BEFORE THE WASHINGTON UTILITIES AND TRANSPORTATION COMMISSION

WASHINGTON UTILITIES AND TRANSPORTATION COMMISSION, Complainant, v. PUGET SOUND ENERGY, Respondent.	DOCKETS UE-151871 and UG-151872 (*consolidated*)

INITIAL BRIEF ON BEHALF OF COMMISSION STAFF

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I. INTRODUCTION

1 Puget Sound Energy (PSE or the Company) seeks to categorically expand its regulated utility business by launching a new, optional, tariff-based service for acquiring and maintaining equipment. PSE's proposal, however, does not qualify as a regulated utility service as a matter of law. The proposed service does not comport with traditional regulatory principles and lacks any credible connection to the Company's principle regulated service: the sale of electricity and natural gas. Moreover, the proposed service is a merchandising program that has the economic effect of a sale. As such, PSE would become a rate-regulated retailer of appliances, which statute expressly prohibits.[1] The proposal is also a distinct departure from both PSE's past and present utility services and the historical circumstances that have justified economic regulation as a substitute for competition. Indeed, the proposed service would be an optional, regulated service that awkwardly interacts with, and competes for customers within, a broader, existing, robust competitive market. PSE's proposed service does not fall within the bounds of Commission-regulated utility service under Washington law.

2 Even if the proposed service were jurisdictional, PSE failed to meet its most basic burdens of proof to establish a new, regulated service. Importantly, PSE did not develop a comprehensive strategy and business plan for the Commission's consideration in these dockets.[2] Instead, it presented a filing full of business jargon, but utterly devoid of substance. To support its proposal, the Company relies on a study rendered invalid by a

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[1] RCW 80.04.270.

[2] Norton, TR. 165:11-168:18; See *In re Amending and Repealing Rules in WAC 480-108 Relating to Electric Companies- Interconnection With Electric Generators*, Interpretive Statement Concerning Commission Jurisdiction and Regulation of Third-Party Owners of Net Metering Facilities, Docket UE-112133, ¶ 77 n. 100 (July 30, 2014).

calculation error and outdated, questionably relevant data.[3] It further relies on a biased, customer survey with no relevant sponsoring witness. Building a house of cards, the Company then used this dubious evidence to develop its rates and allege significant public benefits. The Company's proposed rates are not fair, just, or reasonable. Rather, they are discriminatory. In addition, the consumer protection issues raised by PSE's unfair tariff are numerous and insurmountable. PSE's proposal is alarmingly deficient and should be rejected by the Commission.

3 PSE's filing has also been a moving target from the day it was filed[4] through the close of the record.[5] Of particular concern, the Company materially expanded its proposal on rebuttal by promising to add new products and features and to change the rates only after the Commission approved the proposed service. PSE's attempt to punt its burden of proof until after a Commission decision compromises the administrative process by precluding meaningful review. The Company's attempt to categorically expand its regulated utility business without complying with the most basic requirements for a regulated tariff-based service should fail.

4 Commission Staff requests that the Commission reject PSE's deficient proposal and affirm, as a general principle, that regulated utility service ends at the customer meter unless the overreaching service is narrowly tailored to provide compelling net-benefits to all

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[3] *See* Teller, Exh. No. JET-3 (add up numbers in each percentage column for vintages 1966-1995); Norton, TR. 221:25-230:23 (This is addressed in detail in Section III.A.1. below.).
[4] *Wash. Utils. & Transp. Comm'n v. Puget Sound Energy,* Dockets UE-151871 & UG-151872, Advice No. 2015-23 (Sept. 18, 2015) (hereinafter "Dockets UE-151871 & UG-151872") (PSE did not provide any pre-filed testimony to substantiate its proposed leasing service; only a cover letter that broadly described the proposal accompanied the tariff sheets, which contained terms, but not rates.).
[5] *See* Dockets UE-151871 & UG-151872, Staff Response to PSE Response to Bench Request 1, from Sally Brown (Aug. 10, 2016); Response to Puget Sound Energy's Response to Request No. 1 and Motion to Strike on Behalf of Public Counsel, from Lisa W. Gafken (Aug. 15, 2016); *see also* Dockets UE-151871 & UG-151872, Motion for Summary Determination, ¶¶ 3-7 (July 13, 2016).

customers or otherwise fulfills some statutory purpose articulated in the public service laws. This general principle is fully consistent with legal precedent as well as PSE's past and present optional services. The general principle is also sufficiently flexible to allow the scope of regulated utility service to evolve as circumstance demands. PSE's recent propensity for proposing services that stretch the traditional bounds of regulated utility service demonstrates that the Company would benefit from Commission guidance. Establishing the general principle recommended by Staff would be a helpful start.

II. PSE'S LEASING PROPOSAL IS NOT A REGULATED UTILITY SERVICE

A. PSE's Leasing Platform Would Categorically Expand Regulated Utility Service

PSE seeks to expand its regulated utility business by launching a new optional, tariff-based service for acquiring and maintaining equipment. The Company proposes to initially offer a variety of commercial and residential space and water heat appliances; however, it intentionally designed its "leasing platform" with the flexibility to support additional product offerings, such as solar panels, batteries, electric vehicle equipment, generators,[6] windows, doors, insulation, and any other product that customers are interested in paying for over time.[7] According to PSE: [redacted][8]

[6] Cebulko, Exh. No. BTC-1HCT 5:19-21, Dockets UE-151871 & UG-151872, Advice No. 2015-23, at 2 (Sept. 18, 2015); O'Connell, Exh. No. ECO-3HC at 3.
[7] Englert, TR. 401:8-402:6.
[8] O'Connell, Exh. No. ECO-3HC at 11.

6 Under its proposal, customers would enter into a contract with PSE to pay a fixed monthly rate over a 10-18 year term (depending on the product) for the bundled use, installation, maintenance, and potential repair of a particular product.[9] The contract term is based on PSE's estimate of the "useful life" of each product, which reflects the predicted economic life of the product, not necessarily how long the product remains functional or operational.[10] In fact, PSE claims the service will address an alleged "market gap" by encouraging customers to replace older, but still functioning equipment (service availability and marketing efforts, however, would not be limited to this "market gap").[11] While PSE reserves the flexibility to terminate the lease "at any time upon 30 days' written notice," customers' only option for escaping the agreement before the end of the contract term would be to purchase the equipment.[12]

7 PSE proposes monthly rates based on averages of cost estimates, rather than the actual costs of the products and services customers would receive. As PSE testified: "[Its] rates are built on *estimates of all costs* borne by the Company in installing, operating and maintaining the equipment over the life of the lease term [10-18 years]."[13] These estimates include equipment costs developed by averaging sample costs from multiple contractors for a wide variety of products.[14] Yet, the Company would record in its books "the actual original costs of the assets," rather than the cost estimates embedded in the rates.[15] The actual costs, however, are not yet known because the Company has not contracted for, or

[9] Proposed Sched. 75, Sheet 75-E at § 5.2.
[10] *See* O'Connell, Exh. No. ECO-20; Norton, TR. at 176:21-177:2.
[11] Teller, Exh. No JET-1T at 2:12-17.
[12] Subst. Proposed Sched. 75, Sheets 75-U, 75-R at§§ 5.9, 5.12.b.
[13] McCulloch, Exh. No. MBM-1T at 18:12-14 (emphasis added).
[14] *Id.* at 18:10-19:23; O'Connell, Exh. No. ECO-1THC at 16:10-20; *see* O'Connell, Exh. No. ECO-8HC.
[15] Marcelia, Exh. No. MRM-1T at 15:7-8.

even identified, the specific equipment (makes or models) it would offer.[16] The Company also undertook a similar averaging exercise to estimate installation costs, maintenance costs, repair costs, and the cost of bad debt per unit.[17] No costs included in PSE's proposed rates are known and measurable, [18] which would explain why PSE's initial tariff filing contained *no* rates at all. Exacerbating this inherent problem of cost uncertainty is the fact that each customer's rate would be fixed for the entire contract term; any future rate change that better reflects the true cost of the proposed service would apply only to customers that enter a contract after the new, changed rates go into effect.[19] Similarly situated customers would thus pay different rates for the same product and service, and neither rate would necessarily reflect the actual aggregate cost of the product and service they receive. In other words, fixed-rates based on averages of cost estimates virtually guarantee that cross-generational subsidies within each class of participating customers will occur.[20]

8 By its own admission, PSE does not possess [redacted] to implement its proposed service.[21] The Company plans to engage "service partners [to] facilitate the equipment distribution and in-home fulfillment tasks, including pre-installation site checks, permitting, installation, maintenance, and service repair."[22] The Company proposes to employ three different "paths" to engage service partners.[23] Each path would involve a different level of involvement and responsibilities for

[16] McCulloch, Exh. No. MBM-7T at 8:11-9:9; O'Connell, Exh. No. ECO-9.
[17] McCulloch, TR. at 222:24-225:2.
[18] O'Connell, Exh. No. ECO-1THC at 16:6-8.
[19] McCulloch, Exhibit No. MBM-1T at 11:1-10.
[20] Cebulko, Exh. No. BTC-1HCT at 24:13-14.
[21] O'Connell, Exhibit No. ECO-3HC at 17.
[22] McCulloch, Exh. No. MBM-1T at 15:3-6; *see also* 16:7-17:15.
[23] *Id.* at 15:14-17:15.

both PSE and the service provider.[24] While each path results in a different underlying cost to PSE, customers would pay the same rate regardless, which violates principles of cost causation and again causes cross-subsidization problems.[25] Under each path, PSE's fundamental role is to finance and administer the contracts.[26]

9 PSE plans on conducting its proposed service on an extensive scale. [redacted].[28] The Company testified that "up to 25% of its customers have expressed interest in the service" based on a deeply flawed survey.[29] However, [redacted][31] PSE's ambitious projections are limited to the initial product offerings; they do not account for any additional products or services it hopes to eventually offer.

