

BEFORE THE WASHINGTON UTILITIES AND TRANSPORTATION COMMISSION

In the Matter of the Petition of

PUGET SOUND ENERGY, INC.

for (i) Approval of a Special Contract for Liquefied Natural Gas Fuel Service with Totem Ocean Trailer Express, Inc. and (ii) a Declaratory Order Approving the Methodology for Allocating Costs Between Regulated and Non-regulated Liquefied Natural Gas Services

DOCKET UG-151663

COMMISSION STAFF  
RESPONSE BRIEF

**I. INTRODUCTION**

1 Puget Sound Energy (“PSE” or “Company”) has requested the Washington Utilities and Transportation Commission (“Commission”) (i) approve exemptions from a Commission Order entered in 2007,<sup>1</sup> and (ii) allow one-half of the projected savings associated with an LNG facility at the Port of Tacoma to be treated as a project benefit that is to be added to the actual cost of the regulated asset base upon which the Company can earn a return from ratepayers.<sup>2</sup>

2 For the first request, an exemption from the Commission’s order is necessary because PSE’s parent is doing what it pledged not to do in 2007: Puget Energy seeks to operate and own a business other than PSE.<sup>3</sup> The Company’s second request is an attempt at

<sup>1</sup> *In the Matter of the Joint Application of Puget Holdings LLC and Puget Sound Energy, Inc. for an Order Authorizing Proposed Transaction*, Docket U-072375, Order 08 (Final Order), December 30, 2008. (“Merger Order”)

<sup>2</sup> *In the Matter of the Petition of Puget Sound Energy for (i) Approval of a Special Contract for Liquefied Natural Gas Fuel Service with Totem Ocean Trailer Express, Inc. and (ii) a Declaratory Order Approving the Methodology for Allocating Costs between Regulated and Non-regulated Liquefied Natural Gas Services*, Docket UG-151663, Brief of Puget Sound Energy, April 15, 2016. (“PSE Brief”)

<sup>3</sup> Docket U-072375, Merger Order at Appendix A, Commitment 56, Dec. 30, 2008.

risk mitigation and recognition that the project as currently conceived provides services to rate payers that would likely be more costly if the Company were to build a facility that solely serves the needs of its regulated activities. Staff wants to make clear that while it cannot issue its support at this time for the Company's plan, it is not per se opposed to an LNG facility at the Port of Tacoma. There may very well be broad merit to the plans offered by the Company; however, the Company's proposals invoke novel and complex questions of law and policy. Therefore, Commission Staff ("Staff") recommends the Commission continue on with the current proceeding and invite additional process to allow the Parties to present a full evidentiary record that insures a result that first, insulates rate payers from the risk associated with a new line of unregulated service and second, properly addresses the notion of sharing risk and benefits between the Company and regulated services. .

## **II. SUMMARY OF LEGAL ISSUES AND SCOPE OF COMMISSION AUTHORITY**

3           The first issue is whether to grant PSE an exemption to the Company's merger commitment(s). This is largely a policy question informed by the facts. The Commission is more than capable of weighing the risks and benefits of PSE's LNG facility against the importance of the ring-fencing provision(s) in the Commission's own order. The options appear to be accepting PSE's proposal, rejecting it, or simply sticking to the procedural schedule wherein the parties can present further information and evidence on the proposal's risks and benefits.<sup>4</sup> Here, Staff recommends the Commission adopt the latter option, believing a full record will inform and guide a decision on the necessity of preserving the ring-fencing provisions set forth in the Merger Order.

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<sup>4</sup> Perhaps PSE can develop a corporate-structure-to-be-named-later that allows PSE to construct the LNG plant and preserve merger commitments the Company made in 2007.

4 PSE's second issue wades into more complicated waters. PSE requests the Commission to guarantee a 50/50 sharing of the projected portfolio benefits associated with the LNG facility between ratepayers and shareholders. PSE requests such Commission authorization without final dollar figures, a full evidentiary record, or a completed project. In all material respects, PSE is requesting preapproval. Preapproval departs from the Commission's normal practices, however, and doing so without allowing adverse parties to present testimony raises questions of APA compliance and due process rights. Here again, Staff recommends that any decision on an "equity adder" be preserved until a complete evidentiary record can be provided the Commission on the issues described above, including the provision of notice to affected ratepayers of a decision possibly impacting their rates.

