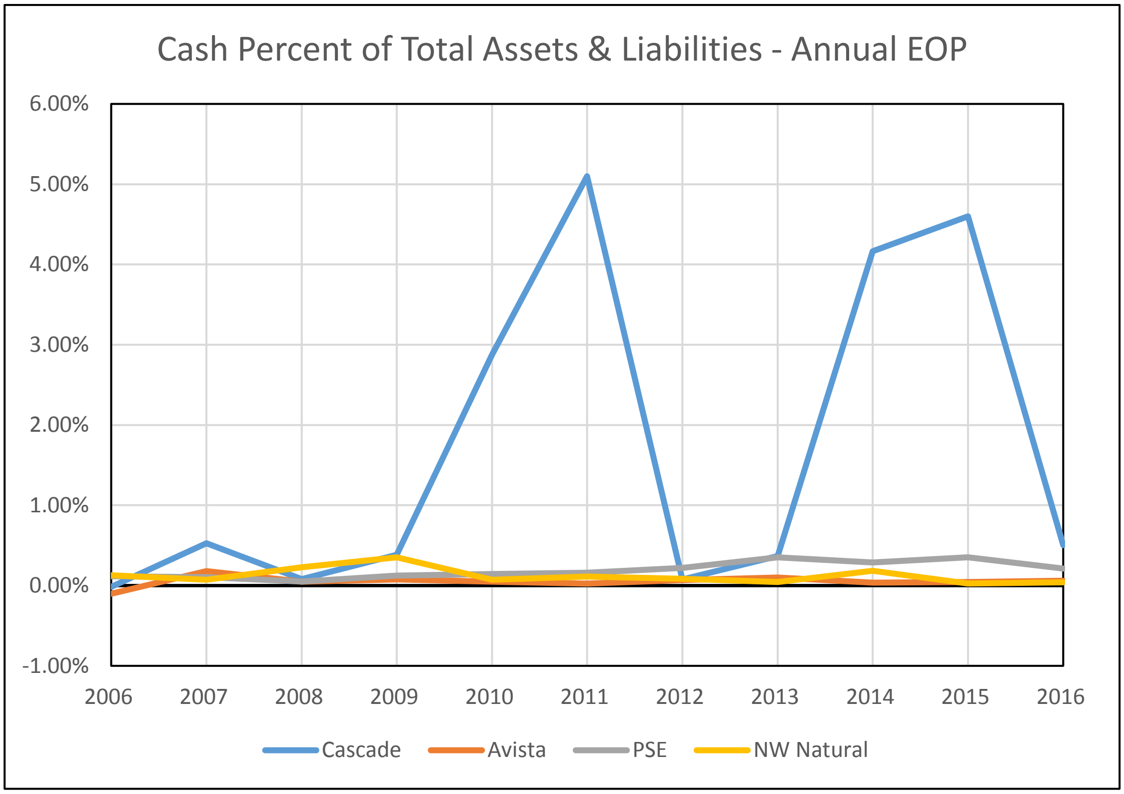
A. The following types of accounts were put into the non-operating category by Staff: accounts earning or accruing interest on behalf of Cascade or the ratepayers (e.g., bank accounts, escrow accounts, and PGA accounts); accounts that are not allowed for ratemaking purposes (e.g., charity and donations); and accounts that are directly related to non-utility operations. These accounts are not allowed to earn a return for ratemaking purposes to assure that ratepayers are not subsidizing non-utility operations or duplicating returns on interest-bearing investments. Either circumstance would be unfair, unjust, and unreasonable.

Additionally, Staff ensured that any account with disallowed expenditures per a prior Commission order, such as the MAOP post-code pipe, was assigned to the non-operating category so that ratepayers do not pay a return.

Q. Please explain Staff's adjustment to Cascade's Cash Account 131.

A. Staff assigns all cash, except for $2 million of the total $34 million in Cash Account 131, to the non-operating category. There are multiple reasons why this is the most fair and reasonable approach: first, as mentioned previously, the AMA cash balance is extraordinarily high, as shown in Exh. BAE-5 and Exh. BAE-7, and unreasonably exceeds the historical amounts that the Company has needed to keep in this account for its operations. Exh. BAE-5 illustrates Staff's calculation of the average cash balance for this account of just under $2 million for the last 10 years, while throwing out four high years and one low year.[12] The graph, below, reproduced from Exh. BAE-5, shows cash as a percentage of total assets and total liabilities at year end. These numbers have been taken from FERC Form 2 reports for Cascade, Avista, PSE, and NW Natural.

