

**EXHIBIT NO. ___(KRK-7T)
DOCKET NO. UE-072300/UG-072301
2007 PSE GENERAL RATE CASE
WITNESS: KARL R. KARZMAR**

**BEFORE THE
WASHINGTON UTILITIES AND TRANSPORTATION COMMISSION**

**WASHINGTON UTILITIES AND
TRANSPORTATION COMMISSION,**

Complainant,

v.

PUGET SOUND ENERGY, INC.,

Respondent.

**Docket No. UE-072300
Docket No. UG-072301**

**PREFILED SUPPLEMENTAL DIRECT TESTIMONY
(NONCONFIDENTIAL) OF KARL R. KARZMAR
ON BEHALF OF PUGET SOUND ENERGY, INC.**

APRIL 11, 2008

PUGET SOUND ENERGY, INC.

**PREFILED SUPPLEMENTAL DIRECT TESTIMONY
(NONCONFIDENTIAL) OF KARL R. KARZMAR**

CONTENTS

I. INTRODUCTION1

II. UPDATE TO RATE BASE.....1

III. UPDATE TO REVENUE REQUIREMENT2

IV. CONCLUSION.....11

1 **PUGET SOUND ENERGY, INC.**

2 **PREFILED SUPPLEMENTAL DIRECT TESTIMONY**
3 **(NONCONFIDENTIAL) OF KARL R. KARZMAR**

4 **I. INTRODUCTION**

5 **Q. Are you the same Karl R. Karzmar who provided prefiled direct testimony**
6 **in this Docket on behalf of Puget Sound Energy, Inc. (“PSE” or “the**
7 **Company”)?**

8 A. Yes.

9 **Q. What topics are you covering in your prefiled supplemental direct**
10 **testimony?**

11 A. I present the update to gas rate base and working capital as well as an update to
12 several pro forma and restating adjustments for new information that has become
13 available to the Company since its original filing made on December 3, 2007.

14 These changes to rate base and to the pro forma and restating adjustments result
15 in an adjustment to the Company's total revenue deficiency from the \$56,770,922
16 set forth in PSE's December 3, 2007 filing to \$58,066,055. This represents an
17 average 5.44% increase as compared to the 5.31% increase in the Company's
18 original filing.

1 **II. UPDATE TO RATE BASE**

2 **Q. Please explain Exhibit No. ___(KRK-8)?**

3 A. The First Exhibit to my Prefiled Supplemental Direct Testimony, Exhibit
4 No. ___(KRK-8), contains only pages 8.03, 8.04 and 8.06, which present similar
5 information as pages 3.03, 3.04 and 3.06 to the Second Exhibit to my Prefiled
6 Direct Testimony, Exhibit No. ___(KRK-3), but corrects the classification of the
7 renewable energy credits within the working capital computation. Within the
8 working capital computation renewable energy credit was reclassified from non
9 operating investment to investor supplied capital thereby reducing working
10 capital by \$76,250. After apportionment, both gas working capital and ratebase
11 are reduced by \$20,087 to \$37,061,609 and \$1,351,380,079 respectively as shown
12 on lines 13 and 14, Exhibit No. ___(KRK-8), page 8.03.

13 **III. UPDATE TO REVENUE REQUIREMENT**

14 **Q. Have you provided a summary of the changes which occurred since the**
15 **original filing and their impacts on the revenue deficiency?**

16 A. Yes. Included in the workpapers with this supplemental filing is a table of
17 contents which provides a comprehensive list of all relevant exhibits in this
18 proceeding taking into consideration this supplemental filing. This table of
19 contents also provides guidance on where the electronic versions of each exhibit
20 and its supporting electronic workpapers can be found. Additionally, a table has

1 been provided which reconciles, by adjustment, the revenue deficiency from the
2 original filing to that included in this supplemental filing. A summarized version
3 of this table is presented later in my testimony.

4 **Q. Please explain Exhibit No. ___(KRK-9)?**

5 A. The Second Exhibit to my Prefiled Supplemental Direct Testimony, Exhibit
6 No. ___(KRK-9), presents similar information as the Third Exhibit to my Prefiled
7 Direct Testimony, Exhibit No. ___(KRK-4), after being updated for the revisions
8 described later in my prefiled supplemental direct testimony. The first column on
9 page 9-A in this exhibit, titled “Actual Results of Operations 12 ME Sept. 30,
10 2007”, sets forth the ratebase and actual operating results for the test year ended
11 September 30, 2007. The columns to the right of this first column show the
12 impact of the pro forma and restating adjustments PSE is proposing for the pro
13 forma rate year. For the adjustments that have changed since the December 3,
14 2007 filing, we have marked the columns as “**REVISED**”.

15 Each adjustment is presented in more detail on the succeeding pages referenced in
16 the title of a particular column. The total of the test year amounts plus the pro
17 forma and restating adjustments is shown in the column titled “Adjusted Results
18 of Operations” on page 9-D of Exhibit No. ___(KRK-9).

