

Exhibit No. \_\_ (JOINT-1T)  
Docket Nos. UE-060266/UG-060267  
Witnesses: Jim Lazar  
Donald Schoenbeck  
Joelle Steward

BEFORE THE WASHINGTON STATE  
UTILITIES AND TRANSPORTATION COMMISSION

WASHINGTON UTILITIES AND  
TRANSPORTATION COMMISSION,

Complainant,

v.

PUGET SOUND ENERGY, INC.,

Respondent.

DOCKET NOS. UE-060266  
DOCKET NO. UG-060267  
(Consolidated)

JOINT TESTIMONY OF JIM LAZAR, DONALD SCHOENBECK  
AND JOELLE STEWARD

NATURAL GAS RATE SPREAD, RATE DESIGN AND LOW INCOME BILL  
ASSISTANCE

July 25, 2005

1 I. INTRODUCTION

2  
3 Qualifications of Jim Lazar

4 Q. Please state your name and the party for whom you are appearing.

5 A. My name is Jim Lazar and I am appearing on behalf of Public Counsel and The  
6 Energy Project. My qualifications are presented in Exhibit No. \_\_ (JOINT-2).

7  
8 Qualifications of Donald Schoenbeck

9 Q. Please state your name and the party for whom you are appearing.

10 A. My name is Donald Schoenbeck and I am appearing on behalf of Northwest  
11 Industrial Gas Users (NWIGU). My qualifications are presented in Exhibit No. \_\_  
12 (JOINT-3).

13  
14 Qualifications of Joelle Steward

15 Q. Please state your name and the party for whom you are appearing.

16 A. My name is Joelle Steward and I am appearing on behalf of Commission Staff. My  
17 qualifications are presented in Exhibit No. \_\_ (JRS-2), which is part of my individual  
18 testimony on decoupling and other matters.

19  
20 Q. What is the purpose of this Joint Testimony?

21 A. The purpose of this Joint Testimony is to present the common recommendation of  
22 Staff, Public Counsel and the Northwest Industrial Gas Users (hereinafter

1 collectively referred to as “Joint Parties”) on the topics of natural gas rate spread and  
2 rate design, and natural gas low-income bill assistance.

3  
4 **Q. Have you prepared any exhibits in support of your recommendations?**

5 A. Yes. They are:

6 Exhibit No. \_\_ (JOINT-4): Commission Basis Cost of Service

7  
8 Exhibit No. \_\_ (JOINT-5): Joint Proposal on Natural Gas Rate Spread, Rate  
9 Design and Low-Income Bill Assistance

10  
11 Exhibit No. \_\_ (JOINT-6): Natural Gas Rate Spread and Rate Design

12  
13 Exhibit No. \_\_ (JOINT-7): Residential Basic Charge Calculation  
14

15  
16 **II. JOINT TESTIMONY ON NATURAL GAS RATE SPREAD**

17  
18 **Q. Please describe rate spread and the policy interests that are important for**  
19 **consideration.**

20 A. Rate spread allocates the revenue requirement to each of the Company’s customer  
21 classes. Rate spread should recognize that rates must be just and reasonable and not  
22 cause undue discrimination. To this end, rate responsibility for any class should be  
23 informed by the cost to serve the class. Therefore, a cost of service study is an  
24 important consideration in spreading a revenue increase. However, the Commission  
25 has often stated that factors in addition to cost weigh in the rate spread decision,  
26 including the appearance of fairness, perceptions of equity, economic conditions in  
27 the service territory, and stability.

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**Q. Please explain what a cost of service study is and how it is used to allocate an increase across customer classes.**

A. A cost of service study is an analytical tool that assigns to each class the costs incurred to serve them. It provides useful information to indicate if a customer class is paying more or less than those costs. A class that is paying 100 percent of its cost is considered to be at “parity”. A class is over or under “parity” if it is paying more or less than its costs, respectively.

We commonly calculate a revenue-to-cost ratio from the results of the cost of service model to assess where a class is in relation to parity. Our ultimate goal is always to move classes towards parity since cost causation is an important aspect of finding that rates are “fair, just, reasonable and sufficient”. We use the revenue-to-cost ratio as a guide to determine what size increase a class should get in order to move them towards, or keep them close to parity.