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[24] *Id.*
[25] O'Connell, Exh. No. ECO-1HCT at 5:1-7.
[26] *Id.* at 10:10-13; Cebulko, Exh. No. BTC-1HCT at 6:5-6.
[27] O'Connell, Exhibit No. ECO-3HC at 3.
[28] *Id.* at 10.
[29] Teller, Exh. No. JET-1T at 5:20-22.
[30] Cebulko, Exh. No BTC-2HC.
[31] *Id.*

10 According to PSE, [redacted]."[32] PSE claims no comparable service is otherwise available in the appliance market.[33] But, the only unique aspect of the proposed service is the on-bill repayment, which PSE exclusively can provide given its de facto monopoly over the provision of retail energy in its service territory.[34] As Staff notes, "similar appliances, installation, maintenance and repair services, and long-term financing options are all available through numerous competitive retail providers, financial institutions, and service contractors."[35] These similar competitive services are generally more flexible and less expensive than PSE's proposed service.[36]

11 PSE's proposed service represents a distinct departure from the Company's past and present regulated utility service.[37] In the 1960s, the Commission approved PSE's legacy rental program because it was narrowly tailored to deliver compelling benefits to the Company's entire customer base by promoting the sale of gas.[38] In contrast, the proposed service lacks any credible public purpose.[39] While the Company alleges the proposed service will produce conservation benefits for all customers at no cost,[40] its claims are illusory[41] and entirely speculative because the Company has not committed to—nor would it be

[32] O'Connell, Exh. No. ECO-3HC at 8.
[33] Teller, Exh. No. JET-1T at 5:17-20.
[34] Cebulko, Exh. No. BTC-1HCT at 7:20-22.
[35] *Id.* at 7:18-20; Exh. No. BTC-6.
[36] O'Connell, Exh. No. ECO-1HCT at 42:7-46:7; Kimball, Exh. No. MMK-1HCT at 25:5-29:16.
[37] Cebulko, Exh. No. BTC-1HCT at 2:13-20.
[38] *Cole v. Wash. Natural Gas Co.*, U-9621 (1968) at 31.
[39] Cebulko, Exh. No. BTC-1HCT at 11:1-3; *Cole v. Wash. Natural Gas Co.*, U-9621 (1968) at 31.
[40] Norton, Exh. No. LYN-T at 25:18-20; Englert, Exh. No. EEE-1T at 8:20-22.
[41] An "illusory promise" is "An apparent promise which, according to its terms, makes performance optional with the promisor no matter what may happen, or no matter what course of conduct in other respects he may pursue, is in fact no promise. Samuel Williston, *A Treatise on the Law of Contracts* § 1A, at 5 (Walter H.E. Jaeger ed., 3d ed. 1957).

accountable for—delivering any quantifiable benefit.[42] By making this illusory promise to realize gains in energy efficiency, PSE remains free to offer products that meet the code minimum for efficiency. Indeed, because of the price structure of PSE's tariff, the Company actually provides an incentive for customers to choose the least efficient products it offers.[43] Granted, this new appliance may be more efficient than the one it replaces, but this is true only because the product is new. Ultimately, the Company designed an optional service that more closely resembles "current market conditions,"[44] and which customers can elect to participate in if they view the service "as beneficial and reasonably priced for the benefits they receive."[45] PSE designed the proposed service solely for the private benefit of participating customers and the Company's shareholders.

12 Importantly, the legacy rental program became a significant burden to the Company's customers, after initial success. By 1992, the program represented about 15 percent of the Company's rate base,[46] its policy purpose (to build out load) was no longer valid,[47] and it required substantial subsidization by general customers.[48] The Commission agreed that the program was "flawed," but it allowed the Company an opportunity to implement proposed solutions to see if the program could again benefit all customers by maximizing efficient use of resources.[49] PSE's solutions failed. In 2000, the Company filed to discontinue the program for new customers because it was "unable to cost effectively

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[42] Englert, TR. at 385:8-15.
[43] Cebulko, BTC-1THC at 38:12-39:2.
[44] McCulloch, Exh. No. MBM-1T at 10:1-6.
[45] Teller, Exh. No. JET-1T at 6:5-7.
[46] *Wash. Utils. & Transp. Comm'n v. Wash. Nat'l Gas Co.*, Docket UG-920840, Fourth Supplemental Order, at 16:4 (Sept. 27, 1993).
[47] Cebulko, Exh. No. BTC-1HCT at 14:1.
[48] *Id.* at 13:12-15.
[49] *Id.* at 13:12-15:9; *Wash. Utils. & Transp. Comm'n v. Wash. Nat'l Gas Co.*, Docket No. UG-920840, Fourth Supplemental Order, at 16:4 (Sep. 27, 1993).

provide these services to new residential and commercial customers under the existing program and rate structure."[50]

13 PSE's proposal also represents a distinct departure from the optional, equipment services that the Company currently offers. In addition to its failed legacy rental program, PSE cites its substation rentals and electric lighting schedules as comparable "optional company-owned end-use equipment service."[51] The Company's testimony that substation rentals are an end-use service because "the transformation of electricity uses electricity" is laughable.[52] By this logic, the generation and transmission of electricity are also end-use services. Substation rentals are simply not comparable to HVAC and water heating appliances: there is a limited supply and demand for such equipment, PSE is uniquely positioned to provide the service, and the equipment is located on the Company's side of the meter.[53] The same is true for the Company's lighting services,[54] which are also on the Company-side of the meter.[55] PSE has never offered as a regulated utility service anything comparable in design, scope, or scale to the service it proposes in these dockets.

14 Upon review, Commission Staff found that PSE's proposed service is fundamentally a merchandising and financing service.[56] PSE failed to demonstrate that its program would

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[50] Docket No. UG-000763, Advice No. 2000-09 Natural Gas Filing Water Heater Rental Service (May 18, 2000).
[51] Englert, Exh. No. EEE-1T 3:5-11, 7:4-26; Englert, TR. at 389:19-391:9.
[52] Englert, TR. at 391:4-6.
[53] Cebulko, Exh. No. BTC-1HCT at 19:2-20:3; Englert, TR. at 390:19-21.
[54] Cebulko, Exh. No. BTC-1HCT at 19:2-20:3.
[55] Despite Mr. Englert's testimony at hearing (*see* Englert, TR. at 398:7-20), the Company's lighting services are unmetered and the equipment is attached directly to the Company's distribution system—i.e., on the Company-side of the meter (*see* PSE Tariff Schedule 50, Sheet 50-b, 6. Other loads on lighting system). The lighting rates generally include fixture, maintenance, and energy consumption costs based on when the lights turn on. If the lighting load was on the customer-side of the meter there would need to be separate tariffed rates in the light schedules that do not include the energy cost so that customers do not pay for their energy consumption twice. In other words, if the Company is also metering these services in some instances and billing for the load under its general service schedule, then the Company is double charging customers. This situation may warrant further investigation by Consumer Protection Staff.
[56] Cebulko, Exh. No. BTC-HCT at 6:11-20; O'Connell, Exh. No. ECO-1HCT at 3:4-13.

produce system benefits for all customers or cost-effective benefits to participating customers.[57] Moreover, "PSE's fundamental role in providing the service is the administration and financing of the lease program—activities more in common with a financial institution than a public service company."[58] Staff also found that the transaction sought by PSE has the economic effect of a sale.[59] As such, PSE would become a rate-regulated retailer of appliances, which is expressly prohibited by statute.[60] PSE's service—for all intents and purposes—is a merchandising program.[61] It is an attempt to categorically expand the Company's regulated utility service to include the primary business of merchandising and financing equipment. The Commission should reject the Company's deficient proposal and clarify the bounds of regulated utility service in Washington State.

B. PSE's Proposed Service is not a Regulated Utility Service as a Matter of Law

15 PSE's proposed service raises fundamental questions about the intended scope of regulated utility service. The Commission should find the proposed service does not qualify as a regulated utility service under Washington law. That is not to say leasing is never a legitimate utility function. Staff acknowledges that equipment leasing may be appropriate under certain circumstance.[62] But jurisdiction over regulated utility service is not without limitation, as the Company should concede.[63] Given PSE's recent propensity for proposing services that stretch the traditional bounds of regulated utility service,[64] the Commission

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[57] Cebulko, Exh. No. BTC-HCT at 20:7-21:11.
[58] O'Connell, Exh. No. ECO-1HCT at 9:3-5, 10:11-13.
[59] *Id.* at 11:3-5, 30:1-42:3.
[60] RCW 80.04.270.
[61] O'Connell, Exh. No. ECO-1HCT at 42:3.
[62] Cebulko, Exh. No. BTC-HCT at 10:1-13, 41-1:10.
[63] Englert, TR. 402:2-6; *See* Englert, TR. 399:7-402:6.
[64] *See In re Matter if 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,*

should affirm that, as a general principle, regulated utility service ends at the customer meter unless the overreaching service is narrowly tailored to provide compelling net-benefits to all customers or otherwise fulfills some statutory purpose articulated in the public service laws.

16 The Commission, "is an administrative agency created by statute and as such has no inherent powers, but only [those] expressly granted to it by the legislature or have, by implication, been conferred upon it as necessarily incident to the exercise of those powers expressly granted."[65] The legislature conferred upon the Commission the general authority to: "Regulate in the public interest, *as provided by the public service laws*, the rates, services, facilities, and practices of all persons engaging within this state in the business of supplying any utility service or commodity to the public for compensation."[66] While several pertinent definitions establish the broad scope of utility service,[67] utility service itself is not a defined term.

17 The public service laws expressly empower the Commission to determine the reasonableness and justness of any rate schedule "the effect of which is to change any rate, charge, *rental*, or toll;"[68] but they do not plainly state that the Commission's authority over "rentals" extends to HVAC, water heater, or any other equipment leasing. The scope of regulated utility service is broad and ambiguous. The Commission must therefore determine in its best judgment whether the legislature intended regulated utility service to encompass PSE's proposal, and further, whether expanding the current scope of regulated utility service

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Docket UG-151663, Order 04, (Dec. 18, 2015); *In the Matter of Puget Sound Energy's Application for Approval of a Special Contract under WAC 480-80-143*, UG-160748, Order 01, (July 7, 2016).
[65] *State ex rel. Pub. Util. Dist. v. Dep't of Pub. Serv.*, 21 Wn.2d 201, 208-09 (1944).
[66] RCW 80.01.040(3) (emphasis added).
[67] RCW 80.04.010 (see the definitions of public service company; electrical [and gas] company; and electrical [and gas] plant); *In re Amending and Repealing Rules in WAC 480-108 Relating to Electric Companies-Interconnection With Electric Generators*, Interpretive Statement Concerning Commission Jurisdiction and Regulation of Third-Party Owners of Net Metering Facilities, Docket UE-112133, ¶¶ 52-56 (July 30, 2014)).
[68] RCW 80.04.130(1).

in the manner PSE has proposed is in the public interest. Upon review of the evidence in record, the Commission will find that PSE's proposed service is both unprecedented in scope and not a regulated utility service as a matter of law.

