BEFORE THE
WASHINGTON UTILITIES AND TRANSPORTATION COMMISSION

WASHINGTON UTILITIES AND TRANSPORTATION COMMISSION,
 	
      Complainant,
 	
   v.
 	
PUGET SOUND ENERGY,
 	
      Respondent.
	Docket UE-22____
	Docket UG-22____

SECOND EXHIBIT (NONCONFIDENTIAL) TO
THE PREFILED DIRECT TESTIMONY OF

MATTHEW R. MARCELIA

ON BEHALF OF PUGET SOUND ENERGY

JANUARY 31, 2022

1 **PUGET SOUND ENERGY**

2 **SECOND EXHIBIT (NONCONFIDENTIAL) TO THE PREFILED**
3 **DIRECT TESTIMONY OF MATTHEW R. MARCELIA**

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PUGET SOUND ENERGY

SECOND EXHIBIT (NONCONFIDENTIAL) TO THE PREFILED
DIRECT TESTIMONY OF MATTHEW R. MARCELIA

I.   ADDITIONAL DETAIL ON BOOK AND TAX
DEPRECIATION PROJECTIONS

A.   Overview

Q.   Please provide an overview of the process used to project book and tax

depreciation.

A.   For all assets in the multiyear rate plan, Puget Sound Energy ("PSE") projected

book and tax depreciation on a monthly basis. The book depreciation rates were

used based on the applicable depreciation studies. The tax depreciation rates were

taken from the modified accelerated cost recovery system ("MACRS") tables.

From that activity, PSE calculated the accumulated deferred income tax ("ADIT")

activity and excess deferred income tax ("EDIT") activity. The accumulation of

this data provides what is needed to calculate gross rate base and accumulated

depreciation on an average of monthly averages ("AMA") basis and the ADIT on

the IRS proration method for the multiyear rate plan.

**Q.   How did you do this from a technology standpoint?**

A.   The process of running all these calculations on existing assets (i.e., assets in

service and included in rate base as of the end of the test year June 30, 2021) and

future assets on a monthly basis from July 2021 through December 2025

1		generates a significant amount of data. While these calculations are relatively
2		straight-forward, the sheer volume presents challenges which are beyond the
3		capacity of Microsoft Excel. So, while Excel remains the preferred tool, PSE
4		processed these calculations in Alteryx and output the results to Excel for use in
5		the multiyear rate plan.
6		One notable exception to Alteryx was the use of PowerTax to calculate the tax
7		deprecation, ADIT, and EDIT activity on existing assets throughout the multiyear
8		rate plan. Given that those assets are in the middle of their useful lives, i.e., part
9		way through their book, tax, and ADIT lives, the most expeditious approach was
10		to roll that system forward for those calculations.
11	**Q.**	**Can you provide a visual aid for this process, before you get into more**
12		**detail?**
13	A.	Yes, Table 1 provides an overall flowchart of the process. The process flows from
14		left to right, starting with the June 30, 2021 "Source" data from PowerPlant and
15		PowerTax and the projections for the new property additions. The next area
16		depicts the addition of "Control" tables to support the calculations that occur in
17		the "Process" column. All calculations are performed in the "Process" column
18		which produces "Outputs" at the level of detail needed to support the multiyear
19		rate plan, which is depicted in the final column.

