

Exhibit __ (JOINT-3)

Docket PG-060215

Witness: King, Johnson, McLain,
Henderson

BEFORE THE WASHINGTON UTILITIES AND TRANSPORTATION COMMISSION

WASHINGTON UTILITIES AND)
TRANSPORTATION COMMISSION,) DOCKET PG-060215
Complainant,)
v.)
PUGET SOUND ENERGY, INC.,)
Respondent.)

SETTLEMENT AGREEMENT
(March 3, 2008)

BEFORE THE WASHINGTON UTILITIES AND TRANSPORTATION COMMISSION

WASHINGTON UTILITIES AND
TRANSPORTATION COMMISSION,

Complainant,

v.

PUGET SOUND ENERGY, INC.,

Respondent.

)
)
) DOCKET PG-060215
)
)

) SETTLEMENT AGREEMENT
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1 This Settlement Agreement ("Agreement") is entered into by the parties to this proceeding for the purpose of resolving all issues raised in this docket. This Agreement is subject to approval by the Washington Utilities and Transportation Commission ("Commission") and it is not effective for any purpose until such approval, except for the limited purposes explained in ¶ 27 below, entitled "Effective date."

I. PARTIES

2 The parties to this Agreement are Puget Sound Energy, Inc., ("PSE") and the Staff of the Commission ("Staff"). PSE and Staff are referred to individually in this Agreement as "Party," and collectively as "the Parties." PSE and Staff are the only parties of record in this docket.

II. BACKGROUND

3 On May 23, 2007, the Commission issued a Complaint in this docket. The Complaint alleged violations of 49 C.F.R. § 192.605(a), which is a rule which the Commission has adopted by reference in WAC 480-93-999, as well as WAC 480-93-187, and WAC 480-93-185.

4 Part of the Complaint is called Attachment 1, which identifies separate events called "Incidents." For each Incident, Attachment 1 itemizes the specific facts supporting the violations involved. As alleged in Attachment 1, the majority of the conduct that violated Commission rules in this docket involved falsification of PSE gas safety records by certain employees of a PSE contractor named Pilchuck Contractors, Inc.

(Pilchuck). This was intentional conduct by these Pilchuck employees; it was not the result of an honest mistake.

5 On June 12, 2007, PSE filed an Answer to the Complaint and on July 31, 2007, PSE filed a First Amended Answer (collectively referred to as "Answer"). In its Answer, among other things, PSE admitted that certain violations may have occurred, but asserted that the alleged violations do not represent knowing or intentional conduct by PSE. Further, PSE asserted in its Answer that after learning of the alleged violations, PSE immediately cooperated with Staff's investigation, conducted its own investigation, and worked with Pilchuck to remedy the practices and correct the violations. PSE asserted that the actions taken by PSE and Pilchuck, after learning of the violations, resulted in a significant improvement to the accuracy of the records and record filing system based on subsequent audits performed by PSE. Additionally, PSE asserted statute of limitations and other defenses.

6 On June 27, 2007, Commission ALJ Mr. Adam Torem convened a prehearing conference, pursuant to a Notice of Prehearing Conference issued June 18, 2007. There were no intervenors. In its June 28, 2007, Prehearing Conference Order, the Commission provided additional opportunity for intervention. No person sought intervention.

7 Discovery ensued. Staff issued numerous data requests to PSE and took deposition testimony of seven current Pilchuck employees and two former Pilchuck employees. Based on its investigation, Staff prepared a "Commission Staff Report of Investigation," which Staff has filed in this docket. That report describes in detail what Staff discovered, including a description of the falsification of records that actually occurred, and what Staff believes were the causes, and it describes the actions taken by PSE and Pilchuck to address that situation.

8 Staff and PSE agreed to meet to negotiate a mutually acceptable resolution of this docket. Mr. C. Robert Wallis (retired Director of the Commission's Administrative Law Division) was retained to mediate. This Agreement is the result of those discussions.

II. AGREEMENT

9 The Parties have reached agreement on the issues raised in the above docket and wish to present their agreement for the Commission's consideration and approval. The Parties therefore adopt the following Agreement, which the Parties enter into voluntarily to resolve the matters in dispute between them and to expedite the orderly disposition of this dispute. The Parties agree as follows:

10 **Admitted violations.** PSE concurs that there were violations of PSE's Standards Manual by certain Pilchuck employees which constituted violations by PSE of Commission rules regarding accuracy of records.