19 The work papers supporting the December 3, 2007 adjustments have been
20 previously provided to Commission Staff and intervenors. For each adjustment
21 that is marked "**REVISED**," new workpapers supporting the adjustment have

1 been provided. The numbers that changed in each adjustment as a result of this
2 supplemental filing have also been presented in bold and italic font.

3 **Q. Have you prepared a reconciliation between the revenue deficiency filed in**
4 **December 2007 and the current revenue deficiency?**

5 A. Yes. The following table shows the impact of each of the pro forma and restating
6 adjustments, in excess of \$100,000, on the December 2007 revenue deficiency.

Description	Adjustment	Revenue Deficiency (\$000s)
As filed December 3, 2007		\$56,770.9
Depreciation Study	9.06	594.6
Miscellaneous Operating Exp.	9.09	315.2
Property Taxes	9.10	383.9
Interest on Customer Deposits	9.13	(214.7)
Incentive Pay	9.21	111.6
Other less than \$100,000		104.6
Updated Revenue Deficiency		\$58,066.1

7 **Q. Please explain the changes for each of the pro forma and restating**
8 **adjustments.**

9 A. I will provide an explanation of each of the adjustments that change and provide a
10 comparison to the net operating income or ratebase impact of each adjustment as
11 originally filed in Exhibit No. ____ (KRR-4). The adjustments are presented in the
12 same page order as they were originally filed.

1 **Adjustment 9.01, Temperature Normalization**, merely corrects the temperature
2 normalization adjustment as the result of a change in the conversion factor caused
3 by a correction of bad debt expense in adjustment 9.08, as discussed later in my
4 supplemental testimony. Net operating income, as a result of this adjustment, is
5 decreased by \$15,227,800 versus a decrease of \$15,228,597 in the original filing.
6 *See Exhibit No. ___(KRK-9), page 9.01.*

7 **Adjustment 9.02, Revenues and Expenses**, corrects for the change in the
8 conversion factor as discussed above and explained in Janet Phelps' Prefiled
9 Supplemental Direct Testimony, Exhibit No. ___(JKP-14T). Net operating
10 income, as a result of this adjustment, is increased by \$16,968,370 versus an
11 increase of \$16,941,026 in the original filing.

12 **Adjustment 9.03 and Adjustment 9.04** There is no change to the original filing
13 amounts shown in **Adjustment 4.03 and 4.04**.

14 **Adjustment 9.05, Tax Benefit of Pro forma Interest**, reflects the cumulative
15 impact of changes to ratebase made to other adjustments. Net operating income
16 is decreased by \$7,205,484 versus a decrease of \$7,156,868 in the original filing.
17 *See Exhibit No. ___(KRK-9), page 9.05.*

18 **Adjustment 9.06, Depreciation Study**, is being adjusted for several updates
19 made in the depreciation study provided by Mr. C. Richard Clarke. Other parties
20 to this filing have received these updates through revised and supplemental data
21 request responses and Mr. Clarke will provide an updated study at rebuttal. These

1 changes include corrections for adjusting the acquisition value only of certain
2 meters and other equipment for study purposes, without adjusting the
3 corresponding reserve. The adjustment now decreases net operating income by
4 \$14,034,111 versus a decrease of \$13,654,359 in the original filing, and decrease
5 ratebase by \$4,587,231 versus \$4,463,810 in the original filing. *See Exhibit*
6 *No. ___(KRK-9), page 9.06.*

7 **Adjustment 9.07, Pass Through Revenues and Expenses**, corrects for a change
8 in the bad debt and state utility tax portion of the conversion factor used in
9 calculating adjustments to pass-through revenue. The change in the conversion
10 factor caused by this correction of bad debt expense is discussed in adjustment
11 9.08, immediately following. Net operating income, as a result of this adjustment,
12 is increased by \$1,432,025 versus an increase of \$1,428,845 in the original filing.
13 *See Exhibit No. ___(KRK-9), page 9.07.*

14 **Adjustment 9.08, Bad Debts**, corrects the bad debt calculation for a write-off
15 associated with bankruptcies that was booked in December 2007. After the
16 original filing, it was discovered that the Company had not been notified of the
17 resolution of several bankruptcies that impact the years 2003 through 2007. This
18 correction reflects the bad debt expense write-offs in the years that would have
19 been recorded had they been booked when these court decisions had occurred.
20 The total adjustment now decreases net operating income by \$276,135 versus a
21 decrease of \$228,386 in the original filing. *See Exhibit No. ___(KRK-9), page*
22 *9.08. The bad debt rate also changes to 0.2780080% versus 0.2720635% in the*

1 original filing which impacts both the bad debt and state utility tax components of
2 the conversion factor, which is reported in Exhibit No. ___(KRK-10), page 10.03.

3 **Adjustment 9.09, Miscellaneous Operating Expense**, has several corrections.