18 Importantly, the Commission has never broadly held that public service companies could lease equipment without limitation.[69] In *Cole v. Wash. Natural Gas Co.*, U-9621 (1968) ("Leasing Order"), the Commission more narrowly determined that it is empowered to regulate rates—including rental charges—for "any service rendered *in connection with gas [or electricity] sales*."[70] A full reading of the Commission's Leasing Order demonstrates the critical import of a public purpose connection between the rental service and the utility's principle regulated service—the sale of energy.[71]

19 In the Leasing Order, the Commission ultimately found the rental service connected to PSE's sale of energy because the promotional service was narrowly tailored to deliver compelling benefits to all of the Company's customers. Specifically, the Commission's decision meticulously established the legitimate function of promotional practices designed to increase energy sales and improve system load factor because such practices result in real benefits to both the utility and all its customers.[72] After a detailed discussion of court and utility commission precedent from other jurisdictions, as well as the record evidence demonstrating the rental program was delivering on its promotional purpose, the Commission found:

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[69] *See* Dockets UE-151871 & UG-151872, *Puget Sound Energy's Opposition to Commission Staff's Motion for Summary Determination*, at 13-14; Englert, TR. at 402:2-6; See generally Englert, TR. at 399:7-402-6.
[70] *Cole v. Wash. Natural Gas Co.*, U-9621 (1968) at 20 (emphasis added).
[71] McCulloch, Exh. No. MBM-36 ("[PSE's] focus is to concentrate on its *core business: retail electric and natural gas utility service* within a regulated environment. The company's strategy emphasizes meeting the energy needs of the growing PSE customer base through incremental, cost-effective energy conservation, low-cost procurement of traditional energy resources (including by producing and generating electricity and natural gas), and far-sighted investment in *energy-delivery infrastructure.*" (emphasis added).).
[72] *Cole v. Wash. Natural Gas Co.*, U-9621 (1968) at 17-31.

> the rental program has resulted in the company being able to improve earnings, reduce rates and gain more customers. It has made a significant contribution to the development and growth of Washington Natural to the benefit of rate payers and share holders. Inactive services have been activated. More gas is being sold to more persons than would be the case without the program. As the company has been able to improve earnings and reduce rates and gain more customers, it has been able to attract the large sums of money necessary to expand its systems to meet the customers' demands. The rental programs have made a significant contribution to the rate reductions in previous years [$1.69 million annually from 1961 – 1966].[73] It has been of benefit to *all its customers*.[74]

The Commission also differentiated the promotional purpose of the program from unlawful merchandising. In discussing RCW 80.04.270, which prohibits public service companies from engaging in the sale of merchandise or appliances, the Commission explained:

> the statute was enacted to *prevent a public utility from conducting such business on an extensive scale where the primary business was merchandising*. Where, however, as in the instant case, the purpose of the public utility is not the sale of the appliance but the purpose is to build load to gain gas customers and to give prospective gas customers who could not afford to purchase the necessary equipment the opportunity to have gas service within their means without the necessity of purchasing the appliances, then the leasing program is not a non-utility function . . ."[75]

Of note, the Commission further established that it would be improper to separate the promotional service from the Company's principle regulated service: "[T]o isolate the revenues and expenses of the rental equipment and treat them as distinct from *the gas sales they are designed to promote* is not only illogical, it is inconsistent to the established regulatory view of such programs."[76]

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[73] *Id.* at 31.
[74] *Cole v. Wash. Natural Gas Co.*, U-9621 (1968) at 31.
[75] *Id.* at 17 (emphasis added).
[76] *Id.* at 37 (emphasis added) (*citing* New York Public Service Commission, April 25, 1967, *Promotional Activities by Gas and Electric Corporations in New York State*, 68 P.U.R. 3d 162, at page 169; Connecticut Public Utilities Commission, November 10, 1966: *Re Promotional Practices of Electric and Gas Utilities*, 65 P.U.R. 3d 405; Maine Public Utilities Commission, June 10, 1965: *Kenneth R. Gifford, et al. v. Central Maine Power Company*, 63 P.U.R. 3d 205, affirmed by Supreme Court of Maine at 63 P.U.R. 3d 208, 212 (1966); New Jersey Superior Court Appellate Division, sustaining promotional program carried on by the City of

20 In *Cole v. Wash. Util. & Transp. Comm'n*, the Supreme Court affirmed the challenged aspects of the Commission's Order.[77] In particular, the Court confirmed the appliance leasing practice was a justifiable "method of stimulating growth of the utility enterprise."[78] The Court also affirmed that Washington law prohibits regulated utility service from engaging in equipment sales, not leases, and that the difference between the two is a question of fact concerning the underlying economic transaction, not a question of statutory interpretation:

> [T]here is a well-recognized difference in meaning between the terms 'sale' and 'lease,' and that the jurisdictional exclusion of RCW 80.04.270 relates only to the former. Absent proof by the appellants of *incidents of sale in the agreement* between the gas company and its customers, appellants cannot expect the commission to decide that a common lease falls within the purview of RCW 80.04.270.[79]

Like the Commission, the Court did not broadly hold that regulated utilities could lease equipment without limitation; it confirmed that *some* leasing activities fall within the scope of regulated utility service. Ultimately, to qualify as a regulated utility service, leasing activities must have a legitimate public purpose connection to the Company's sale of energy. PSE's proposed service, however, lacks this necessary connection.

1. PSE's proposed service lacks a public purpose connection to its sale of energy

21 PSE's proposed service is easily distinguishable from its legacy rental program because it lacks any credible connection to the Company's principle regulated service—the sale of energy. PSE intentionally designed the proposed service to be distinct from its sale of

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Vineland, *George A. Rossi, et al. v Henry A. Garton, Jr., Mayor*, 88 N.J. Super. 233, 211 Atl. 2d 806, 60 P.U.R. 3d 210 (1965)).

[77] *Cole v. Wash. Util. & Transp. Comm'n*, 79 Wn.2d 302 (1971).

[78] *Id. at* 307-08.

[79] *Id.* at 307 (emphasis added).

energy. It characterizes its proposal as a "stand-alone separate tariff rate schedule."[80] PSE also "[took] care to design the service" in a manner that attempts to isolate the revenues and expenses of the equipment and treats them as distinct from the Company's sale of energy:

> all costs for [the service] are included in the proposed rates and paid for by participants. . . . The rates were not set as part of the revenue requirement and rate spread/rate design in a general rate case, nor will they be in the future.[81]

The Commission, however, determined with regard to the legacy rental program that severing the financial connection between the sale of energy and services connected therewith is "not only illogical, it is inconsistent to the established regulatory view of such programs."[82]

22 In its rebuttal testimony, PSE also raised the specter of its "survival" and then claimed the proposed service would "provide new revenue and earnings opportunities that will provide the utility greater financial stability."[83] Yet, there is no evidence in the record to substantiate PSE's financial stability is at stake; a general rate case would be necessary to make such a determination. Even if such claims were true as well as substantiated, it would only make it more illogical to isolate the proposed service from the rest of its business as the Company has proposed.

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[80] Englert, Exh. No. EEE-1T at 8:16.
[81] Norton, Exh. No. LYN-1T at 25:20-26:2.
[82] *Cole v. Wash. Natural Gas Co.*, U-9621 (1968) at 37 (emphasis added) (*citing* New York Public Service Commission, April 25, 1967, *Promotional Activities by Gas and Electric Corporations in New York State*, 68 P.U.R. 3d 162, at page 169; Connecticut Public Utilities Commission, November 10, 1966: *Re Promotional Practices of Electric and Gas Utilities*, 65 P.U.R. 3d 405; Maine Public Utilities Commission, June 10, 1965: *Kenneth R. Gifford, et al. v. Central Maine Power Company*, 63 P.U.R. 3d 205, affirmed by Supreme Court of Maine at 63 P.U.R. 3d 208, 212 (1966); New Jersey Superior Court Appellate Division, sustaining promotional program carried on by the City of Vineland, *George A. Rossi, et al. v Henry A. Garton, Jr., Mayor*, 88 N.J. Super. 233, 211 Atl. 2d 806, 60 P.U.R. 3d 210 (1965)).
[83] Norton, Exh. No. LYN-1T at 14:14-21.

23 The proposed service further lacks any purposeful connection to PSE's principle regulated service because the Company designed the service to provide only private benefits, not public benefits. According to the Company, the core purpose of the proposal is to offer an "optional service" that customers can elect to participate in "if [they] view the lease service as beneficial and reasonably priced for the benefits they receive."[84] The Company alleges the proposed service will produce public benefits for all customers at no cost because the service may yield conservation savings as an ancillary effect of some of the equipment offered.[85] It testified: "Once in place, these tariff schedules will provide a structure and a channel to support additional services and products, *some* of which *may* have conservation savings or other public benefits."[86] Yet, the proposed service is also, paradoxically, not a conservation program according to the Company.[87] Indeed, the Company has not committed to—nor would it be accountable for—delivering any quantifiable public benefit.[88] PSE, admittedly, would face no consequence for failing to deliver conservation savings under the proposed service.[89] PSE's promise of public benefits is illusory; it is a promise "which according to its terms makes performance optional with the promisor."[90]

24 The proposed service also lacks a credible connection to PSE's sale of energy because it is designed to address an alleged "gap" in the competitive HVAC and water heat market,[91] rather than one of the many real challenges it faces in effectively delivering its

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[84] Teller, Exh. No. JET-1T at 6:5-7.
[85] Norton, Exh. No. LYN-T at 25:18-20; Englert, Exh. No. EEE-1T at 8:20-22.
[86] Englert, Exh. No. EEE-1T at 9:5-7 (emphasis added); O'Connell, Exh. No. ECO-HCT at 13:1-17.
[87] Englert, Exh. No. EEE-1T at 8:19-20.
[88] Englert, TR. at 385:8-15.
[89] *Id.* at 386:1-4.
[90] *King Cty. v. Taxpayers of King Cty.*, 133 Wn.2d 584, 600, 949 P.2d 1260, 1268 (1997).
[91] Teller, Exh. No. JET-1T at 2:8-13.