- 11 **Auditable records of employee leak repair and leak surveillance activities.** Effective March 31, 2008, PSE will establish auditable records of each PSE employee and each PSE contractor employee who performs leak repair or leak surveillance work. This may include recording on their timesheets each PSE leak number they performed work on or other such means to establish supporting documentation to the completed leak work order.
- 12 **Leak work orders numbered sequentially.** PSE will assure that its leak work orders are numbered sequentially, whether those leak work orders are completed by a PSE employee or a PSE contractor. Effective December 11, 2007, PSE implemented procedures designed to assure this will be accomplished.
- 13 **Leak records system.** PSE will make changes to its leak records system to implement fraud prevention measures, with the participation of Staff (including a Staff consultant(s)). PSE agrees to investigate use of a paperless (*i.e.*, primarily electronic) system. Following the investigation of options, PSE will submit a written plan to Staff by July 31, 2008. If there is a dispute about what system is appropriate or what changes are appropriate, the Parties will present that issue to the Commission for resolution.
- 14 **Gas Safety Quality Control and Quality Assurance Plans.** By March 31, 2008, PSE will submit to Staff a Pilchuck Quality Control Plan ("QC Plan") that applies to gas safety related activities performed by Pilchuck.
- 15 Also by March 31, 2008, PSE will submit to Staff a Gas Safety Quality Assurance Plan ("QA Plan") that documents PSE's current quality assurance practices and adds audit practices relative to gas pipeline records review for work performed by Pilchuck. PSE will develop the QA Plan with the participation of Staff (including Staff consultant(s)).
- 16 By June 30, 2008, PSE will submit to Staff QC Plans for each of PSE's other contractors performing gas safety activities and PSE's own personnel performing gas safety activities. At present, these other contractors are Quanta/Potelco, Heath, CLS, and Locating, Inc.
- 17 Also by June 30, 2008, PSE will submit to Staff an expanded QA Plan which will apply to each of PSE's other contractors performing gas safety activities and PSE's own field personnel performing gas safety activities. PSE will develop the QA Plan with the participation of Staff (including Staff consultant(s)).
- 18 Once Staff reviews and accepts the QA and QC plans described above, PSE and its contractors will implement the plans. If there is a dispute about the content or implementation of the QC and QA plans, the Parties will present the issue to the Commission for resolution.

- 19 **Other quality assurance measures.** Separate from the Complaint in this docket, Staff and PSE have been meeting and working together cooperatively since September 7, 2007 to address improvements to work processes, quality of service and system performance for other aspects of PSE's operations, including gas operations, electric operations, contractor oversight and customer relations. Meetings on these issues are ongoing. In general, the Parties' plan is to identify specific issues we will work on, agree on needed improvements, and how to measure the success of this effort over time. The Parties agree that this process will continue under the existing administrative docket A-071529.
- 20 **Third-Party Audit.** Also in furtherance of these efforts, PSE and Staff have agreed to work together to develop and implement a third-party audit of PSE's mandated gas safety program to be conducted by a mutually agreed upon consultant. As a result of this audit, PSE and Staff will have an authoritative assessment of PSE's mandated gas safety activities and a plan for PSE to move forward and implement any agreed upon recommendations. The audit will address gas safety issues within and beyond the scope of issues raised in Docket PG-060215. The consultant will also evaluate PSE's operations and those of PSE's contractors and agents against current industry practices and standards and make recommendations on opportunities for process improvements or changes. The audit process and scope of the audit are described in Attachment A to this Agreement. PSE will issue the RFP within 30 days of the Commission order approving the Settlement Agreement in Docket PG-060215, and the contractor will be selected within 60 days of the date the RFP is issued. PSE will pay for the first \$250,000 of the audit without seeking recovery of this amount in rates. Nothing in this Agreement prevents PSE from seeking recovery of audit expenses over this amount through rates.
- 21 **Monetary Penalty.** PSE will pay a penalty totaling \$1,250,000.00. PSE shall pay that amount to the Commission no more than 15 (fifteen) calendar days after the date the Commission issues the order approving this Agreement. PSE agrees that it will not seek recovery of this penalty through rates.
- 22 **Forbearance.** In consideration of the monetary penalty and the other commitments PSE makes in this Agreement to improve its practices and the practices of its contractors, the Parties agree that forbearance as described herein as to possible future enforcement activity is justified.
- 23 First, the Parties understand that in the context of implementing this Agreement, PSE, Staff or others may discover violations of gas safety rules of the type alleged in the Complaint; *i.e.*, intentional violations of § 2625.1300 of PSE's gas safety standards manual, but the work was actually performed. For each such violation that is discovered, PSE will document the violation and correct the deficiency to the extent possible. However, Staff does not intend to utilize information gathered from the effort to generate new enforcement actions and will not recommend the