### **III. EXEMPTION FROM MERGER COMMITMENTS 56 AND 58**

#### **A. History of the Merger Order.**

5 A group of institutional investors purchased PSE a little less than a decade ago. As part of that process, those investors and the Company sought Commission approval for the acquisition of PSE's assets. The Commission and various parties engaged in a lengthy process that ultimately ended with approval of the merger conditioned on a series of commitments from the acquiring investors and the Company.<sup>5</sup>

6 The Commission's final order in the merger docket ("Merger Order") goes on at length about the importance of "ring-fencing" commitments that would protect the utility from its investors' unregulated activities or investments.<sup>6</sup> The Commission's Merger Order contains statements such as, "Ring-fencing is important" and "give the ratepayers the

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<sup>5</sup> Merger Order, Dec. 30, 2008.

<sup>6</sup> Merger Order at 76-82, Dec. 30, 2008.

substantial benefits of ring-fencing protection” and “the critically important fact that ring-fencing commitments create several layers of protection for PSE.”<sup>7</sup> It is no exaggeration to conclude that the Commission approved the PSE merger *because* of the ring-fencing commitments. The merger docket also included a dissenting opinion that advocated for even more stringent economic ring-fencing.<sup>8</sup>

7           The Commission was not alone in its enthusiasm. The Company also testified to the importance of ring-fencing. Mr. Christopher Leslie, the then-Executive Director of the Macquarie Group, testified:

These commitments are intended to isolate PSE’s regulated utility operations from any negative financial impacts flowing from unregulated units. The ring fencing commitments allow PSE to maintain a strong credit rating and attract capital. They prevent cross-subsidization of non-regulated ventures, and they provide the Commission access to timely and accurate information relating to PSE.<sup>9</sup>

**B. PSE’s proposal provides little to no actual ring-fencing.**

8           Under the Company’s proposal, Puget LNG would be a shell company. Puget LNG would have zero employees and no assets beyond a stake in an LNG facility co-owned by PSE.<sup>10</sup> Puget LNG could access capital only through Puget Energy’s credit facilities or from upstream shareholders over which the Commission has little or no control.<sup>11</sup> PSE is thus

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<sup>7</sup> Merger Order at 75 ¶181 and 81 ¶195, Dec. 30, 2008.

<sup>8</sup> “The ring-fencing and other commitments agreed by the investor consortium and the settling parties are extensive and purport to protect against many potential evils, but they are inadequate to mitigate the fundamental and inherent risks in the proposed transaction.” Docket U-072375, Dissenting Opinion of Commissioner Philip B. Jones, at 127 ¶5, Dec. 30, 2008.

<sup>9</sup> *In the Matter of the Joint Application of Puget Holdings LLC and Puget Sound Energy, Inc. for an Order Authorizing Proposed Transaction*, Docket U-072375, Direct Testimony of Christopher J. Leslie, Exh. No. CJL-1T at 34:27-35:1, Dec. 17, 2007. Mr. Leslie also highlighted ring-fencing provisions on rebuttal and in joint testimony in support of settlement. *See* Leslie Rebuttal Testimony (CJL-8HCT) at 19-27, July 8, 2008; Joint Rebuttal Testimony (JD-2CT), Aug. 12, 2008.

<sup>10</sup> PSE Brief at 14 ¶24 (citing Declaration of Roger Garratt in Support of the Brief of Puget Sound Energy at ¶16), April 15, 2016.

<sup>11</sup> PSE Brief at 21 ¶38.

Puget LNG's apparent source for liquidity, operational functionality, and borrowing capacity. As a consequence, PSE would also co-own the first asset against which creditors, or affiliates, may have recourse. The result seems clear: PSE's proposal largely removes economic ring-fencing between PSE and Puget LNG, and would expose the utility to the bankruptcy risks of its affiliate. The existing ring-fencing provisions protect the utility from such a result.<sup>12</sup>

**1. Puget LNG would use Puget Energy's credit facilities.**

9 PSE's brief contains few details of the Company's plans to secure financing for construction of the Tacoma LNG facility.<sup>13</sup> PSE does include a request for the Commission to waive merger commitment 58, if necessary, and allow Puget LNG to access Puget Energy's credit facilities.<sup>14</sup> The Company understandably cannot provide an exhaustive discussion of the borrowing arrangements, and no other Parties have been able to offer expert testimony about the impacts of such a waiver. For example, Staff has not verified issues such as the impact on Puget Energy's cost of debt, the extent, if any, to which creditors would have access to ownership of Puget Energy's utility assets, or whether creditors could convert outstanding debt to equity.<sup>15</sup> Thus, the Parties cannot attest in briefing that the utility's credit facilities should or should not be available to finance a project that includes a sizeable unregulated business venture.