principle regulated service. The proposed service is so distinct from its principle regulated service that PSE does not possess [redacted] to implement the service.[92] It must engage "service partners [to] facilitate the equipment distribution and in-home fulfillment tasks, including pre-installation site checks, permitting, installation, maintenance, and service repair."[93] PSE's fundamental role in providing the service is financing and administering the contracts.[94] [redacted]

[redacted][95]

[redacted][96]

25 The glaring lack of any credible connection between PSE's proposed service and its regulated sale of energy is best demonstrated by the fact that the Company intends to offer appliances to customers that do not receive its service. PSE testified at hearing that it structured the tariff to allow it to offer electric appliances in Seattle, despite the fact that it does not provide electric service in Seattle (only gas service).[97] Obviously, no credible connection exists between PSE's leasing of electric equipment and its sale of electricity if the customers who would lease the electric equipment do not receive electric service from the Company. Likewise, no connection exists between the Company's leasing of electric equipment and its sale of gas. This Seattle example demonstrates that PSE's proposed service lacks any connection to its sale of energy. In reality, the purpose of the leasing

[92] O'Connell, Exh. No. ECO-3HC at 17.
[93] McCulloch, Exh. No. MBM-1T at 15:3-6; *See also* Exh. No. MBM-1T at 16:7-17:15.
[94] O'Connell, Exh. No. ECO-HCT at 10:10-13; Cebulko, Exh. No. BTC-1HCT at 6:5-6.
[95] O'Connell, Exh. No. ECO-3HC at 3.
[96] *Id.* at 10.
[97] Englert, TR. at 426:3-427:5.

platform is to categorically expand the scope of regulated utility service in Washington to include an ever-expanding portfolio of rate base eligible items upon which the Company can earn a rate of return.[98] PSE seeks to expand regulated utility service to include the primary business of merchandising, and it intends to do so on an extensive scale, in violation of law.[99]

2. PSE's proposed service constitutes a sale

26 Under Washington law, public service companies are expressly forbidden from engaging in the sale of merchandise, appliances, and equipment as part of their regulated utility service.[100] Interpreting RCW 80.04.270, the Court, in *Cole*, held: (1) there is a well-recognized difference in meaning between the terms "sale" and "lease," (2) the jurisdictional exclusion relates only to sales, and (3) that absent proof of "incidents of sale in the agreement" the Commission could not be expected "to decide that a common lease falls within the purview of RCW 80.04.270."[101] Whether the proposed tariff constitutes a lease or a sale is a question of fact for the Commission to determine.[102]

27 To determine whether an instrument is a lease or a sales contract, courts look to the instrument to determine the parties' rights and intentions:

> The touchstone of contract interpretation is the parties' intent. In Washington, the intent of the parties to a particular agreement may be discovered not only from the actual language of the agreement but also from viewing the contract as a whole, the subject matter and objective of the contract, all the

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[98] O'Connell, Exhibit No. ECO-3HC at 3, 10.
[99] O'Connell, Exh. No. ECO-1HCT at 42:3; Cebulko, Exh. No BTC-2HC; *Cole v. Wash. Util. & Transp. Comm'n*, 79 Wn.2d 302, 307 (1971); RCW 80.04.270.
[100] RCW 80.04.270.
[101] *Cole v. Wash. Util. & Transp. Comm'n*, 79 Wn.2d 302, 307 (1971).
[102] RCW 80.04.015; See U.C.C. § 1-201(37) (1987) ("Whether a transaction creates a lease or security interest is determined by the facts of each case. . . ."); see also *Crest Inv. Trust, Inc. v. Atlantic Mobile Corp.*, 252 Md. 286, 289, 250 A.2d 246, 248 (1969) (facts are controlling to show parties' intent) (quoting *In re Alpha Creamery Co.*, 4 U.C.C. Rep. Serv. (Callaghan) 794, 797 (W.D. Mich. 1967)); *IFG Leasing Co. v. Schultz*, 217 Mont. 434, 436, 705 P.2d 576, 577 (1985) (facts of case determine character of transaction).

> circumstances surrounding the making of the contract, the subsequent acts and conduct of the parties to the contract, and the reasonableness of respective interpretations advocated by the parties. Contractual language also must be interpreted in light of existing statutes and rules of law.[103]

"A lease term spanning the effective useful life of the equipment is a sign that the parties intended a sale."[104] Courts are particularly likely to find a sale, or the equivalent of a sale, where the transferee has the option to purchase at the expiration of the lease for a small fraction of the anticipated purchase price or for a nominal price.[105]

28 Of note, the prevalence and sophistication of lease transactions are very different today than in 1968 when the Commission issued its Leasing Order and in 1971 when the Court affirmed that Order in *Cole*.[106] Those decisions both occurred prior to adoption of the State's Consumer Lease laws.[107] In enacting the Consumer Lease laws, the legislature declared: "The utility of lease transactions and the well-being of the state's economy and of the leasing industry require that leasing be a legally recognized and distinct form of transaction, creating legal relationships and having legal consequences different from loans

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[103] *Tanner Elec. v. Puget Sound*, 128 Wn.2d 656, 674, 911 P.2d 1301, 1310 (1996) (internal quotes and citations omitted); *See also Technicon Instruments Corp. v. Pease*, 829 S.W.2d 489, 491 (Mo. Ct. App. 1992) (*Citing Chase Third Century Leasing v. Williams*, 782 S.W.2d 408, 413 (Mo.App. 1989).

[104] *In re Pac. Exp., Inc.*, 780 F.2d 1482, 1485 (9th Cir. 1986) (*Citing In re Marhoefer Packing Co.*, 674 F.2d 1139, 1145 (7th Cir. 1982); *In re Peacock*, 6 B.R. 922, 926 (Bankr.N.D.Tex.1980); *In re Teel*, 9 B.R. 85, 88–89 (Bankr.N.D.Tex.1981).

[105] *Patel v. Telerent Leasing Corp.*, 574 So. 2d 3 (Miss. 1990); *Global Credit Services, Inc. v. AMISUB (Saint Joseph Hosp.), Inc.*, 244 Neb. 681, 508 N.W.2d 836 (1993); *Colonial Leasing Co. of New England, Inc. v. Larsen Bros. Const. Co.*, 731 P.2d 483, 3 U.C.C. Rep. Serv. 2d 24 (Utah 1986).

[106] *See* RCW 63.10.010.

[107] Chapter 63.10 RCW (enacted April 29, 1983) (Those decisions also both occurred prior: (1) to The Commission ordering PSE to include a purchase option to help address the many flaws in legacy rental program. *Wash. Util. & Transp. Comm'n v. Wash. Natural Gas Co.*, Fourth Supplemental Order Rejecting Tariff Filing, Authorizing Refiling, Docket No. UG-920840, at 17 (Sept. 27, 1993); (2) Statement of Financial Accounting Standards No. 13 Accounting for Leases issued by the Financial Accounting Standards Board in November 1976 issued accounting guidance for leasing; and more recently the Accounting Standard Codification Update on Leases Topic 842 (ASC Update) promulgated in February 2016 by the Financial Accounting Standards Board (FASB); (3) Article 2A, was added to the State's Uniform Commercial Code, which applies to any transaction, regardless of form, that creates a lease, which was added to the UCC in 1987, and adopted to Washington State's codification of the UCC in 1993 (*see* RCW 62A.2A-102, Notes).).

or installment sales."[108] Under state law, a "consumer lease" is a contract for the use of personal property for a total contractual obligation not exceeding twenty-five thousand dollars, whether or not the lessee has the option to purchase, *except* that such term shall not include any lease which meets the definition of a retail installment contract under RCW 63.14.010 or the definition of a lease-purchase agreement under chapter 63.19 RCW.[109] In contrast, a "retail installment contract" *is considered a sale that includes a contract in the form a lease* if the lessee (1) pays as compensation for their use a sum substantially equivalent to or in excess of the value of the goods sold, and (2) the lessee is bound to become, or for no other or a merely nominal consideration, has the option of becoming the owner of the goods upon full compliance with the provisions of the lease.[110]

29 Under Washington law, PSE's proposed tariff is a retail installment contract for sale of goods and services.[111] The proposed tariff triggers both prongs of a contract in the form a lease that nevertheless meets the definition of retail installment contract, and is thereby not a "consumer lease" under RCW 63.10.020(4). First, the proposed tariff would require a participating customer to pay "in excess of the value of the goods sold" because each category of equipment's rate is based on the estimated full cost of the equipment plus the Company's weighted cost of capital.[112] Second, the proposed tariff provides the participating customer an option to purchase, which the customer could exercise at the end of the lease for "no other or a merely nominal consideration" because the purchase price is based on the equipment's undepreciated value at the time of purchase and at the end of the lease that

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[108] RCW 63.10.010.
[109] RCW 63.10.020(4).
[110] RCW 63.14.010(11).
[111] *Id.*
[112] McCulloch, Exh. No. MBM-1T at 18:11-19.

value is zero.[113] Of note, the proposed tariff as originally filed included a Termination clause that provided for the bill of sale to pass to the customer at the end of the lease term.[114] The Company altered this provision, among many others, to no longer transfer title at the end of the lease term. The revised proposed tariff technically only allows customers to exercise the purchase option at "any time during the Lease Term." The Company confirmed customers would be able to exercise the purchase option up to the last day of the lease and that the purchase prices will be "very, very small" relative to the cost on the first day of the lease.[115] PSE's proposed tariff is thus a retail installment contract for the sale of goods and services, and does not constitute a consumer lease under Washington law.

30 Staff's review confirms that the proposed tariff constitutes a sale, and not a lease. Importantly, Staff found that PSE plans to use an inappropriate accounting method to track the expenses and revenues of its proposed service because PSE acting as a lessor requires the recognition of the value of the asset in its accounting records in a receivable account, as opposed to an electric or gas plant account.[116] Furthermore, Staff found the appliances themselves do not fit any description of utility property in electric or gas plant-in-service because the equipment would not be used for transmission or distribution operations.[117] Applying appropriate accounting guidelines reveals the true economic result of PSE's

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[113] Subst. Proposed Sched. 75, Sheet 75-R at § 5.9.b; McCulloch, TR. at 194:6-195:22; *see* O'Connell, Exh. No. ECO-5HC (Highly Confidential PSE Pricing Worksheet, Tabs 32, 33, 34, 35, 36, 38, 39, 40, 41, 42, 44, 45: cell E128).

