

BEFORE THE WASHINGTON
UTILITIES AND TRANSPORTATION COMMISSION

WASHINGTON UTILITIES AND
TRANSPORTATION COMMISSION,

Complainant,

v.

PUGET SOUND ENERGY, INC.
Respondent.

DOCKET PG-060215

NARRATIVE SUPPORTING
SETTLEMENT AGREEMENT

I. INTRODUCTION

1 This Narrative Supporting Settlement Agreement is filed as documentation supporting the Settlement Agreement (Agreement) filed March 3, 2008. *See* WAC 480-07-740(2)(a). The Agreement resolves all contested issues in the proceeding. *Agreement* ¶ 26. The Agreement is subject to Commission approval. *Agreement* ¶¶ 1, 26 and 27. The Agreement is effective on the date of the Commission order approving it. *Agreement* ¶ 27. Part V below (¶¶18-36), contains each Party's separate statement in support of the Agreement.

II. PARTIES

2 The signatories are the two parties to this docket: Puget Sound Energy, Inc. ("PSE" or "the Company") and the Staff of the Washington Utilities and Transportation

Commission (“Staff”) (collectively, “the Parties”). *Agreement* ¶ 2. Consequently, the Agreement represents a “full settlement” pursuant to WAC 480-07-730 (1).

III. NATURE OF THE DOCKET¹

3 This docket involves a Commission Complaint issued May 23, 2007. The Complaint alleges certain violations of Commission statutes and rules. The Complaint is addressed to PSE, though PSE uses a contractor named Pilchuck Contractors, Inc. (Pilchuck) to do much of PSE’s gas leak activities. All of the violations in this docket involve work performed by Pilchuck. Pilchuck did not intervene in this docket.

4 Commission rules require PSE to have and follow a written gas pipeline safety manual that conforms to applicable gas safety laws and rules. *WAC 480-93-999, adopting 49 C.F.R. § 192.605(a); see also Complaint* ¶¶ 5-7. PSE has such a manual.

5 One of the provisions in PSE’s manual deals with gas leaks called “phantom leaks,” which are often called “P leaks.” P leaks are leaks that previously have been classified (*i.e.*, gas was detected), but after subsequent investigation, no gas is detected and no known repair was made. PSE’s manual requires that a follow-up inspection take place within 30 days of the date the leak was classified as a P leak. *See Complaint* ¶ 6. We call this the “30 day requirement.” In addition, the manual requires that the follow-up inspection be conducted by a person different than the person who classified the P leak in the first place. *Id.* We call this the “different person requirement.”

6 Commission rules also require PSE to maintain accurate gas leak records. When a leak inspection is performed, PSE must include, among other things, the date of the

¹ The Complaint contains three Causes of Action, but only the Causes of Action 1 and 2 are pertinent at this point. The Cause of Action 3 alleges 43 Incidents where PSE allegedly failed to maintain leak records as required. *Complaint* ¶¶ 27-29. However, during discovery, PSE provided virtually all of these records that it did not provide to Staff during Staff’s pre-Complaint investigation. Staff would not have pursued Cause of Action 3 had these records been available initially.

inspection and the name of the person who did the inspection. *WAC 480-93-187(1)*; see also *Complaint ¶ 8*.

7 In the Cause of Action 1, the Complaint alleges 84 separate Incidents in which PSE, through its contractor Pilchuck, failed to observe the second person requirement and the 30 day requirement. *Complaint ¶¶ 5-7*. According to the detailed allegations in Complaint Attachment 1, the same person did the follow-up leak evaluation, and Pilchuck knew it. See, e.g., *Complaint Attachment 1, Incident 1, ¶ 2*.

8 In the Cause of Action 2, the Complaint alleges 82 Incidents in which PSE, through its contractor Pilchuck, failed to maintain correct gas safety records because an incorrect name or date was placed on gas leak work orders, and Pilchuck knew the information was incorrect. *Complaint ¶¶ 23-26*. In these Incidents, though the same person did the follow-up P leak inspection, a different person's name was placed on the form. Or, if a P leak follow-up inspection was performed late, the form was backdated. See, e.g., *Complaint Attachment Incident 1 ¶ 2 (name) and Incident 84, ¶ 173 (date)*.

9 Through PSE's Answer (June 12, 2007) its First Amended Answer (July 31, 2007) and its Response to Staff's Request for More Information (August 12, 2007), PSE admitted that much of the alleged conduct did in fact occur, and that it was intentional, e.g., it was not the result of an honest mistake.