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<sup>12</sup> PSE's existing ring-fencing provisions are believed sufficient to protect the utility from the bankruptcy of Puget Holdings or its subsidiaries. *In the Matter of the Joint Application of Puget Holdings LLC and Puget Sound Energy, Inc. for an Order Authorizing Proposed Transaction*, Docket U-072375, Testimony of Eric M. Markell, TR Vol. 6, at 538-539.

<sup>13</sup> See generally PSE Brief.

<sup>14</sup> PSE Brief at 21 ¶38.

<sup>15</sup> Declaration of David C. Gomez in Support of Staff's Brief, May 16, 2016. Transfer of ownership or issuance of shares would also fall under RCW 80.12.

**2. Operating costs are really an IOU from a shell company to the utility.**

10 Under the proposed operating agreement between PSE and Puget LNG, PSE would serve as the operator of the Tacoma LNG Facility.<sup>16</sup> Puget LNG would compensate PSE for its portion of the costs of operating the plant.<sup>17</sup> As a result, PSE would effectively grant credit to Puget LNG. Even accepting Puget LNG's creditworthiness, the creation of an IOU account between affiliates would, again, seem to reduce any legitimate form of economic ring-fencing between the utility and Puget LNG. Liability risk in the unlikely event of an accident would also sit squarely on PSE's lap as the operator of the LNG facility.

**C. Other corporate structures might better preserve the merger commitments.**

11 Staff believes the Commission should at least review alternative corporate structures that would allow the Company to build the Tacoma LNG Project and better preserve the merger commitments.<sup>18</sup> PSE's filing is, understandably, not an exhaustive discussion of potential business options. The Company's brief offers four choices and concludes that the proposed option is superior.<sup>19</sup> Staff supports a more robust analysis of business alternatives, including alternatives that PSE did not have the time or space to reveal to the Commission in this expedited proceeding.<sup>20</sup>

12 For example, PSE's brief states that the Company considered providing LNG fuel service for the non-peaker portion of the plant as a tariffed, fully regulated offering but ultimately rejected the idea because "for a number of reasons . . . the 'All Regulated'

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<sup>16</sup> PSE Brief at 15 ¶26.

<sup>17</sup> PSE Brief at 15 ¶26.

<sup>18</sup> Gomez Decl.

<sup>19</sup> PSE Brief at 8-11.

<sup>20</sup> Brief at 8 ¶ 15 ("PSE considered proceeding with the Tacoma LNG Facility under *at least* four alternative business models.") (emphasis added).

alternative business model was not feasible.”<sup>21</sup> The Company then cites to renegotiating the TOTE contract and not having enough time to complete a regulated tariff filing before a board meeting in June 2016.<sup>22</sup> Staff believes PSE’s citation to two issues directly within the Company’s own control (i.e. the contract terms PSE negotiated with TOTE and the timing of this filing) is not a sufficient evidentiary basis to conclude that another business structure is infeasible.

13 As noted in Staff’s declaration attached to this brief, there are two common sense alternatives to PSE’s proposal.<sup>23</sup> Both proposals merit at least some analysis and review from the non-company parties and the Commission. First, the Company can file a tariff for LNG transportation customers. The Commission just told PSE that LNG for motive power can fall within Commission jurisdiction.<sup>24</sup> Second, the Company could form Puget LNG as a subsidiary of Puget Holdings rather than Puget Energy.<sup>25</sup> A subsidiary at the Puget Holdings level would not appear to violate the merger commitments and would serve to better insulate regulated operations from liabilities and risks that attend the non-peaker portion of the plant and its services.

**D. Summary of Staff’s Recommendation - Staff understands the scope of Commission authority.**

14 The Commission is more than qualified to weigh the continued importance of ring-fencing against the potential benefits of Puget LNG. However, the Commission should recognize that those goals are mutually exclusive under PSE’s current proposal: either the Commission preserves the ring-fencing provisions or the Commission waives PSE’s merger

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<sup>21</sup> PSE Brief at 9 ¶16.

<sup>22</sup> PSE Brief at 9 ¶16.

<sup>23</sup> Gomez Decl.

<sup>24</sup> Docket UG-151663, Order 04 at 10 ¶19, Dec. 18, 2015.