Figure 1. Cash Percentage of Total Assets & Liabilities – Annual EOP



The extraordinary peaks in 2011 and 2014-2015 illustrate that Cascade is an outlier, when compared with all of Washington's other natural gas utilities. Staff does not believe the Company should be rewarded at the customers' expense for its striking approach to cash management. Staff's recommended categorization of the

[12] Erdahl, Exh. BAE-5 at 1.

cash account adjusts the Company's account in line with what is typically on hand and necessary for its business purposes since 2006.

Further, in UTC Staff Data Request No. 57, marked now as Exh. BAE-6, Staff inquired about: cash balances from 2006–present, the reason for swings in account balance, and the explanation for the use of the cash. The Company provided the following information for the cash balances in 2010-2016:

> 2010 "Largely related to natural gas refundable to customers (balance was up to $18.5M December 2010)."[13]
>
> 2011 "Largely related to natural gas refundable to customers (balance was up to $20.1M April 2011)."[14]
>
> 2012 "Combination of natural gas refundable to customers (balance was as high as $29.4M April 2012) and $46M of debt due within 12 months."[15]
>
> 2013 "Primarily one month in 2013 (August $4.6M) possibly to increasing line of credit too much to meet the month's operation needs. Balance on LOC increased $10M from July 2013 to august 2013."[16] (The AMA cash balance in 2013 was $1,303,193.)
>
> 2014 "Issued $25M in debt November 2014 **to fund future capital projects** and growth."[17]
>
> 2015 "Issued $25M in debt January 2015 **to fund future capital projects** and growth."[18]
>
> 2016 "Cash balance is a residual balance from the previous two debt issuances **to fund capital projects** and growth. Also funded operational expenses during decreased revenue generating months."[19]

The Company's response indicates that debt was issued and used, or will be issued and used, for capital investments, among other things. Capital investments

[13] Erdahl, Exh. BAE-6 at 2.
[14] Erdahl, Exh. BAE-6 at 2.
[15] Erdahl, Exh. BAE-6 at 2.
[16] Erdahl, Exh. BAE-6 at 2.
[17] Erdahl, Exh. BAE-6 at 2 (emphasis added).
[18] Erdahl, Exh. BAE-6 at 2 (emphasis added).
[19] Erdahl, Exh. BAE-6 at 2 (emphasis added).

earn AFUDC, which provides that the Company may add interest to the cost of a capital project during the time it takes to build the project. The increase to the cost of the project is then recovered by the Company as a greater depreciation cost over the life of the plant. Allowing the Company to recover a full regulated ROR from ratepayers on tens of millions of dollars in cash that just sits on its balance sheet in addition to receiving AFUDC treatment for the same funds is double-recovery on that temporary asset. To avoid such double-recovery, Staff determines it is proper to re-categorize this excess cash for ratemaking purposes. Even if this cash is used to reimburse ratepayers for over-collected purchased gas costs from the PGA, it remains unfair and unjust because the purchased gas balances accrue interest to the benefit of customers: effectively, Cascade would earn a return from customers for cash the customers provided in the first place. This should not be allowed.

Exh. BAE-7 shows that Cascade's Cash Account 131 is down to a balance of $46,376 as of October 2017.[20] Also, the Exh. BAE-6 shows an AMA Cash Balance of $4,463,291. The Company did not choose to move this cash to an interest bearing account, but if it had, to illustrate Staff's concern, the funds would have earned interest yet another time. Other utilities in Washington, under similar circumstances, have put cash in Account 136 Temporary Cash, instead. The cash earns some amount of interest and is categorized as a non-operating investment. This should not come as a surprise to Cascade: from 2006-2009 it maintained a balance ranging from $2.3 million to $8 million in its Account 136 Temporary Cash Investments.

[20] Cascade's Response to Public Counsel Data Request No. 3.