10 Staff thoroughly investigated this matter,² and filed its Report of Investigation on March 10, 2008. In that report, Staff describes its investigation and its findings, and analyzes how and why the Company's standards were not followed. Staff notes that the

² In its investigation, Staff used formal discovery methods in almost all instances. Staff issued numerous data requests to PSE and Staff took depositions of eleven present or former Pilchuck employees. Staff counsel later interviewed one person previously deposed, who later filed a sworn declaration. Staff also made three informal requests for information from PSE.

Pilchuck workers who Staff deposed who were engaged in the conduct testified they were not aware of other, similar conduct, and the work in question was completed.

IV. NATURE OF THE AGREEMENT

11 The Parties shared a mutual interest in this docket: to assure that PSE has in place the measures sufficient to prevent this sort of conduct from being repeated, and that there is a positive, pro-safety culture among PSE and its contractors. To that end, the Parties have agreed that a third party will conduct an audit of PSE's mandated gas safety activities, and PSE and Staff will agree upon the recommended improvements that will be adopted from the auditor's recommendations, if any. *Agreement ¶ 20 and Agreement Attachment 1: "Third Party Review of Mandated safety Activities."*

12 To the Parties' knowledge, this sort of audit is unprecedented at the Commission. The scope of the audit is broad and goes beyond the allegations in this docket. It will be undertaken as a collaborative process between PSE and Staff and it involves a comprehensive review of PSE's gas safety programs, including PSE's use of contractors. *Agreement Attachment 1 at 2-3, ¶¶ 3A-3F.* This is a very important undertaking that will involve an extensive analysis, and it promises to provide benefits to PSE, the Commission and the public.

13 PSE also agrees to adopt gas safety Quality Assurance (QA) and Quality Control (QC) plans for PSE and for each of its contractors. *Agreement ¶¶ 14-18.* The Pilchuck-related QA and QC plans are due by March 31, 2008, and QA and QC plans for PSE and PSE's other gas safety contractors are due by June 30, 2008. *Agreement ¶¶ 14-17.*

14 PSE admits it violated Commission rules, through the conduct of its contractor Pilchuck, and agrees to pay a monetary penalty of \$1.25 million, and absorb the first \$250,000 of the Third Party Audit. *Agreement ¶¶ 10, 21 and ¶ 20, last sentence.* Nothing

in the Agreement prevents PSE from seeking cost recovery of additional Third Party Audit costs through rates. *Agreement ¶ 20, last sentence.*

15 There are forbearance elements in the Agreement as a result of the collaborative and transparency associated with proactive measures that will be undertaken jointly by PSE and Staff through the third party audit. Additionally, Staff agrees to forbear recommending a complaint for violations that are the same as the specific conduct alleged in the Complaint. *Agreement ¶ 22-23.* Exceptions are for a) conduct that postdates July 1, 2007, b) intentional conduct by PSE management, or c) conduct that is significantly more widespread than the conduct alleged. *Agreement ¶ 23.* In addition, Staff discovered that in some situations, PSE was not maintaining its leak records in numerical order as required by a settlement in Docket UG-920487. PSE corrected the problem (*Agreement ¶ 12*) and Staff has agreed to forbear pursuing action for these violations that occur up to the date the Commission approves the Agreement. *Agreement ¶ 24.* Finally, if during the Third Party Audit violations are discovered, they will be identified and corrected, but Staff has indicated its intent not to pursue complaints for them unless the conduct is intentional, or systematic or widespread. *Agreement Attachment 1 ¶ 3G.* None of these provisions apply if the violation results in serious bodily injury, loss of life, or more than \$50,000 in property damage.

16 Each Party discusses these provisions in their separate statements in support of the Agreement in Section IV below.

17 Other elements of the Agreement include PSE's commitment to assure its leak records are numbered sequentially, and to implement anti-fraud measures to its leak records system. *Agreement ¶¶ 11-13.* The "General Provisions" include typical settlement provisions. Some of these provisions are described in Part I above.

V. PARTIES' SEPARATE STATEMENTS IN SUPPORT OF THE AGREEMENT

A. Staff's Statement in Support of the Agreement

18 Staff strongly supports the Agreement as soundly in the public interest. Staff
recommends the Commission approve the Agreement.

19 This case involves the gas safety recordkeeping practices of PSE. The recordkeeping
requirements in Commission rules are critical for gas safety regulation to be effective. The
Complaint presents serious allegations: people responsible for the safety of PSE's gas
pipeline system were falsifying gas safety records over an extended period of time. Staff
confirmed this intentional conduct through discovery, and PSE has admitted violations
occurred. *Agreement ¶ 10.*

20 Staff has filed a "Staff Report" summarizing its investigation and its conclusions, so
the Commission will be able to understand in detail what Staff discovered. From Staff's
perspective, the Agreement is designed to address the concerns and recommendations
contained in the Staff Report.