[114] *See* Subst. Proposed Sched. 75, Sheet 75-U, at §5.12.a. ("This Agreement will automatically terminate at the end of the Lease Term. Upon expiration of the Lease Term, PSE will transfer ownership of the Equipment to Customer by delivery of a bill of sale for the Equipment. Customer shall be responsible for payment of all taxes associated with the transfer of the Equipment, including Washington state sale tax. If Customer does not wish to take possession of the Equipment, Customer may contract with PSE or its contractors to remove the Equipment for a removal fee and disposal costs.").

[115] McCulloch, TR. at 194:6-195:22.

[116] O'Connell, Exh. No. ECO-1HCT at 32:3-18; *see generally* O'Connell, Exh. No. ECO-1HCT at 32:3-45:5.

[117] O'Connell, Exh. No. ECO-1HCT at 32:3-18, 43:1-45:5.

proposed tariff: it is a sales-type lease—effectively a direct sale of the appliance to the customer through financing by PSE.[118]

3. PSE's proposed service is not a public service

31 The Commission "considers three factors to determine whether a company provides a utility service to the public: (1) whether the company offers the service to the general public or only to specific individuals or entities; (2) whether the company has a monopoly; and (3) whether regulation is necessary to protect customers from abuse by the Company's monopoly power."[119] The Commission has affirmed this test on at least three occasions, two of which involved PSE.[120] The test comes from Washington courts analyzing the public service requirement embedded in the public service laws.[121] This public service test is generally a factual determination, and in certain circumstances one factor should be given

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[118] *Id.* at 33:1-9.

[119] *In the Matter of Puget Sound Energy's Application for Approval of a Special Contract under WAC 480-80-143*, UG-160748, Order 01, ¶ 4 (July 7, 2016); *In re Amending and Repealing Rules in WAC 480-108 Relating to Electric Companies- Interconnection With Electric Generators*, Interpretive Statement Concerning Commission Jurisdiction and Regulation of Third-Party Owners of Net Metering Facilities, Docket UE-112133, ¶ 59 (July 30, 2014)); *See In re Matter if 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, Order 04, at ¶ 24. (Dec. 18, 2015).

[120] *In the Matter of Puget Sound Energy's Application for Approval of a Special Contract under WAC 480-80-143*, UG-160748, Order 01, ¶ 4 (July 7, 2016); *In re Amending and Repealing Rules in WAC 480-108 Relating to Electric Companies- Interconnection With Electric Generators*, Interpretive Statement Concerning Commission Jurisdiction and Regulation of Third-Party Owners of Net Metering Facilities, Docket UE-112133, ¶ 59 (July 30, 2014)); *see also In re Matter if 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, Order 04, at ¶ 24. (Dec. 18, 2015).

[121] *In re Amending and Repealing Rules in WAC 480-108 Relating to Electric Companies- Interconnection With Electric Generators*, Interpretive Statement Concerning Commission Jurisdiction and Regulation of Third-Party Owners of Net Metering Facilities, Docket UE-112133, ¶ 59 (July 30, 2014) (Citing *Inland Empire Rural Elec., Inc. v. Dept. of Pub. Serv.*, 199 Wash. 527, 537, 92 P.2d 258, 262 (1939) ("A corporation becomes a public service corporation, subject to regulation by the department of public service, only when, and to the extent that, its business is dedicated or devoted to a public use."); *United and Informed Citizen Advocates Network v. Util. and Trans. Comm'n*, 106 Wash. App. 605, 24 P.3d 471, (2001); *Clark v. Olson*, 177 Wash. 237, 31 P.2d 534 (1934); *State ex rel. Stimson v. Kuykendall*, 137 Wash. 602, 243 P. 834 (1926)).

more weight than in others.[122] Therefore, each determination requires an investigation by the Commission and a detailed examination of the particular facts of the case.[123] Here, an analysis of all three factors demonstrates that PSE's proposed service is both ill-conceived and not a regulated utility service as a matter of law.

a. PSE's proposed service is dedicated to private, not public, use

32 The first prong of the Commission's public service test evaluates whether the business activity is dedicated to a public use. In *Clark v. Olson*, the Washington Supreme Court held that the standard for dedication to the public use requires "unequivocal intention," whether express or implied, to hold oneself out to serve the public.[124] Here, PSE's intention to dedicate the proposed service to a public use, however, is equivocal because it limits the availability of its proposed service in several significant ways. First, PSE would limit the proposed service to customers that own the premises where the equipment would be installed.[125] Second, PSE would limit the proposed service to customers that meet its credit approval requirements,[126] which the Company may change on a whim.[127] Third, PSE would maintain sole discretion to restrict where in its service territory it offers the proposed service.[128] Finally, PSE could terminate the contract at any time on 30 days'

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[122] *In re Amending and Repealing Rules in WAC 480-108 Relating to Electric Companies- Interconnection With Electric Generators, Interpretive Statement Concerning Commission Jurisdiction and Regulation of Third-Party Owners of Net Metering Facilities*, Docket UE-112133, ¶ 63 (July 30, 2014) (Citing *SZ Enterprises, LLC v. Iowa Util. Bd.*, 850 N.W.2d 441 (Iowa July 11, 2014).

[123] *Inland Empire Rural Elec., Inc. v. Dept. of Pub. Serv.*, 199 Wash. 527, 538, 92 P.2d 258, 263 (1939) ("The question of the character of a corporation is one of fact to be determined by the evidence disclosed by the record.").

[124] *Clark v. Olson*, 177 Wash. 237, 243 (1934).

[125] Proposed Sched. 75, Sheet 75-G at 5. Lease Terms and Conditions § 4(a).

[126] Proposed Sched. 75, Sheet 75 at § 1.4; Kimball, Exh. No. MMK-1HCT at 10:17-18.

[127] *See* Dockets UE-151871 & UG-151872, *Staff Response to PSE Response to Bench Request 1*, from Sally Brown (Aug. 10, 2016); Dockets UE-151871 & UG-151872, *Response to Puget Sound Energy's Response to Request No. 1 and Motion to Strike on Behalf of Public Counsel*, (Aug. 15, 2016).

[128] Proposed Sched. 75, Sheet 75 at § 1.2.

notice.[129] PSE intentionally designed the proposed service's tariff to provide the Company significant flexibility.[130] PSE could use that flexibility to materially limit the proposed service's availability to the public.

33 Moreover, PSE wishes to offer the proposed service as an optional service that is not accountable to any long-standing regulatory tenets. PSE invariably testifies that the proposed service is not subject to: traditional ratemaking principles;[131] a cost-benefit analysis conducted by anyone other than individual customers;[132] the Energy Independence Act or the requirement that qualifying utilities "pursue all available conservation that is cost-effective, reliable, and feasible;"[133] a service demarcation of the customer meter;[134] or any limitation of the jurisdictional bounds of regulated utility service.[135] PSE seeks the privileges and protections of regulation, but does not want the optional service to be accountable for comporting with long-standing regulatory principles. Instead, it wants the service to compete in the open market, where it will have competitive advantages that unregulated entities do not.

b. PSE does not have a monopoly over equipment markets, but it would be able to leverage its monopoly position over retail energy service to its competitive advantage in those markets

34 As the Commission has found: "The theoretical underpinning of utility regulation is that the regulated company is a natural monopoly, and it is more efficient for a monopoly to

[129] Subst. Proposed Sched. 75, Sheet 75-U at § 12.b.
[130] Englert, TR. at 404:12-405:13.
[131] Norton, Exh. No. LYN-1T at 6:13-16.
[132] Teller, Exh. No. JET-1T at 6:7-17.
[133] Englert, Exh. No. EEE-3T at 26:14-28:9; *See* RCW 19.285.040(1).
[134] Englert, Exh. No. EEE-3T at 24:4-5.
[135] Englert, TR. 402:2-6; *See* Englert, TR. 399:7-402:6.

provide the service than the competitive market. In the absence of robust competition to ensure fair rates, we are more likely to find that the service is a public one."[136]

35 PSE seeks to expand its business to services that are not a natural monopoly. The HVAC and water heat markets would not gain efficiencies and produce greater public benefit through one company's exclusive provision of products and services. In fact, PSE is not asking to replace the competitive market with its proposed service. Rather, the proposed service would be an optional, regulated, tariff-based service that awkwardly interacts with, and competes for customers within, a broader, existing, robust competitive market.

36 PSE's claims that customers are interested in the proposed service and that the service is "specifically tailored"[137] to address some market gap are both disingenuous and not supported by credible evidence. As explained in detail below, the Company's claim that customers are interested in the proposed service is invalid because they rely on a fundamentally flawed Cocker Fennessy survey. The Cocker Fennessy survey is wholly invalid because of the bias presented in its creation, PSE's complete failure to produce a credible witness or evidence demonstrating the survey was designed using a proper methodology, and the survey's failure to disclose critical information to participants.[138]

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[136] *In re Amending and Repealing Rules in WAC 480-108 Relating to Electric Companies- Interconnection With Electric Generators*, Interpretive Statement Concerning Commission Jurisdiction and Regulation of Third-Party Owners of Net Metering Facilities, Docket UE-112133, ¶ 63 (July 30, 2014) (*See Munn v. Illinois*, 94 U.S. 113, 151-52 (1876); *State ex rel. Stimson v. Kuykendall*, 137 Wash. at 609, 243 P. at 836.); see also *Tanner Elec. v. Puget Sound*, 128 Wn.2d 656, 666, 911 P.2d 1301, 1306 (1996) ("In return for their monopoly status, public utilities are regulated by the State through the WUTC." Referring to *Jewell v. Wash. Utils. & Transp. Comm'n*, 90 Wn.2d 775, 776, 585 P.2d 1167 (1978)); see also RCW 54.48.020.

[137] *See* Dockets UE-151871 & UG-151872, *PSE Reply to Public Counsel's Response in Support of Commission Staff's Motion for Summary Determination*, at ¶ 7 (July 29, 2016).

[138] *See* Section III.A.2 below.