**Q. Should cost of service study results be mechanically applied?**

A. No. Cost studies are an important guide in allocating and designing rates, but they contain a fair amount of judgment on classification and allocation and thus should not be mechanically applied. The Commission has reiterated this on several occasions.<sup>1</sup> Rate spread and rate design decisions are usually tempered by consideration of customer impacts and any other pertinent factors appropriate at the time.

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<sup>1</sup> See, for example, Commission orders in Docket Nos. UE-991832, UG-940034, U-89-2688 and U-86-100.

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**Q. Did the Joint Parties rely on a cost of service study in preparing the rates?**

A. The rate spread (and rate design) proposed by the Joint Parties is guided by the results of two cost studies: the Commission Basis study and the proposed PSE Study.

The Commission Basis cost of service study employs the methodologies previously approved by the Commission for natural gas cost studies in earlier litigated cases. A summary of the results of this study was provided by Company witness Janet Phelps in her workpapers and later updated in a data request, which we include here as Exhibit No. \_\_ (JOINT-4).

In the PSE Study, the Company made a significant change to the peak demand allocator, which is a key allocator in the study. The Company relied on this study to prepare its natural gas rates. The PSE Study allocates peak demand on a system design peak day whereas the Commission Basis study defines a peak day as the average of the five highest days in the three most recent years.

The result of this difference is that the PSE Study, under the “peak-and-average” methodology, classifies 40 percent of distribution main costs as commodity related and 60 percent as demand related, whereas the Commission Basis study classifies 42 percent of main costs as commodity related and 58 percent as demand related.

**Q. What are the results of the two cost studies?**

A. Table 1 below shows the differences in the revenue-to-cost ratios from the two cost studies.

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**Table 1**

<i>Customer Class</i>	<i>Commission Basis Cost Study</i>	<i>PSE Cost Study</i>
Residential – Sch 23	1.01	0.98
Comm & Indus – Sch 31 & 36	0.98	0.97
Large Volume Firm – Sch 41	1.25	1.29
Interruptible – Sch 85	1.36	1.56
Limited Interruptible – Sch 86	1.41	1.89
Non-Excl. Interr – Sch 87	0.92	1.52
Transportation – Sch 57	1.25	1.87
Contracts	0.73	1.14
Compressed Natural Gas	0.02	0.02
Rentals	0.64	0.63
Total	1.00	1.00

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**Q. What is the Joint Parties' proposed natural gas rate spread?**

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A. The Joint Parties proposed rate spread is outlined on page 1 in Exhibit No. \_\_

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(JOINT-5). Exhibit No. \_\_ (JOINT-6) presents this rate spread at the Company's

1 proposed revenue deficiency of \$39,211,573. This exhibit also includes a comparison  
2 of this proposal to PSE's rate spread, which is presented by Company witness Janet  
3 Phelps in Exhibit No. \_\_ (JKP-7).

4  
5 **Q. Please explain why the parties believe that this rate spread is in the public**  
6 **interest.**

7 A. While there were differences in the results of the two cost studies, we found some  
8 consistent threads we could use to create a fair and reasonable rate spread.

9 The cost studies consistently show the same classes as being over-parity or  
10 under-parity, with the exception of Schedule 87 and Contracts. Other than these two  
11 schedules, the primary difference is the degree to which the interruptible Schedules  
12 85 and 86 and transportation Schedule 57 are above parity.

13 For Schedules 85, 86, 87 and 57, and Contracts we recommend a total  
14 increase of \$576,000 to be allocated to these classes. This amount was a compromise  
15 based on different rate spread proposals discussed by the joint parties. The Joint  
16 Parties agree that this level of increase is reasonable at any revenue deficiency  
17 determined by the Commission in this proceeding.

18 The allocation of the \$576,000 between these schedules falls out through rate  
19 design because these schedules share many of the same charges. Specifically, they  
20 share the same rates for the procurement charge and the delivery-related demand  
21 charge on the interruptible schedules, the third block delivery charge on Schedules  
22 85, 87 and 57, and the all of the delivery charges on Schedules 87 and 57.

