

EXHIBIT NO. ___(SPR-3T)
DOCKET NO. UG-040640, *et al.* (consolidated)
2004 PSE GENERAL RATE CASE
WITNESS: STEPHEN P. REYNOLDS

BEFORE THE
WASHINGTON UTILITIES AND TRANSPORTATION COMMISSION

WASHINGTON UTILITIES AND
TRANSPORTATION COMMISSION,

Complainant,

v.

PUGET SOUND ENERGY, INC.,

Respondent.

Docket No. UG-040640
Docket No. UE-040641
(*consolidated*)

In the Matter of the Petition of

PUGET SOUND ENERGY, INC.

For an Order Regarding the Accounting
Treatment for Certain Costs of the Company's
Power Cost Only Rate Filing.

Docket No. UE-031471 (*consolidated*)

In the Matter of the Petition of

PUGET SOUND ENERGY, INC.

For an Accounting Order Authorizing
Deferral and Recovery of the Investment
And Costs Related to the White River
Hydroelectric Project.

Docket No. UE-032043 (*consolidated*)

PREFILED REBUTTAL TESTIMONY OF
STEPHEN P. REYNOLDS (NONCONFIDENTIAL)
ON BEHALF OF PUGET SOUND ENERGY, INC.

NOVEMBER 3, 2004

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PUGET SOUND ENERGY, INC.

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PREFILED REBUTTAL TESTIMONY OF STEPHEN P. REYNOLDS

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1 **PUGET SOUND ENERGY, INC.**

2 **PREFILED REBUTTAL TESTIMONY OF STEPHEN P. REYNOLDS**

3 **I. INTRODUCTION**

4 **Q. Are you the same Stephen P. Reynolds who submitted direct testimony in**
5 **this proceeding on behalf of Puget Sound Energy, Inc. ("PSE" or "the**
6 **Company")?**

7 A. Yes, I am.

8 **Q. What is the purpose of your rebuttal testimony?**

9 A. My testimony provides the Company's overall assessment of the testimony that the
10 other parties to this proceeding have submitted to the Commission in response to
11 PSE's April 2004 request for general rate relief. My testimony is particularly
12 focused on the response testimonies submitted by the Attorney General's Office of
13 Public Counsel and the Staff of the Washington Utilities and Transportation
14 Commission. More specifically, my testimony addresses how their positions, if
15 accepted, would undermine the Company's ability to meet its obligations, both to
16 our customers and to our shareholders.

1 **II. PSE'S REACTION TO THE TESTIMONY FILED BY**
2 **OTHER PARTIES TO THE PROCEEDING**

3 **Q. Please describe the Company's view of the response testimony others have**
4 **submitted to the Company's 2004 general rate case filing.**

5 A. The Company's reaction, in a word, is "disappointment." During my two-plus
6 years as the Company's president and CEO, we have worked hard at building a
7 solid foundation on which the mutual interests of our customers and our investors
8 could be served. That process started with the Company's 2002 rate case
9 settlement, which started to return PSE to financial health. PSE needs to finish
10 that effort so it can proceed to build the integrated energy infrastructure I believe
11 this state needs for the next century.

12 Our strategy involves a vigorous initiative to secure a stably priced, long-term
13 supply of energy resources for our customers, and to enhance our risk-
14 management capabilities so we can limit customers' exposure to an uncertain
15 energy marketplace. We have greatly expanded our energy-efficiency services to
16 help customers save more energy and reduce their bills, even though this effort,
17 indirectly, is hurting the Company financially. We have further assisted customers
18 by dramatically increasing our energy-assistance program, enabling approximately
19 20,000 additional low-income households to receive financial help, year-round,
20 with their electricity and natural gas bills. We have worked hard to incorporate
21 input from all stakeholders in regard to these efforts. Furthermore, we have

1 maintained a very high quality of basic utility service while remaining one of the
2 most efficient, low-cost energy-service providers in the country.

3 We now face a critical need for investment in new energy resources and new
4 infrastructure, both to serve the needs of a steadily growing customer base and to
5 upgrade aging facilities that serve existing customers. We cannot fulfill our public-
6 service obligations, however, unless we have the financial wherewithal to obtain
7 the necessary capital under reasonable terms and to support risk management
8 activities.

9 Regrettably, the positions taken by Commission Staff and Public Counsel fail to
10 recognize the significant progress and accomplishments we have made over the
11 past two years in advancing the public interest. I believe if their positions are
12 adopted, the Company's initiatives will not be sustainable.

13 **III. THE POTENTIAL EFFECT OF PROPOSALS OF OTHER**
14 **PARTIES TO THE PROCEEDING ON THE COMPANY'S**
15 **STRATEGIC PLAN**

16 **Q. What are the primary objectives of the Company's strategic plan?**

17 A. The State Energy Strategy of Washington directs all load-serving utilities to pursue
18 integrated resource plans capable of ensuring sufficient energy supplies to serve
19 their customers' projected loads over the long-term. Limiting consumers' exposure
20 to volatile energy markets is one of the state's top priorities. To that end, the State

1 Energy Strategy correctly recognizes the need for regulatory policies that "foster a
2 predictable and stable investment climate to facilitate adequate and efficient access
3 to capital markets" for load-serving utilities in order to ensure that they can meet
4 their public-service obligations.