21 Just as the Complaint raises serious allegations, the Agreement provides a serious
response to the Complaint. PSE agrees to pay a very significant monetary penalty: \$1.25
million. *Agreement ¶ 21.* This will send the appropriate signal to all persons working in gas
safety in this state: the Commission will not tolerate falsification of records.

22 Perhaps even more important, however, is that PSE has agreed to some very
significant measures that hold promise for PSE to be among the leaders in the industry as far
as gas safety is concerned. First, PSE has agreed to an independent audit of its gas safety
programs. *Agreement ¶ 20 and Attachment A to the Agreement.* This audit encompasses all
of PSE's mandated gas safety activities and it will include analysis of the relationship

between PSE and its contractors. PSE agrees to pay the first \$250,000 of this audit. PSE may request rate recovery of additional audit costs, though nothing in the Agreement dictates how the Commission must respond to that request, one way or the other.

Attachment A ¶ 2I. The Agreement prescribes due dates for selecting the auditor and starting the audit are prescribed. *Id. ¶ 2E.*

23 Second, PSE commits to implement Quality Control and Quality Assurance (QA/QC) Plans for itself and for each of its contractors. *Agreement ¶¶ 14-18.* These plans will implement mechanisms that help ensure that the company's construction, operations and maintenance standards are consistently observed in the field. Each contractor will be required to inspect the work it performs for compliance with PSE standards and PSE will monitor each contractor's performance with its own inspections as well as periodic audits. These plans also have prescribed due dates: Pilchuck's plan will be in place by the end of March. Plans for PSE and all other contractors will be in-place by the end of June. *Id.*

24 Finally, PSE has made specific process and record keeping changes to ensure that the kind of misconduct identified in the Complaint will be easier to detect in the future. *Agreement ¶¶ 11-13.*

25 The independent audit and quality plans present a high water mark for cooperation between PSE and Staff on gas safety. PSE cooperated with Staff in the investigation of this matter. That cooperation continues through the proposed independent audit and the quality measures. Through this process, Staff and PSE will work together in a constructive way. Staff's goal is that the result will be in a higher degree of confidence that the Company's gas safety program is geared toward a culture of safety.

26 Part of the Agreement calls for forbearance of additional violations in three regards, which are described in this Narrative and in the Agreement in ¶¶ 22-23, 24 and Agreement Attachment 1, ¶ 2H. It is pertinent to note at the outset that no forbearance of any nature applies if any violation leads to serious personal injury, loss of life or \$50,000 or more in property damage. *Agreement* ¶ 25.

27 The first forbearance is for violations of the type and context of those cited in the Complaint, unless the violations are intentional by PSE management, or if the violations occur after July 1, 2007, or if the violations are more widespread than the Complaint. *Agreement* ¶ 22-23. This is reasonable because Staff's investigation analyzed a sample of documents, and Staff is aware there would be more violations if a larger sample were taken. Staff took this into account in the overall structure of the settlement. However, this forbearance does not apply if Staff finds falsification took place outside the specific context of the phantom leak follow-up leak evaluations, where the work was done.

28 The second forbearance deals with sequential numbering of leak work orders. *Agreement* ¶ 24. Staff discovered that in some instances, PSE did not keep its leak records in sequential numerical order, contrary to PSE's commitment in a settlement the Commission approved in Docket UG-920487. This is reasonable because although there was a substantial suspended penalty in that 1992 docket (\$1 million), PSE promptly corrected the problem, and Staff considers the penalty in this matter is adequate to cover this situation.

29 Finally, the independent audit has a forbearance provision. *Agreement Attachment A. ¶ 2H*. In general, Staff sees the independent audit as an opportunity for PSE and Staff to objectively determine whether PSE's gas safety program needs improvement, and if so, to

make those improvements. For Staff, this process is not a source of additional enforcement actions. Consequently, Staff believes it is reasonable to forbear from recommending a complaint if violations are found, but not if the violations are intentional or systematic and/or widespread. *Id.* If any violations are found in the course of the audit, PSE will inform Staff of the violations and promptly correct them. *Id.*

30 The forbearance provisions here are fundamentally different than the provision the Commission rejected in *Penalty Assessment Against All My Sons Moving & Storage Company*, Docket TV-050537, Order 03 (September 14, 2006). The forbearance provision at issue in *All My Sons* expressly barred Commission action, while the forbearance provisions here deal with Staff's recommendations to the Commission. Moreover, the forbearance provision in *All My Sons* was not in the context of a comprehensive independent audit of the nature in this case.