37 The alleged market gap is not credible because PSE made a calculation error using outdated and questionably relevant data that dramatically skewed its results.[139] Furthermore, a host of products and services already addresses the alleged gap. As the Company acknowledges, [redacted].[140] Staff also notes, "similar appliances, installation, maintenance and repair services, and long-term financing options are all available through numerous competitive retail providers, financial institutions, and service contractors."[141] These similar competitive services are generally more flexible and less expensive than PSE's proposed service.[142] In truth, the only unique aspect of the proposed service is that the Company can bundle it with its retail energy service and provide on-bill payment given its monopoly position in that market.[143]

38 Furthermore, the proposed service is in no way "tailored" to address the alleged market gap. PSE does not testify that it would offer the service only to customers who fall within the "gap," nor does the tariff limit the service in such a manner. Instead, PSE intends to monopolize the market,[144] while maintaining the flexibility to restrict the service offering at its sole discretion. Moreover, as discussed above, the proposed service lacks any credible public purpose connection to the Company's principle regulated service because PSE intentionally designed the service to be distinct from its sale of energy. Again, the proposed service would be an optional, regulated, tariff-based service that awkwardly interacts with, and competes for customers within, a broader, existing, robust competitive market.

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[139] *See* Teller, Exh. No. JET-3 (add up numbers in each percentage column for vintages 1966-1995); Norton, TR. 221:25-230:23 (This is addressed in greater detail in Section III.A.1. below.).
[140] O'Connell, Exh. No. ECO-3HC at 8.
[141] Cebulko, Exh. No. BTC-1HCT at 7:18-20; Exh. No. BTC-6.
[142] O'Connell, Exh. No. ECO-1HCT at 42:7-46:7; Kimball, Exh. No. MMK-1HCT at 25:5-29:16.
[143] Cebulko, Exh. No. BTC-1HCT at 7:20-22.
[144] Cebulko, Exh. No. BTC-2HC.

39 Importantly, PSE could leverage its monopoly position over retail energy service to its competitive advantage in HVAC and water heat markets despite its lack of monopoly status in those markets. PSE enjoys certain privileges as a regulated utility that unregulated entities do not. PSE's code of ethics expressly acknowledges this fact as well as the Commission's role of providing a system of checks and balances to counter the effect of those privileges.[145] Courts around the country recognize the problem faced when a regulated utility conducts business activities in both a regulated and unregulated market:

> We recognize that a special problem is posed by a monopolist, regulated at only one level, who seeks to dominate a second, unregulated level, in order to earn at that second level the very profits that regulation forbids at the first.[146]

Other utility commissions similarly recognize the competitive advantage regulated utilities possess when they venture into unregulated markets:

> By the very nature of [the regulated utility's] monopoly position in the energy and energy services market, its access to comprehensive customer records, its access to an established billing system, and its 'name brand' recognition, it may be that [the regulated utility] enjoys significant market power with respect to any new product or service in the energy field.[147]

40 Moreover, PSE has expressly and impliedly demonstrated its intent to leverage its monopoly position over retail energy service to its competitive advantage in a number of ways. First, PSE intends to capitalize on its name-brand recognition by selling the proposed service on the basis of its "trusted relationship" with its customers.[148] According to the Company, customers will replace their old, inefficient equipment sooner as a result of

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[145] McCulloch, Exh. No. MBM-37 at 6.
[146] *Concord v. Bos. Edison Co.*, 915 F.2d 17, 29 (1st Cir. 1990); *See Olympia Equipment Leasing Co. v. Western Union Tel. Co.*, 797 F.2d 370 (1986).
[147] *Order Instituting Rulemaking to Establish Standards of Conduct Governing Relationships Between Energy Utilities and Their Affiliates*, 183 P.U.R.4th 503, 1997 Cal. PUC LEXIS 1139, at 79 (Cal. P.U.C. Dec. 16, 1997).
[148] Teller, Exh. No. JET-1T at 2:21-3:3; McCulloch, Exh. No. MBM-1T at 8:2-5; Wigen, Exh. No. AJW-1T at 5:16-18.

Company encouragement because customers view PSE as a trusted energy partner.[149] Indeed, the Company claims the ease and convenience of working with a "trusted energy partner" when making difficult energy decisions is a primary benefit of the proposed service.[150] PSE, however, did not win the hearts and minds of its captive energy service customers of its own volition. Rather, "Regulators provide customers with confidence"[151] by providing a system of checks and balances to counter the effect of the Company's monopoly power.[152] Indeed, customers would rightly perceive Commission approval of the proposed service as an endorsement of the rates and assurance of robust consumer protection.[153]

41 Second, PSE intends to tie the proposed service to its principle regulated service—the sale of energy—to provide customers with the ease and convenience of on-bill repayment. As noted, the only unique aspect of the proposed service is on-bill repayment, which PSE exclusively can provide given its de facto monopoly over the provision of retail energy in its service territory.[154]

42 Third, PSE intends to use its access to capital and inexpensive debt as a regulated entity to finance and merchandise equipment.[155] PSE believes it can [redacted],[156] which would yield higher returns because the cost of debt is generally less than the cost of capital.

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[149] Teller, Exh. No. JET-1T at 2:8-23.
[150] *Id.* at 2:21-3:3, 5:7-8.
[151] Norton, Exh. No. LYN-1T at 4:17.
[152] *See* Cebulko, Exh. No. BTC-1HCT at 4:8-16, 29:11-21; McCulloch, Exh. No. MBM-37 at 6.
[153] Cebulko, Exh. No. BTC-1HCT at 4:1-16, 29:16-18.
[154] *Id.* at 7:20-22.
[155] O'Connell, Exh. No. ECO-1HCT at 9:3-5, 10:11-13, 42:3.
[156] McCulloch, Exh. No. MBM-62HC at 2; McCulloch, TR. 290:23-291-7.

43 Fourth, PSE used its monopoly position over retail energy service to solicit critical market information from would-be competitors.[157] It then used this information to develop rates for the proposed service.[158]

44 And fifth, PSE intends to leverage its access to comprehensive customer records for marketing purposes. Specifically, [redacted][160] PSE's monopoly position over retail energy service provides significant market power with respect to the proposed service as well as any new product or service potentially offered through the leasing platform. PSE seeks to use its competitive advantage to merchandise equipment an extensive scale.[161]

c. Regulation would be necessary to protect customers in equipment markets from abuse by PSE's monopoly power only if the Company participates in those markets as a regulated entity

45 Commission regulation is not necessary to protect customers from abuse in the HVAC and water heat markets. No party has argued or presented evidence to the contrary. However, if PSE participates in this market *as a regulated entity*, then all market oversight and consumer protection responsibility would reside with the Commission. Currently,

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[157] McCulloch, Exh. No. MBM-8HC.
[158] McCulloch, Exh. No. MBM-1T at 17:16-23.
[159] O'Connell, Exh. No. ECO-3HC at 13.
[160] *Id.* at 10 (emphasis added).
[161] O'Connell, Exh. No. ECO-1HCT at 42:3; Cebulko, Exh. No BTC-2HC; *Cole v. Wash. Util. & Transp. Comm'n*, 79 Wn.2d 302, 307 (1971).

customers are protected from abuse in equipment markets through effective competition. In Washington State, the Consumer Protection Act, RCW 19.86 ("CPA") complements the federal antitrust laws in order to protect the public and foster fair and honest competition.[162] The Legislature enacted the CPA to "promote free competition in the marketplace for the ultimate benefit of the consumer."[163] The CPA, however, "exempts public utilities from the sphere of free competition, *and in fact discourages it*."[164] Specifically, the CPA exempts "actions or transactions otherwise permitted, prohibited or regulated under laws administered by . . . the [Commission]."[165] Indeed:

> By statutory authority, regulatory agencies may approve anticompetitive acts and practices which would, unless so immunized by agency action, violate the antitrust laws. . . . An exemption for public utilities pursuant to the express exemption accorded WUTC transactions makes sense given the need for regulated monopoly *in the power industry*.[166]

The Legislature decided that the public interest is best served by the Commission's "direct and uniform regulation of almost every phase of industry activity."[167] As a result, "once [the Commission] has acted on a matter over which it has authority, jurisdiction of the courts based on the [CPA] is ousted."[168] Therefore, if the Commission approves the proposed service, all remedies for egregious conduct become the responsibility of the Commission.[169] Critically, the exemption from the CPA—and thus the Commission's market and consumer

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[162] RCW 19.86.920.
[163] *Tanner Elec. v. Puget Sound*, 128 Wn.2d 656, 684, 911 P.2d 1301, 1315 (1996) (citing *State v. Black*, 100 Wn.2d 793, 799, 676 P.2d 963 (1984); *Ballo v. James S. Black Co.*, 39 Wash. App. 21, 25, 692 P.2d 182 (1984)).
[164] *Id.* at 684 (emphasis added).
[165] *Id.* at 680; RCW 19.86.170.
[166] *Id.* at 682, (emphasis added).
[167] *Id.* at 682-83.
[168] *Id.* at 682.
[169] *Id.* at 684.

protection oversight responsibilities—matches the scope of the Commission's jurisdictional authority.[170]

46 Of note, the CPA's exemption for public utilities is "broader than any exemption from federal antitrust laws granted by a federal agency."[171] Under federal antitrust laws, the conduct of regulated utilities is most commonly exempt if subject to the state action doctrine. The state action doctrine applies if: (1) there is a clearly articulated regulatory policy under state law that leads to an inconsistency with the antitrust law as applied to the situation; and (2) there is active, significant state supervision over the conduct that is involved in the alleged antitrust violation.[172] Courts have struggled with whether a broad delegation of authority to regulated utilities, such as most states grant to their public utility commissions, is sufficient to immunize anticompetitive conduct by utilities in competitive markets. [173] "[Several cases] suggest that immunity can be granted pursuant to a broad delegation of authority, while [other cases] suggest that a more specific grant will be required."[174] Importantly, "The most difficult state action immunity issues are those that arise when a utility obtains regulatory approval for a program that appears to fall clearly outside the monopoly franchise."[175] Consequently, if the Commission were to approve the proposed service, it would need to clearly articulate both the scope of its jurisdictional authority and its rationale for why the particular service falls within that authority. Failure to

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[170] *Id.* at 680; RCW 19.86.170.
[171] *Tanner*, 128 Wn.2d at 682.
[172] *California Retail Liquor Dealers Association v. Midcal Aluminum, Inc.*, 445 U.S. 97 (1980); *Parker v. Brown*, 317 U.S. 341 (1943).
[173] John T. Nimmons, Legal, Regulatory & Institutional Issues Facing Distributed Resource Development, at 42 (1996) (copy available in WUTC library and at http://www.nrel.gov/docs/legosti/old/21791.pdf).
[174] *Id.*; *Compare: Grason Electric Co. v. Sacramento Municipal Utility District*, 770 F.2d 833 (9th Cir. 1985); *Lease Lights, Inc. v. Public Service Company of Oklahoma*, 849 F.2d 1330 (10th Cir. 1988); *Cantor v. Detroit Edison Co.* 428 U.S. 579 (1987); *Nugget Hydroelectric, L.P. v. Pacific Gas & Electric Co.*, 981 F.2d 429 (9th Cir. 1992); *Transphase Systems, Inc. v. Southern California Edison Co.*, 839 F. Supp. 711 (C.D. Cal. 1993).
[175] John T. Nimmons, Legal, Regulatory & Institutional Issues Facing Distributed Resource Development, at 43.

do so could leave PSE, and ultimately the Company's customers, open to significant antitrust liability.