<sup>25</sup> Gomez Decl.

commitments. With a full record, it is legally possible for the Commission to decide the ring-fencing provisions are no longer as important, the public interest in promoting LNG is more important than the merger commitments, Puget LNG's potential economic liabilities are immaterial to PSE's financial viability, or some combination thereof. For its part, Staff does not believe the Commission should make those determinations without that more complete record.

**E. The Merger Order contains other commitments that apply to PSE's proposal.**

15 Although PSE has requested exemptions from Merger Commitments 56 and 58, the Company's proposal implicates several other commitments included in Docket U-072375.<sup>26</sup>

1. **Commitment 9(ii) and 9(iii):** *PSE will . . . (ii) agree to prohibitions against loans or pledges of utility assets to Puget Energy or Puget Holdings without Commission approval; and (iii) generally hold PSE customers harmless from any business and financial risk exposures associated with Puget Energy, Puget Holdings and its other affiliates.*

16 Commitment 9 means the PSE's parent companies will not pledge the utility's assets to secure loans for non-utility operations and those same parents will hold PSE customers harmless from non-utility business and financial risks. PSE's proposal may thus violate Commitment 9 because the Company's proposed borrowing and corporate structure commingle utility and non-utility operations.

17 First, it is Staff's understanding that Puget LNG would borrow money through Puget Energy's credit facilities.<sup>27</sup> Puget Energy's credit facilities presumably include notice of Puget Energy's ownership of PSE. Second, PSE has requested this Commission authorize an

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<sup>26</sup> See Docket U-072375, Multiparty Settlement Stipulation, Appendix A, July 23, 2008 and Docket U-072375, Order 08 (Merger Order) at 4 ¶8, Dec. 30, 2008. The list of merger commitments was presented as Attachment A to the settlement stipulation in Docket U-072375. The Commission ratified those commitments, subject to certain clarifications, in Order 08 of that same docket.

<sup>27</sup> PSE Brief at 21 ¶38.



economic incentive that, depending upon one's perspective, can be seen either as an incentive to the Company for choosing an alternative less than a stand-alone facility or as a means of expressly shifting some of the Tacoma LNG Plant's risk to ratepayers.<sup>28</sup> If it's the latter, then PSE's request would effectively be a subsidy to its unregulated enterprise which reduces financial risk associated with a non-utility line of business.

2. **Commitment 26(a):** *In furtherance of Commitment 9: (a) Puget Holdings and PSE commit that PSE's customers will be held harmless from the liabilities of any non-regulated activity of PSE or Puget Holdings. In any proceeding before the Commission involving rates of PSE, the fair rate of return for PSE will be determined without regard to any adverse consequences that are demonstrated to be attributable to the non-regulated activities. Any new non-regulated subsidiary will be established as a subsidiary of either Puget Holdings, Puget Intermediate Holdings, Inc., or Puget Energy rather than as a subsidiary of PSE. . . ."*

18           Commitment 26 poses the same concerns as Commitment 9, above. Namely, the lack of substantive economic ring-fencing and express request for an economic incentive from ratepayers to shareholders mean the Company is not holding PSE ratepayers harmless from all risks of nonregulated activities.

3. **Commitment 19:** *Puget Holdings and PSE will make reasonable commitments, consistent with recent Commission merger orders, to provide access to PSE's books and records; access to financial information and filings; audit rights with respect to the documents supporting any costs that may be allocable to PSE; and access to PSE's board minutes, audit reports, and information provided to credit rating agencies pertaining to PSE.*

19           Commitment 19 means the Company must be completely transparent. Here, PSE and Puget LNG will be indistinguishable in operation.<sup>29</sup> In the highly competitive transportation fuel market, Puget LNG is very likely to generate business plans, costs, technology, and

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<sup>28</sup> PSE Brief at 1 ¶1.