4 After the original filing it was found that the accounting for Company employee
5 association stores items had been recorded in some above the line accounts on the
6 Company's books. Previously the accounting for these items had been
7 maintained separately. The adjustment on lines 7 through 9 removes \$13,348 of
8 revenues net of costs associated with inventory for this activity, increasing net
9 operating income by \$8,676. In the future this activity will be recorded below the
10 line. See Exhibit No. ___(KRK-9), page 9.09.

11 After the filing the Company agreed to a Commission Staff suggestion that the
12 amortization associated with the Summit Building purchase option¹ be amortized
13 equally over the remaining life of the building lease rather than the Company's
14 original proposal to shape the amortization to lease payments over a seven year
15 period. This adjustment shown on line 12 of Exhibit No. ___(KRK-9), page 9.09,
16 reflects this reduction in amortization to \$548,888 compared to the original filing
17 of \$923,525. This change in the amortization reduces net operating income by
18 \$243,514 from the original filing.

19 Line 14 of this adjustment reflects savings associated with the New York Stock

¹ Docket No UE-071876 Petition For an Accounting Order Authorizing Deferred Accounting Treatment for terminating and removing a transferable purchase option from a building lease agreement.

1 Exchange Filing Fee if the merger is approved. This fee would no longer be
2 necessary as the Company's stock would no longer be traded on that exchange. If
3 the merger is not approved then this amount will need to be removed from this
4 adjustment. Lines 17 through 19 of this adjustment remove labor and related
5 overheads that should have been charged to the merger work order during the test
6 year. Because the Company is not requesting recovery of merger related costs,
7 this labor should be removed from the test year in the same manner as the labor
8 directly charged to the merger activity. These merger-related changes decrease
9 net operating income \$38,784.

10 The total miscellaneous operating expense adjustment now increases net
11 operating income by \$231,967 versus an increase of \$428,022 in the original
12 filing. *See* Exhibit No. ____ (KRK-9), page 9.09.

13 **Adjustment 9.10, Property Tax**, updates the property tax ratio used in
14 determining the property tax to reflect the Department of Revenues final property
15 valuation used in 2007. The adjustment now decreases net operating income by
16 \$1,234,767 versus a decrease of \$996,079 in the original filing. *See* Exhibit
17 No. ____ (KRK-9), page 9.10.

18 **Adjustment 9.11 and Adjustment 9.12** There is no change to the original filing
19 amounts shown in **Adjustment 4.11 and 4.12**.

20 **Adjustment 9.13, Interest on Customer Deposits**, updates the interest
21 calculation for the lower cost of interest since the original filing. The adjustment

1 now decreases net operating income by \$187,784 versus a decrease of \$321,319
2 in the original filing. See Exhibit No. ___(KRK-9), page 9.13.

3 **Adjustment 9.14 and Adjustment 9.15** There is no change to the original filing
4 amounts shown in **Adjustment 4.14 and 4.15**.

5 **Adjustment 9.16, Property and Liability Insurance**, corrects the liability
6 insurance expense test year amount reflected in the income statement to reflect
7 the actual amount incurred in the test year. The adjustment now decreases net
8 operating income by \$85,111 versus a decrease of \$115,718 in the original filing.

9 **Adjustment 9.17, Pension Plan** There is no change to the original filing amount
10 shown in **Adjustment 4.17**.

11 **Adjustment 9.18, Wage Increase**, corrects the percentage increase used for the
12 union wages to reflect the actual percentage increase. In addition, the wages
13 removed in the **Miscellaneous Operating Expense Adjustment** are removed
14 from this calculation. The adjustment now decreases net operating income by
15 \$1,474,301 versus a decrease of \$1,443,449 in the original filing.

16 **Adjustment 9.19, Investment Plan**, reflects the changes made to the **Wage**
17 **Increase Adjustment**. The adjustment now decreases net operating income by
18 \$61,592 versus a decrease of \$61,108 in the original filing.

19 **Adjustment 9.20, Employee Insurance** There is no change to the original filing
20 amount shown in **Adjustment 4.20**.

1 costs for each capital category. The capital structure and costs are presented in
2 the Prefiled Direct Testimony of Mr. Donald E. Gaines, Exhibit No. ___(DEG-
3 1T). The rate of return is 8.60% and 7.29% net of tax. This Exhibit page has not
4 changed from the original filing.

5 **10.03 Conversion Factor**

6 The conversion factor, shown on Exhibit No. ___(KRK-10), page 10.03, is used
7 to adjust the net operating income deficiency for revenue sensitive items and
8 Federal income tax to determine the total revenue deficiency. The revenue
9 sensitive items are the Washington State utility tax, Washington Utilities and
10 Transportation Commission filing fee, and bad debts. The conversion factor used
11 in the revenue requirement calculation, taking into consideration the adjustments
12 to bad debt expense, adjustment 9.08 discussed earlier, and its resultant impact on
13 the state utility tax component of the conversion factor, is .62193 versus the
14 .62196 used in the original filing.

15 **IV. CONCLUSION**

16 **Q. Does that conclude your prefiled supplemental direct testimony?**

17 A. Yes, it does.