47 Importantly, PSE's proposed service raises numerous consumer protection issues. As discussed at length below, the proposed tariff contains a number of grossly unfair terms. In addition, some aspects of the program—like advertising, non-standard installations, and the Company's selection of equipment for individual customers—would be exceedingly difficult for Staff to supervise.[176] The proposed service also does not adequately align the Company's financial interests with those of its participating customers, which raises the potential for the Company to take advantage of its position as a "trusted energy advisor." For example, a financial incentive could exist for PSE or its service partners to secure new customers by promising unrealistic energy bill savings, to run-up the cost of non-standard installations, or to install equipment that is not appropriate for the customer's need because doing so provides a higher profit margin (e.g., installing 2.0 ton, rather than 3.0 ton, capacity heat pumps). These are all "unfair or deceptive acts or practices in the conduct of any trade or commerce" that the CPA expressly prohibits,[177] but neither the proposed tariff nor Commission rules adequately addresses. While the Commission has rulemaking authority to proactively prevent harm to customers, doing so requires a lengthy rulemaking process. Until the Commission has such protections in place, customers remain vulnerable to unfair or deceptive practices. Importantly, remedy harm to customers post hoc, especially if the harm resulted from conduct permitted by an approved tariff, could prove difficult.

48 Staff raises these issues not to accuse or even imply the Company's bad faith, but rather to highlight the significant issues that could result from the proposed service. As PSE

[176] Roberts, Exh. No. AR-1T at 10:7-13.
[177] RCW 19.86.020.

noted at hearing, the Company does not intend to take advantage of customers, but the Company is also not accountable for its intentions.[178] Ultimately, the public service laws, Commission rules, orders, and tariff provisions articulate the minimum standards applicable to PSE as well as the full scope of the Company's commitments and obligations under law.

4. The Commission should adopt Staff's common sense general principle to clarify the jurisdictional bounds of regulated utility service

49 The Commission should affirm, as a general principle, that regulated utility service ends at the customer meter unless the overreaching service is narrowly tailored to provide compelling net-benefits to all customers or otherwise fulfills some statutory purpose articulated in the public service laws.[179] As the ultimate delivery point for the sale of energy, the utility meter provides an intuitive and practical demarcation for where regulated utility service ends and unregulated, competitive market services begin.[180]

50 Staff's general principle is fully consistent with legal precedent as well as PSE's past and present optional services. As the Commission found, and the Supreme Court affirmed, the Commission is empowered to regulate rates—including rental charges—for "any service rendered *in connection with* gas [or electricity] sales;" and further that promotional practices narrowly tailored to increase energy sales and improve system load factor were a legitimate utility function because they provided compelling benefits to all customers.[181] Further establishing the importance of a purposeful connection between rental service and the sale of energy, the Commission found that it was both illogical and inconsistent to the established

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[178] Compare McCulloch, TR. 353:12-354:17; Englert, TR. 405:1-409:9.
[179] Cebulko, Exh. No. BTC-1THC at 10:1-13.
[180] *Id.* at 10:11-13.
[181] *Cole v. Wash. Natural Gas Co.*, U-9621 (1968) at 20 (emphasis added), 17-31.

regulatory view to separate the promotional service from the Company's principle regulated service.[182]

51 Similarly, Staff's general principle allows regulated utility service to extend beyond the customer meter if the overreaching service is narrowly tailored to provide compelling net-benefits to all customers. Staff's principle would also encompass PSE's current optional services because there is a limited supply and demand for substation rentals and area lighting services, PSE is uniquely positioned to provide these services, and the equipment is all located on the Company's side of the meter.[183] Staff's general principle would further encompass legislative directives such as those related to electric vehicle equipment[184] and compressed natural gas[185] because it allows for overreaching services that fulfill some statutory purpose articulated in the public service laws.

52 Finally, Staff's recommended general principle is sufficiently flexible to allow the scope of regulated utility service to evolve over time. Staff does not recommend that the Commission limit future regulated services that extend beyond the meter to *only* promotional programs, or conservation, or demand response, or any other single category. Rather, Staff maintains that public service companies should provide a public service—that is, the service should be narrowly tailored to deliver net-benefits to all customers. Said differently, narrowly tailoring a service on the customer-side of the meter to provide

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[182] *Id.* at 37 (emphasis added) (*citing* New York Public Service Commission, April 25, 1967, *Promotional Activities by Gas and Electric Corporations in New York State*, 68 P.U.R. 3d 162, at page 169; Connecticut Public Utilities Commission, November 10, 1966: *Re Promotional Practices of Electric and Gas Utilities*, 65 P.U.R. 3d 405; Maine Public Utilities Commission, June 10, 1965: *Kenneth R. Gifford, et al. v. Central Maine Power Company*, 63 P.U.R. 3d 205, affirmed by Supreme Court of Maine at 63 P.U.R. 3d 208, 212 (1966); New Jersey Superior Court Appellate Division, sustaining promotional program carried on by the City of Vineland, *George A. Rossi, et al. v Henry A. Garton, Jr., Mayor*, 88 N.J. Super. 233, 211 Atl. 2d 806, 60 P.U.R. 3d 210 (1965)).

[183] Cebulko, Exh. No. BTC-1HCT at 19:2-20:3.

[184] RCW 80.28.360.

[185] RCW 80.28.280; .290.

compelling net-benefits to all customers is necessary for the overreaching service to be "rendered in connection with the sale of energy." Further, the net-benefits offered by the overreaching service should be sufficiently compelling to justify expanding the scope of regulated utility service in the new or unique manner proposed. The general principle in no way limits the Commission's ability to evaluate filings on a case by case basis. If the Commission were to adopt Staff's recommendation, but later found the general principle no longer apt, it could always amend the principle at that time. PSE has proven that it would benefit from Commission guidance. Establishing Staff's recommended general principle would be helpful start.

III. PSE FAILED TO MEET THE MOST BASIC REQUIREMENTS FOR ESTABLISHING A NEW REGULATED UTILITY SERVICE

53 PSE failed to present sufficient evidence to establish its proposed service meets the minimum standards required by the public service laws. The filing is based on two fundamentally flawed surveys that deserve no evidentiary weight. The two surveys infect the Company's presentation of both the costs and benefits of the proposed service. Moreover, the Company's proposed rates are not fair, just, or reasonable; they are plagued by cost uncertainty and were developed in a manner that will result in undue discrimination to similarly situated customers. Finally, PSE's proposed tariff creates numerous consumer protection concerns. The Commission should reject the Company's alarmingly deficient proposal.

A. PSE's Filing Lacks Credible Evidence to Demonstrate the Proposed Service is in the Public Interest

1. PSE failed to establish a "market gap"

54 PSE's evidence in support of a "market gap" is not credible. The Company offered a 2012 Regional Building Stock Assessment by the Northwest Energy Efficiency Alliance (NEEA) (the NEEA survey) as evidence of a market gap. Specifically, the Company claimed that the NEEA survey "revealed that approximately 40 percent of [HVAC and water heat] products in service today have exceeded their useful life."[186] The Company further claimed it could successfully fill this gap by encouraging customers to replace their old, inefficient equipment because customers view PSE as a trusted energy partner.[187] The NEEA survey, however, does not demonstrate a market gap of 40 percent. PSE's numbers simply do not add up.

55 PSE miscalculated its alleged market gap by including the wrong date range in its calculation. The data used in the NEEA survey was from 2011, not from 2016. Therefore, when PSE calculated the percentage of equipment that was beyond 15 years old—which is the Company's estimate of the equipment's average useful life—it should have included only equipment vintages from 1996 or earlier. Instead, PSE included vintages up to the year 2000, which had the effect of heavily skewing the results. Properly calculated, PSE's "market gap" is approximately *half* of what the Company claimed.[188]

56 PSE's gross overstatement of the market gap also does not account for the other problems with the Company's use of the NEEA survey. For example, PSE estimated that

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[186] Teller, Exh. No. JET-1T at 7:8-12; Exh. No. JET-3.
[187] Teller, Exh. No. JET-1T at 2:8-23.
[188] *See* Teller, Exh. No. JET-3 (add up numbers in each percentage column for vintages 1966-1995).

each product had a "useful life" of 15 years, but that number is merely an average of estimates that may not accurately reflect the true useful life of the products in people's homes and businesses. [189] In addition, the NEEA survey occurred shortly after the "Great Recession," which according to NEEA, "pared back water heater sales and made customers more skittish about major purchases."[190] Given the economic recovery that has since occurred, it is questionable whether the data from the NEEA survey remains relevant today or if it will hold for the foreseeable future.

57 PSE's refusal to acknowledge the effect of its calculation error should give the Commission pause. At hearing, Ms. Norton admitted that NEEA conducted its survey over four years ago.[191] She also admitted that the survey consisted of a single snapshot in time and that it essentially extrapolated the current percentage of equipment that has exceeded its useful life by freezing that snapshot.[192] Ms. Norton later admitted that freezing the snapshot in time resulted in incorrect numbers.[193] Nevertheless, Ms. Norton steadfastly testified that the market gap remained 40 percent: "We are using 40 percent as our statement of the market gap. Our projections to the Company are relative to what we expect from that gap."[194] Similarly, Mr. McCulloch testified, "we believe that the 40 percent accurately represents what is the potential unmet need in the market today."[195] PSE's testimony at hearing about the NEEA survey casts serious doubt about the credibility of its witnesses and

[189] *See* O'Connell, Exh. No. ECO-20; Norton, TR. 176:21-177:2.
[190] Kimball, Exh. No. MMK-3 at 5.
[191] Norton, TR. 142:9-11.
[192] Norton, TR. 142-:14-17.
[193] *Id.* 136:20-23, 144:7-12.
[194] *Id.* 145:18-20.
[195] McCulloch, TR. 268:17-19.

their use of data, as well as the Company's ability to serve in the role as a "trusted energy advisor."