31 In sum, the Agreement provides substantial benefits to the public, PSE and the Commission. Therefore, Staff urges the Commission to approve the Agreement because it is in the public interest.

B. PSE's Statement in Support of the Agreement

32 PSE recognizes the Commission's important responsibilities in auditing and enforcing pipeline safety with respect to the companies it regulates. PSE is committed to operational excellence and full compliance with federal and state regulations—by its employees and by the independent contractors who work on its gas system. PSE's goal is to continue to maintain a safe and reliable gas system, and PSE is constantly looking for ways to improve and enhance pipeline safety.

33

When Staff notified PSE of the alleged violations, PSE cooperated with Staff's investigation and conducted its own investigation of the allegations. PSE also undertook an audit and an internal review of Pilchuck's work, and acted promptly to correct all of the violations. Additionally, PSE has worked with Pilchuck to provide additional training to employees regarding natural gas leak recording practices. PSE and Pilchuck have advised employees of the importance of accurate record keeping and that any falsification of records will result in termination of employment.

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PSE's safety manual goes above and beyond the federal and state requirements by requiring the "different person requirement" for the follow-up inspection of phantom leaks. PSE added this policy to its safety manual in 2001, shortly after the gas construction and leak inspection work was outsourced to Pilchuck. Notwithstanding, the conduct by Pilchuck employees was wrong and violated PSE's safety manual. Pilchuck employees have been advised that even though PSE's requirements go beyond state and federal requirements, PSE's safety manual must be followed, and correct and accurate records must be kept.

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Without minimizing the seriousness of the violations identified in this docket, it is important to note that a follow-up leak inspection was always performed. There is no evidence of leak inspections that were documented as completed when the inspection had not actually been performed.

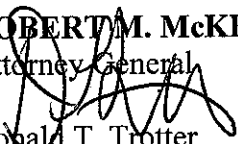
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PSE believes that overall the Agreement is fair and just, when the Agreement is viewed as a whole. PSE has agreed to pay a significant monetary penalty and to implement quality assurance and quality control programs for PSE and its contractors. In addition, PSE has agreed to work with Staff to develop and implement a third-party audit of PSE's mandated gas safety program. The scope of this third-party audit goes beyond the scope of

issues raised in this docket. Staff and PSE have agreed that PSE will not recover the first \$250,000 of the cost of this audit in rates, but PSE may seek recovery in rates of the audit expenses in excess of \$250,000.

DATED: March __, 2008.

For Commission Staff:

ROBERT M. McKENNA
Attorney General

Donald T. Trotter
Assistant Attorney General

3/10/08
Date signed:

For Puget Sound Energy, Inc.:

PERKINS COIE LLP

Sheree Strom Carson
Attorneys for Puget Sound Energy, Inc.

Date signed:

issues raised in this docket. Staff and PSE have agreed that PSE will not recover the first \$250,000 of the cost of this audit in rates, but PSE may seek recovery in rates of the audit expenses in excess of \$250,000.

DATED: March __, 2008.

For Commission Staff:

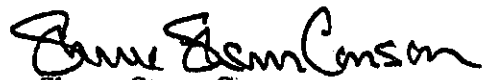
ROBERT M. McKENNA
Attorney General

Donald T. Trotter
Assistant Attorney General

Date signed:

For Puget Sound Energy, Inc.:

PERKINS COIE LLP



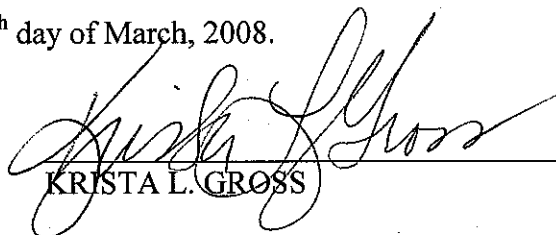
Sheree Strom Carson
Attorneys for Puget Sound Energy, Inc.

3/10/08
Date signed:

Docket PG-060215
CERTIFICATE OF SERVICE

I hereby certify that I have this day served the attached document upon the persons and entities listed on the Service List below by depositing a copy of said document in the United States mail, addressed as shown on said Service List, with first class postage prepaid.

DATED at Olympia, Washington this 10th day of March, 2008.



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