Staff re-categorized most of Cash Account 131 as non-operating because this account far exceeds what is a normal amount of cash to have on hand to run the business day-to-day. If the Commission does not find Staff's adjusted six-year average of $2,000,000 compelling, then Staff would also accept an alternative adjustment: the unadjusted average of $10.3 million.[21] This amount is still significantly higher than cash accounts in relation to current assets and total liabilities at other utilities in Washington, but the amount would not be as unjust and unfair as allowing the Company's proposal to remain unchanged.

Regardless of the amount to which the Commission decides is fair, just, and reasonable to reduce the balance in Cash Account 131, it is clear that a reduction is required. The level of cash currently in the account far exceeds what is necessary for the Company's day-to-day business and is reasonable for the Company to receive ISWC treatment.

Q. Please explain Staff's other adjustments to Cascade's ISWC.

A. Portions of two deferral accounts were moved to the non-operating category because they relate to Cascade's compliance with post-code documentation of MAOP on its system. It is not fair to make ratepayers pay for documentation of MAOP when it has been a federal requirement since 1971. Until 2015, Cascade had not filed a general rate case since 2006. The fact that the Company did not incur expenditures to comply with federal requirements, is a reflection of management decisions, which resulted in those cost savings flowing to shareholders. It is not fair to saddle

[21] Exh. BAE-5 at 3, fifth column from the left.

ratepayers with this cost. Staff assigned amounts related to post-code compliance of MAOP into the non-operating investment category and also calculated a percent of the pre-code/post-code amount to put into the non-operating category based on post-code footage of pipe. This is consistent with Staff witness Ms. Amy White's treatment of the post-code MAOP expenses. Compliance of post-code pipe must be paid for by the shareholders and not the ratepayers, as instructed by the Commission in Order 01 of Docket PG-160293.[22] Staff advocates that the Company comply with the Commission's order.

The other two accounts that Staff categorized differently than Cascade are Customer Deposits, Accounts 2351 for Washington and Oregon. Staff re-categorizes the Customer Deposit Accounts to WA Operating Investment and OR Operating Investment in order to recognize that a portion of rate base is funded by customer deposits that earn interest.

Q. What about the accounts that Cascade has already corrected or revised in response to Staff's data requests?

A. As I noted above, Cascade identified four accounts that the Company categorized incorrectly in its initial filing. The Company re-categorized those accounts in an updated ISWC calculation provided in Exh. BAE-4.[23] Staff and the Company agree that the accounts should be re-categorized for two reasons: the account for dividends declared was re-categorized from current liability to invested capital, and three Misc.

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[22] *In the Matter of Cascade Nat'l Gas Corp.'s Pipe Replacement Program Plan*, Docket PG-160293, Order 01 (Apr. 7, 2016).
[23] Cascade's Response to UTC Staff Data Request No. 54.

Deferral 186 accounts were originally categorized as current assets and are re-categorized to non-operating. The three deferral accounts are Oregon deferrals that earn interest. The exhibits I provide along with my testimony already incorporate the Company's revisions and corrections as well as my account-by-account analysis in Exh. BAE-3, which also reflects the Company's acknowledged changes.

C. Explanation of Exhibits

Q. Please walk through your Exh. BAE-2.

A. The starting point for my analysis is Cascade's total company trial balance sheet as of December 31, 2016, on an AMA basis, shown in Exh. BAE-4.[24]

Exh. BAE-2 shows that the total average invested capital on Line 3 less the total average investments on Line 16 equals the ISWC of $19.7 million shown on Line 18, Column D. The ISWC is then allocated between Washington operating of $12.7 million, Oregon operating of $4.3 million, and non-operating of $2.7 million, as shown on Lines 23, 26, and 30, respectively. The ISWC amount is allocated based on the percentage of total average investment: Washington operating investments are 64.26 percent on Line 24; Oregon operating investments are 22.16 percent on Line 27; and, non-operating investments are 13.58 percent on Line 30.

[24] *Id.*

Q. Please explain how ISWC is calculated in Exh. BAE-3.

A. Column A shows Cascade's total company balance sheet as of December 31, 2016, with AMA balances. These amounts go into the following categories and columns:

- Current Assets (Column B);
- Current Liabilities (Column C);
- Average Invested Capital (Column D); and
- Total Investments (Column E).