<sup>29</sup> See PSE Brief at 14 ¶24 and 15 ¶26 ("It is not expected that Puget LNG would have employees" and "PSE would serve as the operator of the Tacoma LNG Facility")

strategies that are considered valuable trade secrets. The Commission and its Staff may not have access to those documents. This is not merely a hypothetical concern. PSE has already limited Staff access to certain documents in discovery.<sup>30</sup>

4. **Commitment 20: Affiliate Transactions, Cross-Subsidization:** *PSE agrees (i) to file cost allocation methodologies used to allocate Puget Energy or Puget Holdings-related costs to PSE; (ii) to propose methods and standards for treatment of affiliate transactions; and (iii) that there will be no cross-subsidization by PSE customers of unregulated activities.*

20 Commitment 20's first two points present more hypothetical concerns. Parties will almost certainly contest the PSE-Puget LNG cost allocation methodologies and affiliate transaction methods in this or future proceedings.<sup>31</sup> Operating cost allocations also go directly to how or whether PSE's proposal provides economic benefits to customers and represents the least cost alternative.<sup>32</sup> Part (iii) presents ripe concerns. Puget LNG's proposed use of Puget Energy's credit facilities creates the potential for an indirect subsidy to Puget LNG's cost of debt. PSE's request for an equal sharing of projected benefits between ratepayers and shareholders can also be considered a subsidy that reduces the risk profile of a non-utility operation.

#### IV. AUTHORIZE A 50/50 SHARING OF PORTFOLIO BENEFITS

21 PSE's request for a 50/50 sharing is really about reducing risk. From the ratepayer perspective, PSE's proposal is also about recognizing that the project may result in lower regulated cost than would a stand alone project that provides similar peaking service for regulated activity. When PSE committed to provide TOTE with LNG, oil was expensive and natural gas was not. The price spread between oil and natural gas is, for the moment, gone.

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<sup>30</sup> Gomez Decl.

<sup>31</sup> Merger Commitment 28 also concerns those affiliate transactions and allocation methodologies. Docket U-072375, Multiparty Settlement Stipulation, Appendix A, July 23, 2008

<sup>32</sup> Gomez Decl.

Projects designed for natural gas to displace petroleum-based fuels now carry far more risk. PSE rationally, and perhaps justifiably, seeks to reduce the risk of its LNG business venture by placing a share of that venture on ratepayers' shoulders.

**A. Timeline of Events.**

22 In 2013, TOTE received competitive proposals from bidders to provide LNG fuel to its ships at the Port of Tacoma. TOTE selected PSE's bid and the two companies agreed to contract terms in October 2014.<sup>33</sup> On October 27, 2014, the Brent Crude spot price was \$85.64; the Henry Hub Natural Gas spot price was \$3.56.<sup>34</sup> PSE initiated the present filing at the Commission ten months later on August 11, 2015, when Brent Crude and Henry Hub spot prices were \$47.33 and \$2.84, respectively.<sup>35</sup> After a series of questions around jurisdiction and clarifying the Company's request, the Parties and Commission agreed to the current proceeding where the Commission will review two issues prior to PSE's board meeting in summer 2016.

**B. PSE's contract with TOTE is the immovable object.**

23 PSE entered into a contractual agreement with TOTE on October 27, 2014.<sup>36</sup> PSE thus has a contractual obligation to provide TOTE with LNG service at the Port of Tacoma.

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<sup>33</sup> Riding, Exh. No. CR-4HC, Aug. 11, 2015 (copy of the TOTE Special Contract). Garratt, Exh. No. RG-1CT at 6:6-7, Aug. 11, 2015.

<sup>34</sup> Brent Crude is priced \$/barrel and Natural Gas is priced \$/million BTU. See Europe Brent Spot Price, US Energy Information Administration, [http://www.eia.gov/dnav/pet/PET\\_PRI\\_SPT\\_S1\\_D.htm](http://www.eia.gov/dnav/pet/PET_PRI_SPT_S1_D.htm) (accessed May 1, 2016) and Henry Hub Natural Gas Spot Price, US Energy Information Administration, <http://www.eia.gov/dnav/ng/hist/rngwhhdm.htm> (accessed May 1, 2016). Staff recognizes that PSE does not buy gas at Henry Hub, but daily Henry Hub spot price data is publicly available from the Energy Information Administration and supports Staff's general point that the price spread between gas and oil changed materially between the time PSE committed to TOTE and the time PSE filed its case with the Commission.

<sup>35</sup> Europe Brent Spot Price, US Energy Information Administration, [http://www.eia.gov/dnav/pet/PET\\_PRI\\_SPT\\_S1\\_D.htm](http://www.eia.gov/dnav/pet/PET_PRI_SPT_S1_D.htm) (accessed May 1, 2016) and Henry Hub Natural Gas Spot Price, US Energy Information Administration, <http://www.eia.gov/dnav/ng/hist/rngwhhdm.htm> (accessed May 1, 2016).