1            Similar to the Company's proposed rate spread, these schedules all receive a  
2 below-average increase in recognition that they are above parity in both cost studies,  
3 with the exception of Schedule 87 in the Commission Basis study. Although the  
4 Commission Basis study shows Schedule 87 to be slightly below parity, we took into  
5 consideration the revenue-to-cost ratio for Schedules 87 and 57 combined, since  
6 these customers receive the same delivery service. Combined, these schedules are  
7 above parity in both cost studies; therefore, a below-average increase is reasonable  
8 for Schedule 87 in rate spread.

9  
10 **Q. Please explain why the allocations to the other classes are in the public interest.**

11 **A.** For the other classes, there wasn't a significant difference between the results of the  
12 cost studies, but we did refine some of PSE's allocations to these classes.

13            For the residential class, we allocated 100 percent of the average increase  
14 since both cost studies showed the class to be nearly at parity – one study slightly  
15 over parity and the other study slightly under parity. The Company's proposed  
16 increase of 110 percent of average appears unreasonable for this reason. Similarly,  
17 we allocated the commercial and industrial class 105 percent of the average increase  
18 since both studies show the class to be just slightly below parity.

19            For Schedule 41, Large Volume High Load Factor, we allocated 85 percent  
20 of the average increase because this schedule is above parity in both studies. While  
21 we agreed with the Company that this class should receive a below-average increase,  
22 we found the Company's allocation to be unreasonable.



1           There is no difference between the Joint Parties rate spread and the  
2 Company's proposed rate spread for Rentals, Contracts and Compressed Natural Gas  
3 (CNG). We found the Company's allocations to these schedules to be reasonable.

4           Any remaining unallocated increase is spread proportionally to the  
5 residential, commercial and industrial, large volume and Compressed Natural Gas  
6 classes.

7           The Joint Parties believe that this proposed rate spread is in the public interest  
8 because it makes efforts to move all classes toward parity, but with attention to the  
9 results of different cost studies and to minimizing severe customer impacts.

10  
11           **III. JOINT TESTIMONY ON NATURAL GAS RATE DESIGN**

12  
13 **Q. Please describe the importance of rate design.**

14 A. Rate design is the pricing mechanism for the Company to recover its costs. Rate  
15 design determines the rates that each individual customer actually pays. As a result,  
16 rate design is important for the same reasons that rate spread is important.

17  
18 **Q. What are the policy interests involved in rate design?**

19 A. There are a variety of interests that need to be addressed. Rates should be designed to  
20 correctly reflect costs and to provide for revenue collection within customer classes  
21 that is fair and reasonable. The joint proposal balances a number of considerations  
22 including the following. It is important to provide customers with appropriate price  
23 signals, as individual consumption and conservation decisions will be affected by the

1 prices customers are charged. Minimizing rate shock for customers, that is, a sudden  
2 and severe change in utility rates, is another important regulatory policy interest. The  
3 rate design should also provide the utility with a reasonable opportunity to recover its  
4 revenue requirement. Finally, rates should not be overly complex, so that most  
5 customers can readily understand how they are charged for electric or gas service.

6  
7 **Q. Were these principles applied in order to develop the proposed gas rate**  
8 **structures?**

9 A. Yes.

10  
11 **Q. What is the Joint Parties' proposed rate design for natural gas rates?**

12 A. The Joint Parties' rate design is outlined on pages 2-3 in Exhibit No. \_\_ (JOINT-5).  
13 Additionally, we revised Company witness Ms. Phelps Exhibit No. \_\_ (JKP-7) to  
14 show the rates using this rate design at the Company's proposed revenue deficiency  
15 of \$39,211,573. This is presented in Exhibit No. \_\_ (JOINT-6), beginning on page 2.  
16 This exhibit also includes the estimated bill impacts, beginning on page 7.

17  
18 **Q. First, please explain why the proposed rate design for residential customers,**  
19 **Schedule 23 is reasonable and in the public interest?**

20 A. There are only two components in the residential Schedule 23, a customer charge  
21 and a flat delivery charge. The Joint Parties agreed that a \$0.75 increase in the basic  
22 charge is reasonable, with any remaining increase applied to the delivery charge.