5 Our resource acquisition strategy is designed specifically to uphold these principals
6 and obligations. As advocated by state policymakers, we are striving to secure all
7 the energy resources our customers will need, long-term, in the most cost-effective
8 manner, while mitigating risks to customers. Our resource needs are significant
9 and growing due to a combination of expiring contracts and strong load growth.
10 We are making significant progress, but there is much yet to do. I firmly believe
11 our strategy and actions are consistent with the direction the Commission would
12 have its regulated utilities take.

13 **Q. How would the recommendations of Commission Staff and Public Counsel**
14 **affect the Company's ability to successfully reach its strategic objectives?**

15 A. Even though the Company has made noteworthy progress on the path to financial
16 recovery, as discussed in my direct testimony, we still are far from where we need
17 to be. We are far from where our *customers* need us to be. Our credit rating
18 remains weak--just one step away from non-investment grade status. Our stock
19 price remains relatively static. Our balance sheet needs substantial improvement.

20 The opposing parties' proposals would undermine the Company's efforts to
21 procure reliable, low-cost, long-term energy resources for our customers, to better

1 manage risk and protect them from volatile energy markets and to provide reliable
2 service.

3 The positions of Commission Staff and Public Counsel appear to suggest that the
4 chronically weak credit status of Washington's investor-owned utilities affects only
5 the utilities themselves, that there is no downside for the state's consumers,
6 businesses, and the overall economy. Their positions might indeed save utility
7 customers a little money in the short term. But in time, I believe, they would
8 prove disastrous for Washington's energy industry *and* the people it is obliged to
9 serve. Over the long term, utility customers would face unnecessary risk and
10 higher costs.

11 **IV. THE COMMISSION SHOULD GRANT THE COMPANY'S**
12 **RATE PROPOSAL TO STRENGTHEN THE COMPANY'S**
13 **FINANCIAL PROFILE SO WE CAN SERVE THE NEEDS**
14 **OF OUR CUSTOMERS**

15 **Q. How does your rate proposal address the Company's need to strengthen its**
16 **financial profile and to serve the interests of your customers?**

17 A. With greater ability to recover our costs and a fair opportunity to earn a reasonable
18 return for investors, the Company would be far better positioned to serve our
19 customers' interests. As Don Gaines discusses in his rebuttal testimony, we could
20 expect to see a significant improvement in the Company's credit rating under our
21 proposal. That improvement, in turn, would produce a number of direct benefits

1 for our customers over time. Those benefits include a reduction in the cost of
2 capital needed to execute a successful energy-supply strategy and make needed
3 infrastructure investments; an enhanced ability to manage customers' energy-supply
4 costs through hedges and other risk-management strategies; and the financial
5 flexibility not only to access capital markets but also to effectively cope with
6 adverse events in the region or industry.

7 The basis for the Company's rate proposal, I believe, is overwhelmingly sound.
8 We have proposed changes to our rate design that allow for more adequate,
9 timely, and accurately proportional recovery of Company costs. Furthermore, the
10 general rate increases we've proposed--7.3 percent, on average, for electric
11 customers; 6.3 percent, on average, for gas customers--are modest. Our requested
12 change in rates not only is supportable, I believe, but is much preferable to any of
13 the alternatives put forward by other parties to this proceeding.

14 V. CONCLUSION

15 **Q. Please summarize your testimony**

16 A. Commission Staff and Public Counsel assert that little to no rate increase, a lower
17 rate of return, and a less-proportionate rate design are warranted. I strongly
18 disagree. Our proposal is designed, in part, to continue the Company's efforts to
19 rebuild the Company's financial health. An improved Company financial profile,
20 however, is not the end goal. Rather, by helping the Company recover its costs,
21 stabilize PSE's financial position, and improve its balance sheet, our proposal aims

1 to help us meet the public-service obligations expected of us.

2 To secure a positive energy future for Washington state, all of us must step up to
3 the plate. We all must contribute. In the course of developing and implementing
4 our strategic plan and in taking significant steps to improve the Company's
5 financial strength prior to requesting rate relief, the Company has stepped up to its
6 public responsibilities. We have demonstrated a commitment to serve our
7 customers in the best way possible. But reliable, affordable energy service must be
8 predicated on a widespread recognition of mutual needs and shared
9 responsibilities. It demands a partnership among utilities, industry regulators,
10 investors, customers, environmental interests, and others. I believe the Company's
11 proposed rate relief represents a reasonable request for participation in these
12 efforts by the Company's customers, and should be approved.

13 **Q. Does that conclude your testimony?**

14 **A.** Yes, it does.

15 [BA043050.015 / 07771-0089]