<sup>36</sup> Riding, Exh. No. CR-4HC, Aug. 11, 2015 (copy of the TOTE Special Contract filed as attachment 3). Garratt, Exh. No. RG-1CT at 6:6-7, Aug. 11, 2015.

Among its 100-plus pages, that contract contains provisions for non-performance and interim supply.<sup>37</sup> The bottom line is PSE and its shareholders already negotiated terms and conditions for the provision of LNG service at the Port of Tacoma, including those terms by which either party could terminate the agreement or avoid performance. The Commission's decision now will not change the terms agreed upon by TOTE and PSE.

24           The economics and benefits of combining a peaking resource with the Company's LNG obligations is a separate question from PSE's already-negotiated obligations to TOTE. The details and alternatives to PSE's peaking proposal should be explored by the Commission with access to a full evidentiary record. This is a far better outcome than the kind of pre-authorization or guarantee of future treatment now sought by PSE in this preliminary stage of litigation. The Company's request for a decision from the Commission based on the record to-date, while understandable under the circumstances, is not fair to potentially adverse Parties, ratepayers, or this Commission.

### **C.     Legal Concerns.**

#### **1.     The Administrative Procedure Act limits the usefulness of a declaratory order.**

25           PSE's filing in Docket UG-151663 is still officially a petition for declaratory order under RCW 34.05.240 of the Administrative Procedure Act ("APA").<sup>38</sup> The purpose of a declaratory order process is to declare the applicability of law to an unproven set of facts

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<sup>37</sup> Riding, Exh. No. CR-4HC, Aug. 11, 2015 (copy of the TOTE Special Contract filed as attachment 3).

<sup>38</sup> PSE initially filed this docket as a Petition. The Commission issued the requisite notices under RCW 34.05.240 and WAC 480-07-930. Staff, NWIGU, Public Counsel requested the Commission formally convert PSE's filing to a formal adjudication. All Parties to the litigation then reached an agreement to continue settlement negotiations and present threshold questions to the Commission. Therefore, PSE's filing appears to retain its status as a petition for declaratory order. *See* Docket UG-151663, Order 04 at 3-5 (Procedural History), Dec. 18, 2015.

presented by the Petitioner.<sup>39</sup> While it might be theoretically possible for the Commission to apply the public service statutes to the facts presented by PSE in this filing, such an application is exceedingly difficult and unhelpful in practice.<sup>40</sup>

26 First, the facts in this case are unverified, complicated, and would almost certainly be contested in an adjudicative proceeding.<sup>41</sup> Any Commission order would therefore only legally apply under PSE's hypothetical set of facts. When other parties inevitably contest any of those underlying facts, the Commission's declaratory order would serve little to no legal purpose. Therefore, a Commission order at this stage may only function to complicate a future proceeding in which PSE's proposed facts are disputed or otherwise heard.

27 Second, the Commission should not use its influence and resources to resolve hypothetical cases. Commission time and resources should generally be reserved for actual cases. Avoiding hypotheticals is particularly relevant in this case because the Commission is nearly certain to duplicate its efforts in a future proceeding.

28 Third, it is unclear if PSE's request meets the APA requirements for a declaratory order in RCW 34.05.240. Of particular note for this case, RCW 34.04.240(1) requires a petitioner to show that (a) an uncertainty necessitating resolution exists, (b) that there is actual controversy arising from uncertainty . . . , (c) that the uncertainty adversely affects the

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<sup>39</sup> See RCW 34.05.240(1) ("the applicability to *specified* circumstances of a rule, order, or statute enforceable by the agency" and "there is an *actual* controversy arising from the uncertainty such that a declaratory order will not be merely an advisory opinion.") (emphases added). See also 1981 Model APA § 2-103(d) cmt. (2000):

"there are no contested issues of fact in declaratory order proceedings because their function is to declare the applicability of the law in question to unproven facts furnished by petitioner. The actual existence of the facts . . . will usually become an issue only in a later proceeding"

<sup>40</sup> If Staff is mistaken and the Commission views the current docket as a formal adjudicative process under the APA, then the limited ability of the Commission to issue an order is even more clear. The APA requires agencies to provide all parties an opportunity to "respond, present evidence and argument, conduct cross-examination, and submit rebuttal evidence . . ." RCW 34.05.449(2).