1

Table 1: Flowchart of the Process
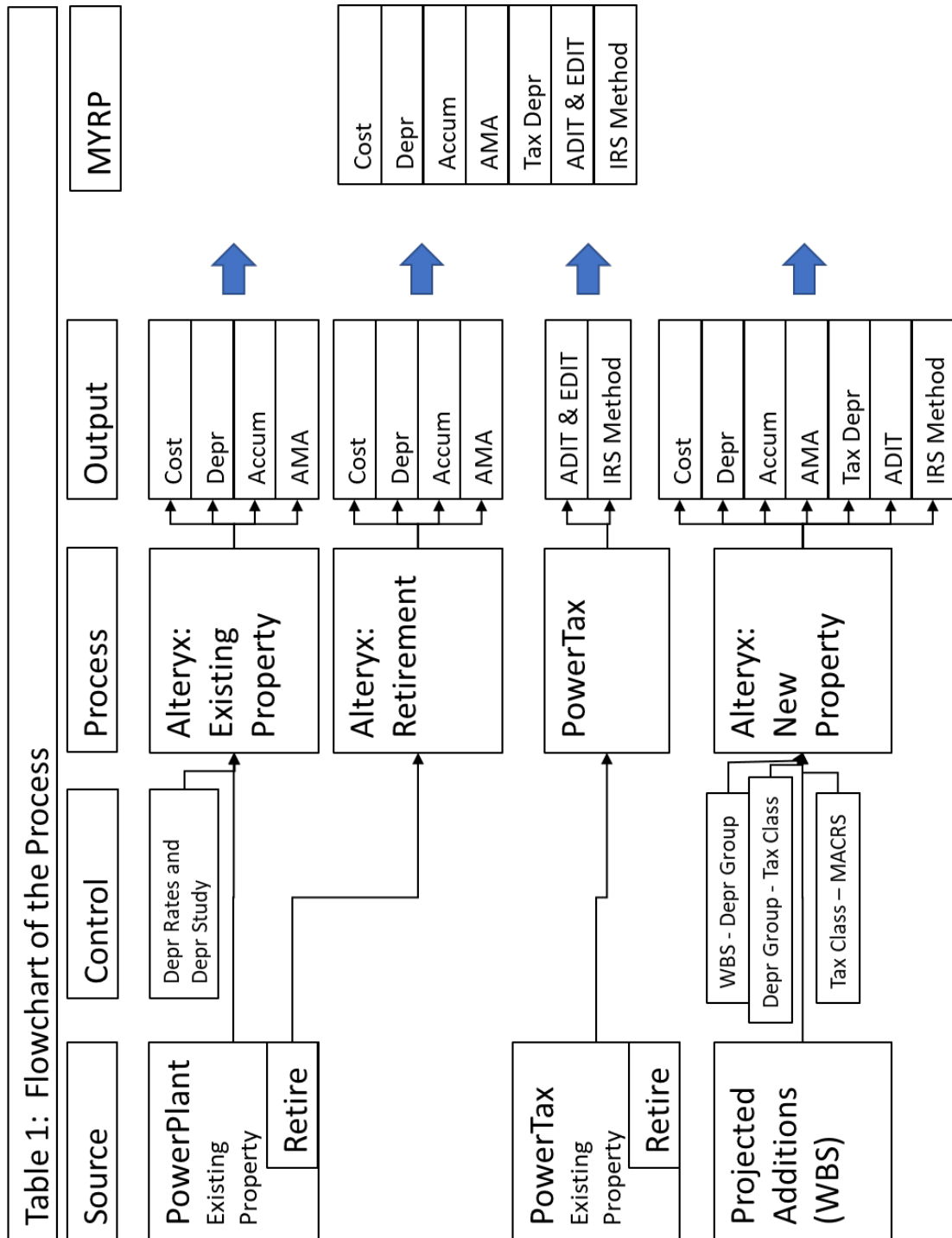
B.   Projections for Existing Property ("EP")

Q.   Please elaborate on the process for EP.

A.   For the EP, PSE extracted book data from PowerPlant for all assets in service at June 30, 2021. This data included primarily the original cost, accumulated depreciation, and depreciation rate. From this data, PSE projected book depreciation and accumulated depreciation on a monthly basis.

The book depreciation that was calculated became an input to PowerTax in order to compare the projected book deprecation with the projected tax deprecation to establish the projected movement in ADIT. This also determined the movement in EDIT within PowerTax. One of the strengths of the PowerTax system is its ability to calculate and control the movement in deferred taxes, especially the application of the average rate assumption method ("ARAM") to the reversal of EDIT. This approach allowed PSE to use standard PowerTax reports to see the tax and ADIT results for the EP.

Q.   Does this approach comply with the IRS normalization requirements?

A.   Yes, it does. The book depreciation projection is used (a) for cost of service, (b) in accumulated depreciation and rate base, and (c) in calculating ADIT and EDIT

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1   activity. Tax depreciation is calculated on the same assets and for the same time

2   periods that are used for book depreciation.

3   **C.**   **Projections for New Property ("NP")**

4   **Q.**   **Please elaborate on the process for NP.**

5   A.   The projections for the NP are derived from PSE's projection for the projects it

6   expects to pursue. The Prefiled Direct Testimony of Joshua A. Kensok, Exh.

7   JAK-1T, discusses the process for tracking budgets and actuals for formally

8   approved projects. To use this data, it must be converted from the project-level[1]

9   to the depreciation group ("DeprGroup") level.[2] It is not uncommon for a project

10   at the WBS level to encompass assets falling under various DeprGroups.

