Exhibit No. __ (JOINT-1T)
Docket Nos. UG-040640, et al
Witnesses: Joelle Steward
Donald Schoenbeck
Kevin C. Higgins
James A. Heidell
Jim Lazar

BEFORE THE WASHINGTON STATE
UTILITIES AND TRANSPORTATION COMMISSION

WASHINGTON UTILITIES AND TRANSPORTATION COMMISSION, Complainant, v. PUGET SOUND ENERGY, INC., Respondent.	DOCKET NOS. UE-040641 and UG-040640 (Consolidated)

JOINT TESTIMONY OF JOELLE STEWARD, DONALD SCHOENBECK, KEVIN C. HIGGINS, JAMES A. HEIDELL AND JIM LAZAR IN SUPPORT OF THE RATE SPREAD AND RATE DESIGN SETTLEMENT

December 6, 2004

QUALIFICATIONS OF JOELLE STEWARD

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

A. My name is Joelle Steward and I am appearing on behalf of Commission Staff. My qualifications were presented in Exhibit No. __ (JRS-1T).

QUALIFICATIONS OF DONALD SCHOENBECK

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

A. My name is Donald Schoenbeck and I am appearing on behalf of Industrial Customers of Northwest Utilities (ICNU), Northwest Industrial Gas Users (NWIGU) and Cost Management Services. My qualifications were presented in Exhibit No. __ (DWS-2).

QUALIFICATIONS OF KEVIN C. HIGGINS

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

A. My name is Kevin C. Higgins and I am appearing on behalf of The Kroger Co. My qualifications were presented in Exhibit No. __ (KCH-1).

QUALIFICATIONS OF JAMES A. HEIDELL

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

A. My name is James A. Heidell and I am appearing on behalf of Puget Sound Energy, Inc. My qualifications were presented in Exhibit No. __ (JAH-2).

QUALIFICATIONS OF JIM LAZAR

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

A. My name is Jim Lazar and I am appearing on behalf of Public Counsel, The Energy Project and A World Institute for Sustainable Humanity. My qualifications were presented in Exhibit No. __ (JL-2).

JOINT TESTIMONY ON RATE SPREAD

Q. Please describe rate spread and the policy interests that are important for consideration.

A. Rate spread allocates revenue recovery to each of the Company's customer classes. Rate spread should recognize that rates must be just and reasonable and not cause undue discrimination, that is, it should be based on established principles of fairness, equity and sufficiency. To this end, rate responsibility for any class should be guided by the cost to serve the class.

Therefore, a cost of service analysis is an important consideration in spreading a revenue increase. However, because of the high degree of judgment on classification and allocation that goes into a cost study, the results do not generally lend themselves to a strict application, as the Commission has often noted in the past.[1] Rate spread decisions are usually tempered by consideration of customer impacts and any other pertinent factors appropriate at the time.

Q. Please describe the proposed settlement on electric rate spread.

A. For settlement purposes, the parties agree to disaggregate any electric revenue increase between power costs and non-power costs. The distinctions between power costs and non-power costs are illustrated in the table on page 4 of the Settlement Terms for the Power Cost Adjustment Mechanism (PCA), which the Commission approved in Docket Nos. UE-011570 and UG-011571.

Any power cost-related increase will be spread to all customer classes on an equal cents per kilowatt-hour basis, with the exception of retail wheeling customers (Schedules 449 and 459). Since retail wheeling

[1] See, for example, Commission orders in Docket Nos. UE-991832, UG-940034, U-89-2688 and U-86-100.

customers procure their own energy supply and use only the Company's transmission and distribution systems, the parties agree that it is appropriate to exclude them from any cost increase related to power supply. It is important to note that this approach is being used to allocate the increase between customer classes; it is not establishing a specific rate to be applied within each class. Specific rate design considerations outlined in the settlement stipulation set forth the methods for calculating the changes to the energy charges, demand charges, and other rate elements in each rate schedule.

Any increase related to non-power costs will be spread on an equal percentage basis to all classes, except Schedule 25 and the retail wheeling Schedules 449/459, which will receive 75 percent of the average non-power cost increase.

Q. In the event the Commission orders a decrease in non-power costs, how do the parties propose to allocate that decrease?

A. The parties agree to first allocate the decrease in non-power costs in a similar manner as the agreement for an increase, whereby Schedules 25 and 449/459 would receive a decrease of 125 percent of the non-power cost average

decrease. Any increase related to power costs would then be applied as set forth in the settlement stipulation.

Q. Please explain why the parties believe that this approach for electric rate spread is in the public interest.

A. The power cost related rate spread is generally consistent with the stipulated rate spread for the variable costs in the PCA.[2] Since any increase related to power costs in this proceeding can generally be attributed to variable costs for fuel and purchased power, the parties agreed to use this previously established method, which, we believe, fairly allocates these costs on the basis of energy.