Commission take additional enforcement action (including monetary penalties) as to such violations, except: 1) if the intentional act occurred after July 1, 2007; and/or 2) if the intentional act was performed by a PSE management employee or at the direction of a PSE management employee; and/or 3) if the intentional acts are significantly more widespread than the conduct alleged in the Complaint.

24 Second, Staff will not pursue action against PSE for potential violation(s) of Part II.3.E of the Settlement and Operating Agreement in Docket UG-920487 relating to sequential numbering of leak records, if such potential violations occurred before the effective date of this Agreement.

25 Nothing in this Agreement affects the ability of the Staff to recommend penalties or other remedy for any violation of any statute, rule or provision in PSE's gas safety standards manual that leads to serious personal injury (*i.e.*, requires in-patient hospitalization), loss of life, or property damage or loss of \$50,000 or more. PSE may contest any such enforcement action based on such a violation or violations, but PSE will not use anything in this Agreement as limiting any such enforcement action.

IV. GENERAL PROVISIONS

26 **Settlement of all issues.** The Parties agree that this Agreement is a settlement of all contested issues between them in this proceeding. The Parties understand that this Agreement is not binding unless and until accepted by the Commission.

27 **Effective date.** This Agreement is effective on the date the Commission enters its order approving this Agreement in its entirety, except the provision of this Agreement entitled "Cooperation in processing this Agreement before the Commission" is effective on the latest date of signature on this Agreement. If the Commission's order does not approve this Agreement in its entirety, this Agreement is not effective, except the provision of this Agreement entitled "Procedures in the event the Commission rejects this Agreement or any portion thereof" shall then apply.


28 **Cooperation in processing this Agreement before the Commission.** The Parties agree to cooperate in submitting this Agreement promptly to the Commission for acceptance. The Parties agree to support adoption of this Agreement in proceedings before the Commission, if any, through whatever procedures the Commission may require, including testimony, exhibits, and briefing. Each Party agrees that none of its agents, employees, consultants, or attorneys will engage in advocacy contrary to the Commission's adoption of this Agreement.

- 29 **Publicity.** Each Party retains the right to provide information to the public about this Agreement, after this Agreement is filed with the Commission. PSE and Staff each agree to provide the other Party a copy of each public announcement, news release or similar communication (hereafter "public communication") that the Party intends to make regarding this Agreement, two business days in advance of publication. The Party receiving such public communication may review the public communication and make a reasonable request to the issuing Party to change the text of such public communication. Notwithstanding anything else in this paragraph, the Parties agree that each such public communication shall include a statement to the effect that this Agreement is subject to Commission approval and the Staff's signing of this Agreement and/or Staff's recommendation that the Commission approve this Agreement is not binding on the Commission itself.
- 30 **Claims against other entities.** Nothing in this Agreement shall limit or bar PSE's ability to pursue legal remedies against any other entity.
- 31 **Admissibility of negotiations; construction of this Agreement.** The Parties have entered into this Agreement to avoid further expense, inconvenience, uncertainty, and delay. The Parties recognize that this Agreement represents a compromise of the Parties' positions. As such, conduct, statements, and documents disclosed during negotiations of this Agreement shall not be admissible as evidence in this or any other proceeding, except in any proceeding to enforce the terms of this Agreement or any Commission order fully adopting those terms. This Agreement shall not be construed against either Party because it was a drafter of this Agreement.
- 32 **Integrated Agreement.** The Parties have negotiated this Agreement as an integrated document. This Agreement supersedes all prior oral and written agreements on issues addressed herein, if any. Accordingly, the Parties recommend that the Commission adopt this Agreement in its entirety.
- 33 **Manner of execution.** The Parties may execute this Agreement in counterparts and as executed shall constitute one agreement. Copies sent by facsimile are as effective as original documents.
- 34 **Compliance with this Agreement.** The Parties shall take all actions necessary as appropriate to efficiently carry out this Agreement, once it is approved. PSE understands that lack of compliance with this Agreement once it is approved by the Commission can subject PSE to enforcement action by the Commission, and possible penalties and/or other remedies.
- 35 **Procedures in the event the Commission rejects this Agreement or any portion thereof.** In the event the Commission rejects all or any portion of this Agreement, each Party reserves the right to withdraw from this Agreement by written notice to the other Party and the Commission. This written notice must be served within 10 calendar days of the Commission order rejecting part or all of this Agreement. In