1 The Joint Parties did not agree on the methodology that should be used for  
2 computing the customer charge.

3 Exhibit No. \_\_ (JOINT-7) presents the customer charge calculation with  
4 service lines included at 100 percent costs, 50 percent costs, and with no service  
5 lines. At 100 percent of the service line cost included, the calculation supports a  
6 customer charge of nearly \$11.00. If we exclude service lines, the calculation  
7 supports a customer charge of \$6.31, which is close to the current customer charge of  
8 \$6.25.

9 Given this range of reasonable analytical results, we find that a customer  
10 charge of \$7.00, which is an increase of 12 percent, is fair, particularly in the light of  
11 the fact that the class increase is less than five percent. The customer charge has been  
12 increased by more than two-times the average increase. This is preferable to the  
13 Company's proposed rate design for the residential class of a 29 percent increase in  
14 the customer charge because it is a more gradual change, it reflects the range of  
15 reasonableness in cost analysis, it will encourage energy conservation and the  
16 efficient use of natural gas, and it places less burden on small use customers.

17  
18 **Q. What are the differences between the Joint Parties' rate design and the PSE**  
19 **proposed rate design for commercial and industrial Schedules 31, 36 and 51?**

20 A. The main difference is that the Joint Parties' proposal gives Schedule 31 a smaller  
21 increase of \$2.50 to the basic charge to \$17.50 per month, rather than the \$5.00  
22 proposed by the Company. Similar to our position on the residential basic charge, we  
23 found that a 33 percent increase in the basic charge, as proposed by PSE, had

1 unreasonable impacts on smaller customers, particularly in light of the lower revenue  
2 requirement presented in Staff's case. Other than this, the differences between the  
3 two proposals for these customers are minimal.  
4

5 **Q. What are the differences between the Joint Parties' rate design and the PSE**  
6 **proposed rate design for Large Volume Schedules 41?**

7 A. The Joint Parties' proposal provides smaller increases to the customer charge and the  
8 demand charge than proposed by PSE. Like the other schedules, we gave a smaller  
9 increase to the basic charge in order to moderate increases to the smaller customers  
10 on this schedule. For the demand charge, PSE proposed a 100 percent increase. As a  
11 result, this charge would collect more than two times the Company's total allocated  
12 increase to the class, resulting in a 10 percent decrease in the delivery charge. Even  
13 at the Joint Parties' higher allocated increase to the class, the 100 percent increase to  
14 the demand charge disproportionately collects more of the revenue increase. In order  
15 to balance the increase across the customer charges, the Joint Parties propose a 40  
16 percent increase in the demand charge to \$0.70.  
17

18 **Q. Please explain the Joint Parties recommended rates for the interruptible and**  
19 **transportation Schedules 87 and 57.**

20 A. The starting point for the Joint Parties Schedule 57 and 87 rate design was PSE's  
21 proposed charges for these rate schedules. However, our primary goal was to narrow  
22 the very large cost of service disparity between Schedules 57 and 87 rate charges.  
23 Since these schedules have the same volumetric rate charges, the most

1 straightforward manner to close this pricing gap is through the setting of charges  
 2 unique to each rate schedule. These charges are the customer charges, the  
 3 procurement charge applicable to Schedule 87 sales service, and the balancing  
 4 charge for Schedule 57 transportation service. Accordingly, the Joint Parties  
 5 recommend increasing the Schedule 87 customer charge to \$800 per month,  
 6 increasing the procurement charge to 0.65 cents/therm but with the total Schedule 57  
 7 balancing charge maintained at its present rate—and not accept PSE’s proposed  
 8 increase---0.061 cents/therm. Finally, to achieve the targeted revenue increase for  
 9 Schedules 57 and 87, the second block volumetric rate is increased from PSE’s  
 10 proposed charge of 7.65 cents/therm to 8.205 cents/therm. The following table  
 11 compares the Joint Parties recommendation with the PSE proposal for these two rate  
 12 schedules.