For the non-power cost related rate spread, the parties took into consideration the cost of service analyses presented by the parties in this proceeding. While there was considerable difference in the methodologies and allocations employed by the various parties, we found some consistent threads we could use to create a fair and reasonable rate spread. The cost studies consistently showed that the retail wheeling Schedules 449/459 and Schedule 25 were above parity, exceeding a 110 percent revenue to cost ratio

[2] See Settlement Terms for PCA, Exhibit A to the Settlement Stipulation in Docket No. UE-011570/UG-011571, paragraph 15.

in nearly all of the studies. All other classes were generally in the range of a 90 percent to 110 percent revenue to cost ratio. The parties agree that given the nature of cost of service studies, the classes within this "range of reasonableness" should be allocated an equal percentage increase. The two classes exceeding this range are given a less than average increase in order to make movement toward parity. Therefore, the new rates generally reflect costs.

Q. Please describe the proposed settlement on natural gas rate spread and explain why it is in the public interest.

A. The parties took the same approach to natural gas rate spread as we used for spreading the non-power cost increase on the electric side. We generally relied upon a natural gas cost of service study using the methodology approved in Docket No. UG-940814, with one adjustment. For cost study purposes, Schedules 87 and 57 were combined since they receive the same delivery service. In general, classes significantly above or below parity are targeted to 150 percent/50 percent of the average increase and classes moderately above or below parity are given a 125 percent/75 percent of the average increase. Finally, classes within 110 percent of parity are given an

average increase, as well as any residual increase. The combined class of Schedules 87 and 57 was given 25 percent of average increase since that class is considerably above parity. The parties believe that this proposed rate spread is in the public interest because it makes efforts to move all classes toward parity, but with attention to minimizing severe customer impacts.

JOINT TESTIMONY ON RATE DESIGN

Q. Please describe the importance of rate design.

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

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

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

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

Q. Were these principles applied in order to develop the proposed electric and gas rate structures?

A. Yes.

<u>Electric Rate Design</u>

Q. What rate design is proposed for the residential customer class, Schedule 7?

A. The parties agree to retain the current rate structure but to increase the customer charge by $0.25 to $5.75, in order to provide the Company with more fixed cost recovery. The remainder of any rate increase will be applied proportionally to the two rate blocks.

Q. Are any structural changes proposed for the secondary and primary voltage general service schedules (Schedules 24, 25, 26, 29, 31, 35 and 43)?

A. No, the settlement retains the current structures for these classes.

Q. What factors did the parties consider in deciding how to apply the increases within the current structures for the general service schedules?

A. In deciding how to apply the increase within the rate structures, we were guided by the cost studies, along with consideration of customer impact. We based the customer charges for these schedules on the methodology used in the rate design case in Docket Nos. UE-920499 and UE-921262. We also looked at the demand-related and energy-related costs from the cost of service study in determining how to balance the remaining increase between these two charges. As a result, many of the general service schedules will receive higher proportional increases to the demand charges in relation to the energy charges in order to bring demand revenues closer to demand-related costs.

Q. Does the settlement take into consideration the intentions of the parties in the prior rate case settlement in Docket Nos. UE-011570/UG-011571, to have Schedules 26 and 31 reflect a cost-based differential?

A. Yes. It was the intention of the parties in the last rate case to provide some rebalancing of the rates between secondary service Schedule 26 and primary service Schedule 31, in order to more closely reflect a cost-based rate differential. In short, the rate differential was greater than the cost of transformation and losses associated with secondary service. To that end, three annual rate changes were added in the tariff to bring these schedules closer together. The settlement rate design uses the final adjustment (slated for July 1, 2005) as the starting point for setting rates for Schedules 26 and 31 in this case. As a result, these schedules will be much closer to a cost-based differential. Additionally, the settlement includes a provision to allow primary voltage service on Schedule 26, with a cost-based discount. It is anticipated that Schedule 31 will be closed to new customers at some point in the future.

Q. What is the proposed rate design for the high voltage class, Schedules 46 and 49?

A. These schedules will also retain their current structures and the increase will be applied on an equal percentage basis to the two schedules, such that the energy charges will continue to be equal between them.

Q. Are any changes proposed to the rate structure for retail wheeling service, Schedules 449 and 459?

A. No. The increase will be recovered on an equal percentage basis for both primary and high voltage customers, through the demand charges. The number of decimals of the demand charge may be expanded in order to more equitably accommodate an increase.

Q. Please describe the new schedule being proposed for large load general service, Schedule 40.

A. This schedule will be available to customers with concentrated load on a non- dedicated distribution feeder. Distribution feeders are designed to carry and serve about 5 MVA. Customers eligible for Schedule 40 must have over 3 MVA of peak load on a feeder. This schedule will require customers

to pay the costs of the distribution facilities where they typically constitute a majority of the load. The distribution charges will be calculated separately for each customer at the time of a rate case, in accordance with the methodology outlined in Section 3 of the schedule. The rates for these customers are cost based.

Q. Have the parties had an opportunity to conduct discovery on the proposed schedule and review workpapers to support the charges?