such event, neither Party will be bound or prejudiced by the terms of this Agreement, and either Party shall be entitled to seek reconsideration of the order. The Parties will also jointly request that the Commission reconvene a pre-hearing conference to establish a procedural schedule to complete this docket.

WASHINGTON UTILITIES AND
TRANSPORTATION COMMISSION

PUGET SOUND ENERGY, INC.




STEVEN KING
Director – Safety & Consumer Protection Division

Dated: March 3, 2008.

SUE MCLAIN
Senior Vice President - Operations

Dated: _____, 2008.

Approved as to form:



Donald T. Trotter, WSBA # 8752
Assistant Attorney General
Counsel for the Utilities and
Transportation Commission

Dated: March 3, 2008.

PERKINS COIE LLP

By _____
Sheree Strom Carson, WSBA # 25349

Steven R. Secrist, WSBA #17305
Attorneys for Respondent Puget Sound Energy, Inc.

Dated: _____, 2008.

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WASHINGTON UTILITIES AND
TRANSPORTATION COMMISSION

PUGET SOUND ENERGY, INC.

STEVEN KING
Director – Safety & Consumer Protection Division

Dated: _____, 2008.

Sue McLain

SUE MCLAIN
Senior Vice President - Operations

Dated: March 03, 2008.

Approved as to form:

Donald T. Trotter, WSBA # 8752
Assistant Attorney General
Counsel for the Utilities and
Transportation Commission

Dated: _____, 2008.

PERKINS COIE LLP

By *Sheree Strom Carson*

Sheree Strom Carson, WSBA # 25349

Steven R. Secrist, WSBA #17305
Attorneys for Respondent Puget Sound Energy, Inc.

Dated: 3/3, 2008.

ATTACHMENT A

Third-Party Review of Mandated Safety Activities

1. Goals:

PSE and Staff will develop and implement a third-party audit of PSE's mandated gas safety program. As a result of the audit, PSE and UTC will have an authoritative assessment of PSE's mandated gas safety activities and a plan for PSE to move forward and implement key recommendations. By working together on this audit, PSE and UTC will have forged an effective working relationship characterized by joint problem solving, information sharing and mutual respect.

2. Key process elements:

- A. The audit will be performed by an independent third party selected by PSE but agreed to by UTC Staff.
- B. To ensure the consultant understands the UTC's concerns, Staff and PSE will meet together with the consultant before the scope of the work is finalized to discuss implementation.
- C. Each party may meet separately with the consultant to discuss their concerns and interests. The consultant will make notes of any such meetings available to all parties.
- D. It is important that the process of the audit be both independent and transparent to the UTC. To that end UTC Staff will: 1-participate in reviewing proposals from potential consultants, determining the scope of the study and methods the consultant uses; 2-be included in all conferences between the consultant and PSE where the scope, status, findings or recommendations are discussed; 3-be notified in advance of and selectively participate in any fact finding conducted by the consultant; and 4-receive directly from the consultant all documents circulated to PSE for comment and all drafts of reports, correspondence, etc.
- E. The target starting date for the audit will be approximately 90 days after completion of the quality assurance / quality control (QA/QC) programs required as part of the settlement in UTC Docket PG-060215. The implementation date for Pilchuck's QA/QC programs is March 31, 2008 and the implementation for PSE and all other contractor QA/QC programs is June 30, 2008. So that the auditors may observe work during the 2008 construction and maintenance season, the parties agree make the necessary preparations so that the audit may begin with Pilchuck after July 1, 2008 and then turn to PSE and its other contractors after October 1, 2008. To this end, PSE will issue the RFP within 30 days of the Commission order approving the Settlement Agreement in Docket PG-060215, and the contractor will be selected within 60 days of the date the RFP is issued.
- F. PSE and Staff will actively cooperate and support the audit in good faith and to limit the overall cost. PSE will promptly make available documents, records and employees at all levels to expedite the inquiry.