Next, Exh. BAE-3 documents the "Total Investments" as sub-categorized into Washington operating (Column F), Oregon operating (Column G), and non-operating (Column H).

Once all accounts are categorized appropriately, total investments are subtracted from average invested capital to determine whether the investors have provided working capital to meet the day-to-day needs of the business. Staff's ISWC calculation of $19,745,534 (shown on Line 598, Column E) is the amount being provided by investors. This $19,745,534 is then allocated based on operating and non-operating investment and divided by the total average investments to get each component's prorated share of working capital. The calculated allocation factors are shown on Line 600, Columns F, G, and H: 64.26 percent for Washington operating; 22.16 percent for Oregon operating; and, 13.58 percent for non-operating.

The percentage for each of these categories is then multiplied by Staff's proposed working capital amount on Line 598, Column E to determine the amount of working capital that should be allocated to each category on Lines 602, Columns F, G, and H. Ultimately, Staff believes the proper AMA cash balance that should remain in Account 131 as a current asset and receive ISWC treatment is $2,000,000.

VI. STAFF ADJUSTMENT UTC-4, CHANGE IN TAX LAW

Q. Please summarize Staff's recommendation for the TCJA.

A. Staff recommends the Commission decrease Cascade's effective tax rate to reflect the TCJA change effective January 1, 2018. Staff proposes an adjustment as a place holder, calculated similarly as to the one provided by the Company in its response to Bench Request No. 1. Staff's calculation is slightly different in that the per books tax change is calculated on the Operating Report tab rather than on the per books column of the Results of Operations tab, as done by the Company. Staff is uncertain about the alteration of the Investment Tax Credit ("ITC") Adjustment in Account 411.4 and does not change this amount in its calculation. This amount is only $37,382 which is immaterial. There is no justification from the Company explaining why it changed the ITC. This tax adjustment is a place holder and should be updated as parties better understand the impact of the TCJA.

Q. Please explain Staff's proposed tax calculation.

A. Staff makes two changes to its final revenue requirement model and compares the two results to get the difference that makes up the estimated tax adjustment. First, Staff changes the conversion factor to reflect 21 percent FIT instead of the prior 35 percent FIT. Second, similar to Cascade's proposal, but in a different spreadsheet, Staff changes two tax numbers on the operating report by dividing by 35 percent and then multiplying by 21 percent. Staff does not change the ITC mainly due to a lack of certainty that doing so is necessary. This results in a slightly different tax number than calculating it the Company's way. Any revisions or improvements to the FIT calculations may be deferred and implemented at a later date.

The calculation of the estimated tax adjustment is shown on Exh. BAE-9, Column G. I started by considering Ms. Kristen Hillstead's Exh. KMH-2. I took Exh. KMH-2 and changed the tax rate to 21 percent, as mentioned above, which resulted in Staff's total case recommendation, after the estimated tax adjustment, of $6.8 million. The tax adjustment amount was calculated by subtracting Staff's pre-tax decrease to revenue requirement of $3.4 million from the total proposed decrease after tax of $6.8 million, resulting in an additional decrease to revenue requirement of approximately $3.5 million. My understanding is that this method is consistent with how the Company has made its changes for the tax adjustment.

VII. CONCLUSIONS

Q. What are your conclusions?

A. For the reasons I have stated, the Commission should support Staff's method for calculating working capital. It should:

- Categorize each account as shown in Exh. BAE-3;
- Allow only $2 million of cash from account 131 as a current asset for ISWC consideration.; and

- Allocate ISWC based on percentage of total average investment as shown in Exh. BAE-2.
- Adjust the revenue requirement amount to decrease the booked amount of FIT and adjust the FIT related to all adjustments to reflect the new tax rate of 21 percent.
- Disallow all expenditures and deferrals related to compliance of MAOP post-code pipe as directed by the Commission in Order 01 of Docket PG-160293.[25]
- Require the Company to complete a load study, with the conditions that the Company may not increase basic charges and may only seek an equal percentage of margin increase for any rate request, except for Special Contracts, until the load study is complete.

Q. Does this conclude your testimony?

A. Yes.

[25] *In the Matter of Cascade Nat'l Gas Corp.'s Pipe Replacement Program Plan*, Docket PG-160293, Order 01 (Apr. 7, 2016).