11   Based on historical activity and other information, PSE created a control file to

12   translate the WBS project-level data to the appropriate DeprGroup(s).

13   When a project is placed in service, book depreciation begins using the half-

14   month convention. The depreciation rate comes from the same depreciation data

15   extracted from PowerPlant that is used for the EP, discussed above.

16   Because this is new property, the tax depreciation and ADIT activity can be

17   calculated outside of PowerTax using the MACRS tables and follows the standard

18   tax conventions of half-year depreciation in the first year. The difference between

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[1] At PSE, the project-level is often referred to as the WBS. Generally, each project has a unique WBS number. The work breakdown structure (WBS) is the data element within SAP which is used to track projects and budgets.

[2] The DeprGroup can also be used to determine the FERC account.

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1	book and tax depreciation is used to calculate the ADIT activity. These
2	calculations are performed on a monthly basis.
3	Further refinement was made to account for the different cost basis between book
4	and tax. There are differing capitalization rules between book (FERC) and tax
5	(IRS) accounting which often, but not always, permit the tax basis of an asset to
6	be smaller than the book basis. One example of this is tax repairs, which allows
7	for an upfront tax deduction of some costs, while those same costs must be
8	capitalized for book purposes. An opposing example would be contributions in
9	aid of construction, which reduces the capitalized cost for book purposes but for
10	tax purposes is treated as taxable income when received and an increase to
11	capitalized cost. The overall impact of all basis differences results in a smaller
12	tax basis which has the effect of increasing the ADIT balance. PSE projected the
13	basis difference by using a three-year average of the actual activity in PowerTax
14	from 2018 through 2020, similar to the approach used for projected retirements,
15	discussed below.
16	There is no EDIT with respect to the NP as it is new property placed in service
17	post TCJA.
18	To determine the correct tax depreciation by DeprGroup, PSE extracted the book
19	to tax mapping table from PowerTax. This allowed the matching of the correct tax
20	deprecation rates with each DeprGroup.

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D. Retirements

Q. What did you do with asset retirements after the test year?

A. PSE created an asset retirement model based on the actual book and tax retirements recorded in 2018, 2019, and 2020. From that activity, a number of non-recurring retirements were removed (e.g. Colstrip Units 1 and 2 shutdown, the sale of water heaters, etc.) to create a retirement model by DeprGroup, by month, and by vintage. A further refinement was made with respect to AMR retirements to replace the historical activity with PSE's projected replacement plan for those assets. The same adjustments were made to both book and tax retirements.

For the book retirements, PSE treated them as if they were negative additions that went into service on the date of the retirement. Negative depreciation was calculated from that point onward. The impact of the negative addition and the negative depreciation was netted against the EP to create the "after-retirement" results reported in the multiyear rate plan for the EP.

For the tax retirements, PSE recorded the modeled retirements in PowerTax. Once recorded, PowerTax applies the tax retirement against the tax basis of the tax assets in order to calculate the correct tax depreciation and ADIT activity for each tax year. The impact of tax retirements are then available in standard Power Tax reports for EP.

1	**E. EDIT Reversals**
2	**Q. Can you explain how the EDIT reversal will work in the multiyear rate plan?**
3	A. The reversal pattern for the plant-related timing difference will continue to follow
4	the ARAM for EDIT reversal, consistent with Order 14 from PSE's 2019 general
5	rate case. For the historical test year ending June 30, 2021, the historical EDIT
6	reversal that was recorded for that period is presented in PSE's Tax Adjustments
7	in the Prefiled Direct Testimony of Ms. Susan E. Free, in Exhs. SEF-3 and SEF-
8	11 in Adjustments 6.04 and 11.04 for electric and gas operations, respectively.
9	From this starting point, the EDIT reversal is determined for each period, the pro
10	forma period, the gap year, and multiyear rate plan, years 2023 through 2025. In
11	each period, the book depreciation that has been calculated for that period has
12	been posted into Power Tax. When matched against the tax deprecation on the
13	assets, the ADIT and EDIT activity is determined.
14	In short, the EDIT reversal will be matched with the book depreciation. When the
15	book depreciation rates change (e.g. due to the depreciation study that is being
16	requested in this case and which is sponsored in the Prefiled Direct Testimony of
17	Ned W. Allis, Exh. NWA-1T), the EDIT reversal will change in a like manner.
18	**II. CONCLUSION**
19	**Q. Does that conclude your additional explanation for the book and tax**
20	**depreciation projection?**
21	A. Yes, it does.