- G. After the consultant delivers its final audit findings and recommendation, PSE will respond to each recommendation in writing, including a timetable for implementation of the recommendation or a discussion why implementation is not appropriate. PSE and Staff will agree on a method of resolving disagreements, should these occur. If PSE and staff cannot agree on a method, the matter will be taken to the Commission for resolution.
- H. As a matter of policy, Staff considers this independent audit to be an important tool to address needed improvements in PSE's gas safety programs, if any, and not to be a primary resource for future commission enforcement actions. Consequently, if in or during the audit it is discovered that PSE is in non-compliance with any relevant gas safety requirements, the consultant, PSE or Staff, as appropriate, will notify each other of the non-compliance and PSE will promptly correct the non-compliance.

In general, Staff does not intend to utilize information gathered from this effort to generate new enforcement actions and will not consider recommending the Commission issue a complaint regarding such non-compliance. However, Staff may consider recommending the Commission issue a complaint if the non-compliance reflects: 1) intentional misconduct other than the sort described in the complaint in Docket PG-060215, or 2) conduct that is systematic and/or widespread.

Nothing in this document affects the ability of the Staff to recommend penalties or other remedy for any violation of any statute, rule or provision in PSE's gas safety standards manual that leads to serious personal injury (*i.e.*, requires in-patient hospitalization), loss of life, or property damage or loss of \$50,000 or more. PSE may contest any enforcement action described in this paragraph, but PSE will not use anything in this Agreement as limiting any such enforcement action. This section does not affect paragraph 33 of the Settlement Agreement in Docket PG-060215.

- I. PSE will pay for the first \$250,000 of the audit without seeking recovery of this amount in rates. Nothing in this agreement prevents PSE from seeking recovery of additional audit expense through retail rates.

3. Scope:

To address gas safety issues within and beyond the scope of UTC Docket PG-060215, PSE and the UTC will agree on a consultant to review PSE's mandated gas safety-related activities.¹

The consultant will evaluate PSE's operations and those of its contractors and agents against current industry practices and standards and make recommendations on opportunities for process improvements or changes, including recommendations based on practices of other utilities that are efficient and effective.

¹ Mandated gas safety activities include all gas-related activities PSE undertakes to meet the requirements of state and/or federal gas safety rules.

The consultant will determine whether:

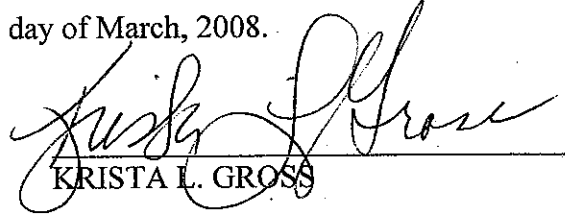
- A. PSE has programs, structures and incentives (implicit and explicit) in-place to maintain a “culture of safety and compliance” for PSE and its contractors and the extent to which PSE is responsive to employees or contractor employees bringing safety issues to management.
- B. The training PSE provides to or requires of its employees and contractor personnel for compliance with its standards and procedures is appropriate and effective.
- C. PSE’s contracts with its contractors are structured to ensure that gas facilities are installed, repaired or replaced properly, safely and cost-effectively.
- D. The methods that PSE employs to track and document work allow for auditing of such work for compliance by both PSE and the UTC.
- E. PSE’s practices related to 49 CFR 192.613 (continued surveillance) are effective and result in the company taking the appropriate action when needed.
- F. PSE has provided sufficient resources to its gas safety compliance program to adequately and effectively monitor its mandated safety activities and programs for compliance, whether those programs are implemented by PSE employees or contractor employees.

- G. Following the implementation period, the consultant will return to evaluate the effectiveness and completeness of the implementation of its recommendations. PSE will share this assessment with the commission.

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 3rd day of March, 2008.


KRISTA L. GROSS

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