**Comparison of Schedules 57 & 87**

	<u>PSE Proposal</u>	<u>Joint Parties</u>
57 Customer Charge	\$800.00	\$800.00
87 Customer Charge	\$500.00	\$800.00
Demand Charge	\$1.02	\$1.02
87 Procurement Charge	\$0.0050	0.0065
57 Balancing Charge	0.00140	0.00061
First 25,000 Therms	\$0.12512	\$0.12512
Next 25,000	\$0.07650	\$0.08205
Next 50,000	\$0.04950	\$0.04950
Next 100,000	\$0.03255	\$0.03255
Next 300,000	\$0.02405	\$0.02405
All Over	\$0.01905	\$0.01905

13

14 **Q. Please explain the Joint Parties recommended charges for Schedule 85 and 86.**

15 **A.** The Joint Parties recommend that the same procurement charge of 0.65 cents/therm  
 16 be used for these schedules as well. With this exception, PSE’s proposed rates,

1 coupled with a slight increase to the first volumetric charge of each tariff, were used  
 2 to achieve the revenue increase from these schedules. The following table compares  
 3 the Joint Parties' recommendation with the PSE proposal for these two rate  
 4 schedules.

**Comparison of Schedules 85 & 86**

	<b>PSE Proposal</b>	<b>Joint Parties</b>
85 Customer Charge	\$500.00	\$500.00
86 Customer Charge	\$100.00	\$100.00
Demand	\$1.02	\$1.02
Procurement	\$0.0050	\$0.0065
85 Delivery		
First 25,000	\$0.09570	\$0.10000
Next 25,000	\$0.07150	\$0.07150
All Over 50,000	\$0.04950	\$0.04950
86 Delivery		
First 1,000	\$0.2052	\$0.2100
All Over	\$0.1552	\$0.1552

5  
 6 **Q. What are the differences between the Joint Parties' rate design and the PSE**  
 7 **proposed rate design for Rentals Schedules 71, 72 and 74?**

8 A. First of all, we apply an increase to all the schedules since the class is below parity.  
 9 PSE had not applied an increase to Schedule 72 since they were given larger  
 10 increases in the last rate case. We found that 25 percent of the average was  
 11 reasonable for these customers to reflect that costs are increasing. For Schedule 71,  
 12 we applied a 125 percent of the average increase since these customers received no  
 13 increase in the last case. PSE had included a constraint that none of the rates in  
 14 Schedule 71 would receive more than \$1.00 increase. This constraint is reasonable  
 15 and should be retained. Schedule 74 is given a 250 percent of the average increase,  
 16 which is a little less than the Company's proposal. The appliance models on this

1 schedule are older models that are costly to maintain and not efficient, therefore we  
2 apply a higher increase to encourage customers to move to more efficient models.  
3

#### 4 **IV. JOINT TESTIMONY ON PURCHASED GAS COST ALLOCATION**

5

6 **Q. Do the Joint Parties accept Puget's proposed change in purchased gas cost**  
7 **allocation?**

8 A. No. The testimony of Ms. Phelps at page 20-21 indicates that the proposed change  
9 follows the Company's revised cost allocation methodology, including the use of  
10 design-day peak allocation methods. Because not all of the Joint Parties accept that  
11 methodology, we recommend that the Commission continue to use the current  
12 methodology.  
13

#### 14 **V. LOW INCOME BILL ASSISTANCE**

15

16 **Q. What is the proposal of the Joint Parties with respect to low-income bill**  
17 **assistance for natural gas customers?**

18 A. We recommend an increase in the amount of the low-income bill assistance program  
19 for natural gas customers of \$525,000 (net of taxes and revenue sensitive items)  
20 above the current level of \$2.8 million. Together with the increase agreed to by all  
21 parties in the electric rate proceeding, the total increase in low income bill assistance  
22 is \$1.75 million. PSE proposed a \$1 million increase.  
23

1 **Q. Why is this appropriate?**

2 A. Natural gas rates have increased sharply since the low income bill assistance  
3 program was initiated. This adjustment to the low income bill assistance program  
4 will enable the program to provide a similar level of benefit, relative to the total  
5 natural gas bills of low income consumers. Basically, it keeps the program  
6 proportionate to the bills.

7

8 **Q. How have the Joint Parties agreed to allocate this increase across customer**  
9 **classes?**

10 A. The increase of \$525,000 will be allocated across classes on the same basis as the  
11 existing Schedule 129 surcharge, which is an equal percent of margin increase. The  
12 amount of revenue generated by the Schedule 129 surcharge, applied to test year  
13 sales levels, is increased by \$525,000.

14

15 **Q. Does this conclude the joint testimony?**

16 A. Yes.