<sup>41</sup> Gomez Decl.

petitioner, (d) that the adverse effect of uncertainty on the petitioner outweighs any adverse effects on others or on the general public. Here, the only apparent uncertainty is PSE's hesitancy to commit further capital to the LNG project without preauthorization from the Commission before a summer 2016 board meeting. Even accepting business risk from PSE's unilateral decision to bid, negotiate, and sign a contractual obligation to construct the LNG venture as legally acceptable "uncertainty", there is no evidence of actual controversy.<sup>42</sup> The non-company Parties have not presented testimony or attempted to block the LNG project, and Staff is completely unaware of whether TOTE and PSE are involved in a legal controversy over their negotiated contract.

29           It is also questionable whether the Company's uncertainty over a project for which it obligated itself and now seeks a regulatory decision to coincide with its director meetings could outweigh procedural and legal rights of the Parties to conduct discovery and present testimony on the reasonableness of costs, incentives, and the viability of alternatives before adding a large capital project into rates. Staff does not believe that it should.

**2.       PSE's request for preapproved rate treatment creates a statutory notice problem.**

30           A series of statutes and Commission rules require notice to affected parties prior to any rate change. Under RCW 80.28.060(1), "no change may be made in any rate or charge . . . or in any general privilege or facility" without notice to the Commission and public. The Commission can deviate from those notice requirements only after finding good cause.<sup>43</sup>

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<sup>42</sup> For reference to standards for declaratory actions in judicial settings, see *Diversified Industries Development Corp. v. Ripley*, 82 Wn.2d 811, 815 (1973) (preventing parties from obtaining a declaratory judgment on hypothetical, speculative, or premature claims) and *Port of Seattle v. Wash. Utils & Transp. Comm'n.*, 92 Wn.2d 789, 805-806 (1979) (refusing to issue declaratory judgment on a hypothetical factual situation)

<sup>43</sup> RCW 80.28.060(1)

Rules in WAC 480-90 also set out notice provisions for gas companies seeking any tariff changes to increase charges.

31 Here, PSE is not filing for a specific tariff change, but the Company is asking for a guarantee of future rate treatment that, if granted, would also guarantee a rate charge for PSE's customers. The Company's proposal is an ultimatum because PSE clearly argues throughout its brief that the Company will not build the LNG plant without a Commission preapproval.<sup>44</sup> Therefore, the lack of an opportunity for parties to present testimony and evidence also prompts due process concerns.

**3. Due Process requires the Commission to allow other parties to be heard before authorizing rate treatment.**

32 Due Process stems from the federal and state constitutions.<sup>45</sup> Constitutional property interests trigger due process rights and grant an affected party the right to be heard.<sup>46</sup> Due process rights can require hearings or opportunities to present evidence even when such a hearing is not required under the APA or another statute.<sup>47</sup>

33 PSE's request triggers due process concerns. PSE is requesting the Commission issue an order *to guarantee* future treatment of a yet-to-exist capital project. PSE again makes clear throughout its briefing that, absent such economic guarantee, the Company will not construct the LNG plant.<sup>48</sup> By asserting that the Commission's pre-authorization is a necessity, PSE's request is not just a theoretical application of law to proposed facts. The

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<sup>44</sup> *E.g.*, PSE Brief at 3 ¶6.

<sup>45</sup> U.S. Const. amend. XIV § 1 ("nor shall any State deprive any person of life, liberty, or property, without due process of law"). Wash. Const. art. 1 § 3.

<sup>46</sup> Any one of several hundred cases

<sup>47</sup> RCW 34.04.413 requires a hearing "when required by law or constitutional right . . ."

<sup>48</sup> *E.g.*, PSE Brief at 3 ¶6 ("The investors have determined that they cannot proceed with the construction of the Tacoma LNG Facility without an equitable sharing of the costs and benefits of the facility between PSE's investors and customers.") and 38 ¶66 ("Without an incentive of an equal sharing of the projected portfolio benefits, PSE can no longer proceed with the Tacoma LNG Facility")

Company is requesting preapproval of future rate treatment without an opportunity for other Parties to present evidence and witnesses.

34 The resulting legal analysis is straightforward. A guarantee of future rate treatment looks like an agency action under RCW 34.05.010(3).<sup>49</sup> Customers' financial obligations in the form of future rates are property interests under the APA, the public service statutes, and existing rules and understandings for rate setting in Washington State.<sup>50</sup> As a result, a state action that directly impacts customers' property interests should trigger those customers' due process rights.