A. Yes. Staff and ICNU have conducted informal discovery on the proposed schedule and have worked with the Company and interested parties in reviewing workpapers to support the methodologies for calculating the rates. The specific rates, of course, cannot be finalized until the Commission issues an order in this case with a final revenue requirement and capital structure.

Q. How many customers will be eligible for service under Schedule 40?

A. We estimate that five customers currently will qualify. These customers currently take service under Schedules 25, 26 and 31.

Q. Will there be any cost shifts as a result of creating this new schedule?

A. Yes. The parties agree to incorporate the difference between the Schedule 40 rates and the customer's current schedule rates (either 25, 26 or 31) for the customers electing to take service on Schedule 40 into the relevant schedule. We estimate that this difference will result in an increase of 0.017% to Schedule 25, 0.207% to Schedule 26, and 1.159% to Schedule 31.

Q. Why is Schedule 40 proposed as voluntary for three years and mandatory thereafter?

A. The schedule requires a considerable amount of customer-level detail and is somewhat work intensive for the Company to 1) identify all eligible customers and 2) to compute the distribution charges for each customer. Likewise, on the customer side, it may take more effort and understanding for the customer to become comfortable with the methodologies for calculating their rates. Therefore, we want to give the parties a period of time to gain an understanding of the schedule and for the Company to continue to work at identifying any additional eligible customers. The schedule will become mandatory after three years in order to prevent customers from migrating to other schedules in the event that the relevant

distribution facility upgrades or replacements result in a higher average cost for these customers.

Q. How will the charges other than those associated with distribution charges be calculated?

A. The customers will continue to pay the same basic charges as they would under their current schedules. The production and transmission charges will be calculated at the high voltage rate, adjusted for parity and losses at the metering points. The customers will also continue to pay the low-income assistance program rate at the current level until the next true-up period, at which time their rate will be calculated according to the approved allocation methodology. Similarly, the schedule will be added to Schedule 120, the conservation rider, with the same rates that they pay under their current schedules. Beginning in 2006, Schedule 40 customers will be eligible to participate in PSE's self-directed industrial conservation program, Schedule 258. The customer amounts eligible for self-direction will be calculated in accordance with the same provisions as established for Schedules 46 and 49. Additionally, in 2006, the Schedule 120 rate for this schedule will be

calculated as a separate class in accordance with the approved allocation methodology.

Natural Gas Rate Design

Q. What is the proposed rate design for residential customers, Schedule 23?

A. Residential customers will receive a $0.75 increase in the basic charge, to $6.25. This increase will allow the Company more fixed cost recovery without resulting in a decrease to the current delivery charge. The basic charge of $6.25 is within the parameters of the unit cost results in the cost of service study. The remaining increase will be applied to the delivery charge.

Q. Do the parties propose any changes to the rate structures for the commercial and industrial heating customers, Schedules 31, 36 and 51, or the general service Schedule 41?

A. No. The rate structures for these schedules are retained with the increases being applied to the customer charges and delivery charges.

Q. What is the basis for the level of proposed monthly customer charges for the rate schedules?

A. The proposed level of customer charges for these and all other rate schedules was guided by the unit cost report from the cost of service study, but moderated by consideration of the bill impact analysis. We believe that the proposed charges strike a fair balance at this time between increased fixed cost recovery for the Company and minimizing bill impacts.

Q. What is the proposed rate design for the interruptible sales service Schedules 85 and 86?

A. Both schedules will retain the current rate structure but with the addition of a procurement charge, up to 0.355 cents per therm. For Schedule 85, the last block of the delivery charge (for usage over 50,000 therms) will be equal to the third block of the delivery charge in Schedules 87 and 57 (for usage between 50,000 to 100,000 therms). Thereafter, any remaining increase will be applied proportionally to the first 2 blocks. For Schedule 86, the remaining increase will be applied proportionally across the delivery charge blocks. The demand charges for these schedules, as well as Schedules 57 and 87, will remain unchanged.

Q. Please explain the procurement charge.

A. The procurement charge is a volumetric rate applying to Schedules 85, 86 and 87 to recover the administrative costs of procuring and managing gas supply and storage related costs for sales customers. The parties agree to support a procurement charge up to 0.355 cents per therm. This is a cost-based level. The charge may be less than this if the final rate spread cannot support this level. In order to implement this charge, we will not decrease the current delivery rates.

Q. After the procurement charge is applied, how will the remaining increase to Schedules 57 and 87 be recovered?

A. The customer charge for Schedule 87 will increase up to $500. This would provide a $300 difference between the customer charge for Schedule 87 and 57. Three hundred dollars is the estimated incremental administrative cost related to the provision of transportation service. Any remaining increase will be recovered through the first block in the delivery charge, such that these charges remain equal for Schedules 87 and 57.

Q. Are there any changes proposed for customers switching between sales and transportation service?

A. Yes. The tariff will be modified to allow an annual service election period for customers choosing to migrate to or from transportation service. Eligible customers will be allowed to migrate after 30-days notice, after one year of service. Migration and conversion charges may apply to protect other customers against stranded costs.

Q. Does this conclude the joint testimony?

A. Yes.