35 In sum, PSE's request for an equal sharing is fundamentally about a guarantee for future ratemaking treatment. The Commission providing such a guarantee on an incomplete record and without affording affected parties an opportunity to present evidence likely violate customer groups' due process rights and leave the Commission's order open to appeal.

**C. Commission preapproval departs from traditional practice and is bad policy.**

36 It is the Company, and the Company alone, that must manage its operations for the benefit of its shareholders. The Commission is not a partner in the Company's business ventures.<sup>51</sup> Commissioners do not attend director meetings or receive shareholder dividends or have positions on the board. The Commission does not allocate company capital or set the

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<sup>49</sup> ““Agency action” means licensing, the implementation or enforcement of a statute, the adoption of an agency rule or order, the imposition of sanctions, or the granting or withholding of benefits.” RCW 34.05.010(3).

<sup>50</sup> Property interests are created and defined by existing rules or understandings that often stem from state law. *See e.g., Conard v. University of Washington*, 119 Wn.2d 519 (Wash. 1992) (stating that protected property interests can be established through contract, common law or statutes and regulation); RCW 80.28.020 (“the commission shall find *after hearing* . . .”) (emphasis added); RCW 80.28.060 (requiring proper notice for tariff changes or decisions “the effect of which is to increase any rate or charge”); WAC 480-07-300 (defining adjudicative proceedings to include general rate proceedings and declaratory order proceedings).

<sup>51</sup> *Wash. Utils. & Transp. Comm'n. v. Avista Utilities*, Docket UE-150204, Order 05 (final order) at 69 ¶192, January 6, 2016.



strategic vision for a regulated entity.<sup>52</sup> Regulation certainly plays an important role and is an indispensable fixture in the utility business landscape, but Commissioners should not be expected to serve as a preapproval board for the board of directors.

37 In this case, PSE has requested a Commission determination prior to the Company's board of directors meeting in summer 2016.<sup>53</sup> PSE is effectively asking the Commission to approve the project so that its own board of directors will have a somewhat easier decision to approve that same project later this summer. Traditional Commission practice requires the contrary order of events: the Company's board allocates capital and approves projects and the Commission sits as an ex-post economic regulator to review for prudence and reasonableness. Staff believes, as a matter of policy, the Commission should stick to its traditional role and decline to provide a preapproval decision for PSE's directors.

**D. Summary of Staff Recommendation - The Commission should not preapprove an equal sharing of projected LNG portfolio benefits.**

38 Staff recommends the Commission issue an order declining to offer judgment until the 50/50 sharing proposal arrives in a formal adjudicative process. Should this Commission want to go further, an order recognizing PSE's proposed situation as the *type* of situation where the Commission *would consider* non-traditional ratemaking tools is all that is necessary or legally valid.<sup>54</sup> Sound public policy also dictates that the Commission should not guarantee any future rate treatment on the basis of an incomplete record for the benefit of a regulated entity's officers and directors.

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<sup>52</sup> *Id.*

<sup>53</sup> PSE Brief at 9 ¶16.

<sup>54</sup> RCW 80.28.280 declares LNG and LNG fueling stations are in the public interest.

## V. CONCLUSION

39           The current record is incomplete. Absent a full process, the Commission will remain in the dark about cost certainties, alternative business models, usefulness for ratepayers, and economic viability of PSE's proposed LNG plant. Staff thus recommends the Commission decline the Company's invitation to act prior to a June 2016 board meeting and continue with the current proceeding. Alternatively, the Commission should invite further process and allow for the Parties to provide a full evidentiary record.

40           Staff recognizes the Commission has the expertise and legal authority to weigh the policy implications of the proposed merger waiver. Staff's current position comes down to "the Commission shouldn't grant an exemption now, but it has the authority to do so when it believes the public interest would be best served to take such action." PSE's proposed 50/50 sharing is more complicated. A declaratory order would have limited, if any, practical value and would, at the very least, be legally questionable.

41           Staff wants to re-iterate that it is not per se opposed to an LNG facility at the Port of Tacoma. As portrayed by PSE, the Tacoma LNG Project is probably a good, albeit risky, idea. At this point, however, given the complicated nature of the Company's proposal, the Commission should establish a formal process where Staff, PSE, and the intervening Parties

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can develop a complete record for the Commission. Staff remains prepared to explore all the evidence in an objective manner and arrive at the recommendation that is most fair to all stakeholders, including the Company.

DATED this 18<sup>th</sup> day of May 2016.

Respectfully submitted,

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