2. PSE failed to establish customer interest in the proposed service

58 The Commission should accord PSE's claims of customer interest no evidentiary weight.[196] PSE relies on a flawed survey conducted by Cocker Fennessy to demonstrate customer interest in the proposed service.[197] The Cocker Fennessy survey is wholly irrelevant for three reasons. First, the survey is fundamentally flawed due to biases presented in its creation. PSE commissioned the survey for the purpose of this litigation more than a month after the Commission suspended the proposed tariff and set the matter for hearing.[198] Despite testifying that "one of the reasons PSE asked Cocker Fennessy to conduct the survey was so the survey process was *entirely removed* from PSE,"[199] PSE employees provided survey inputs to Cocker Fennessy and reviewed several drafts of the survey.[200] Federal courts have excluded as untrustworthy, survey evidence offered by a party who had the opportunity to shape the survey in accordance with its litigation needs.[201] The worries about the reliability of survey results shaped by litigation needs apply equally here: PSE commissioned this survey after this litigation began, and had extensive involvement with the design of the survey.

59 Second, PSE failed to produce any testimony or evidence stating that Cocker Fennessy designed the survey using proper methodology or followed that methodology

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[196] Cebulko, Exh. No. BTC-1HCT at 32:20-33:6.
[197] *Id.* at 32:20-33:6; *see* McCulloch, Exh. No. MBM-4.
[198] Cebulko, Exh. No. BTC-1HCT at 32:20-33:1.
[199] McCulloch, Exh. No. MBM-7HCT at 26:9-10 (emphasis added).
[200] Norton, Exh. No. LYN-4.
[201] *See e.g., U.S. v. S. Ind. Gas & Elec. Co.*, 258 F.Supp.2d 884, 894-95 (S.D. Ind. Apr. 11, 2003).

when performing the study. The only evidence Cocker Fennessy provides about its methodology comes from: (1) a letter describing the survey using two bullet points,[202] and (2) two short paragraphs devoid of substance that preface the summary of survey results.[203] Nothing documented by Cocker Fennessy describes controls that would ensure a proper methodology was used or followed. Whether or not Cocker Fennessy is capable of producing a methodologically sound survey does not mean that *this survey* was designed in such a manner. The fact that no witness from Cocker Fennessy testified in support of the survey, or authenticated it in any manner, raises legitimate concern about the survey's credibility, especially in light of the fact that it was created for the purpose of *this litigation*.[204] Without a proper evidentiary foundation, the Commission cannot know whether to assign the survey any weight. In the absence of such evidence, the Commission should give it no weight at all.

60 Third, Cocker Fennessy's failure to provide necessary information to survey participants renders the survey results meaningless. Customers could only truly evaluate whether they would use PSE's leasing service by comparing the service to other options, such as purchasing equipment outright.[205] Cocker Fennessy did not provide to survey participants information necessary make to that comparison.[206] Cocker Fennessy incorrectly informed the customers surveyed that the monthly tariff charge would be similar to the cost of purchasing, installing, maintaining, and disposing of equipment.[207] It also failed to

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[202] McCulloch, Exh. No. MBM-43 at 3.
[203] McCulloch, Exh. No. MBM-4 at 1.
[204] *See* Cebulko, Exh. No. BTC-1HCT at 32:20-33:6; McCulloch, Exh. No. MBM-43 at 3-4.
[205] Cebulko, Exh. No. BTC-1HCT at 33:5-34:9.
[206] *See Id.* at 34:5-9; Fluetsch, Exh. No. BF-1T at 15:14-17.
[207] Fleutsch, Exh. No. BF-1T at 19:11-21:22.

provide survey participants with the total lifetime cost of the lease, the interest rate involved, and exit terms.[208] If given accurate information about the significantly higher cost of leasing, simple economics dictate that customers' interest in participating in the proposed service decline.[209] Taken together, these glaring evidentiary defects render the study irrelevant.

3. PSE failed to demonstrate the proposed service is cost effective

61 PSE used the results of the invalid Cocker Fennessy survey to develop its rates[210] and to forecast benefits.[211] Because the Cocker Fennessy survey is fundamentally flawed for multiple reasons, so too are the Company's proposed rates and benefit forecast. Moreover, PSE used the invalid survey inconsistently to develop the proposed rates and the benefit forecast. For its rates, PSE used the invalid survey to estimate the addressable lease market; it assumed the percentage of respondents interested in each of the products categories equaled the total addressable market, and further assumed 50 percent of that total addressable market would participate in the proposed service.[212] For its benefits, however, PSE assumed the entire addressable market would participate in the proposed service.[213] Ultimately, PSE's flawed Cocker Fennessy survey infects both its proposed rates and its forecast of benefits, rendering them inaccurate and invalid.

62 PSE further failed to show that Commission approval is reasonable based on a costs-benefits comparison.[214] Even if the proposed service would produce some gains in

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[208] Cebulko, Exh. No. BTC-1HCT at 34:6-7; Kimble, Exh. No. MMK-1HCT at 16:14-23:24.
[209] Fleutsch, Exh. No. BF-1T at 19:11-13.
[210] McCulloch, Exh. No. MBM-7HCT at 33:4-12; O'Connell, Exh. No. ECO-5HC [redacted]).
[211] Cebulko, Exh. No. BTC-1HCT at 32:20-33:6; Faruqui, Exh. No. AF-1T at 16:6-18:2.
[212] McCulloch, Exh. No. MBM-7HCT at 33:4-12
[213] Faruqui, Exh. No. AF-1T at 16:6-18:2, 22:10-13.
[214] *See* Cebulko, Exh. No. BTC-1HCT at 20:10-15 (Commission evaluates whether or not to adopt a program by looking at costs and benefits).

efficiency, the Company is obligated to pursue those gains cost-effectively.[215] PSE refuses to produce a cost-benefit analysis to demonstrate that any efficiency gains produced by the service exceed their production costs.[216] Thus, the Company has failed to demonstrate that the proposed service complies with state law or is cost-effective for participating customers, making its adoption by the Commission unreasonable.

B. PSE's Proposed Rates are Not Fair, Just, or Reasonable

63 Tariffed rates for utility service must be "fair, just, reasonable, and sufficient."[217] Tariffed rates must also not unduly or unreasonably prefer or prejudice certain customers over other similarly situated customers.[218] The public service company carries the burden of proof to show that its proposed rates are just and reasonable.[219] PSE failed to carry its minimum burden of proof in these dockets.

64 PSE's proposed rates contain speculative costs "divorced" from the actual costs of the products and services that customers would receive.[220] As PSE testified: "[Its] rates are built on *estimates of all costs* borne by the Company in installing, operating and maintaining the equipment over the life of the lease term [10-18 years]."[221] While PSE has identified some common types of equipment and technical specifications, it has not yet selected any of the specific equipment (makes or models) that it would actually offer.[222] The Company

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[215] RCW 19.285.040(1).
[216] Cebulko, Exh. No. BTC-1HCT at 34:12-15.
[217] RCW 80.28.010(1); *See Wash. Utils. & Transp. Comm'n v. PacifiCorp d/b/a Pac. Power & Light Co.*, Docket No. UE-100749, Order 06, 287 P.U.R. 4th 333, 344 (2011) (citing *Fed. Power Comm'n. v. Hope Nat. Gas*, 320 U.S. 591 (1944); *Bluefield Water Works & Improvement Co. v. Pub. Serv. Comm'n of W. Va.*, 262 U.S. 679 (1923)).
[218] RCW 80.28.090.
[219] RCW 80.04.130(4).
[220] O'Connell, Exh. No. ECO-1HCT at 21:1-3.
[221] McCulloch, Exh. No. MBM-1T at 18:12-14 (emphasis added).
[222] McCulloch, Exh. No. MBM-7T at 7:8-12.

plans to select specific equipment *only after* the Commission approves the proposed tariffs.[223] As PSE has not even identified the specific equipment it will install, much less purchased any goods or services for the leasing program,[224] "[n]o costs included in PSE's proposed rates are known and measurable by even a liberal interpretation of the intent of the standard."[225] Compounding the inherently uncertain nature of its costs is that the Company would record in its books "the actual original costs of the assets," rather than the cost estimates embedded in the rates.[226] This critical defect ensures the proposed rates are not just or reasonable.

C. PSE's Proposed Rates are Discriminatory

65 In addition, PSE's proposed rates are unduly and unreasonably discriminatory. PSE's cost estimates include equipment costs developed by averaging sample costs obtained from multiple contractors in response to the Request for Qualifications that the Company used to gather information on market conditions.[227] Specifically, PSE calculated the proposed rates by averaging the sample cost it received from the contractors for the various products and services it would offer;[228] it then averaged again those average costs for groups of like products;[229] and then converted that group average cost into a monthly tariff rate using its approved cost of capital.[230] The Company also undertook a similar averaging exercise to

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[223] *Id.* at 8:13-15; *see* Norton, Exh. No. LYN-1T at 9:1-3.
[224] *See Utils. & Transp. Comm'n v. Avista*, Docket No. UG-060518, Order 10, 279 P.U.R. 4th 77, 91 (2009) ("[t]o be approved, a pro forma adjustment to test year operations must comport with the three key principles expressed above," one of which is the known and measurable standard").
[225] O'Connell, Exh. No. ECO-1THC at 16:6-8.
[226] Marcelia, Exh. No. MRM-1T at 15:7-8.
[227] McCulloch, Exh. No. MBM-7T at 18:7-9; McCulloch, Exh. No. MBM-1T at 18:10-19:23; O'Connell, Exh. No. ECO-1THC at 16:10-20; *see* O'Connell, Exh. No. ECO-8HC.
[228] McCulloch, Exh. No. MBM-1T at 19:19-21.
[229] *Id.* at 19:19-23; *see* O'Connell, Exh. No. ECO-8HC at 1.
[230] McCulloch, Exh. No. MBM-1T at 18:11-19:3.

estimate installation costs, maintenance costs, repair costs, and the cost of bad debt per unit.[231] PSE's proposed rates are inherently uncertain, and do not relate to the actual bundled products and services that customers would receive.

66 While PSE would charge a tariff rate based on a hypothetical "average" product, it would not actually offer that "average" product. Instead, PSE would offer various models in each product class that all differ from the "average" product by having greater or lesser capacity, or more or fewer features, and a greater or lesser cost.[232] Under the tariff, a customer that leases a product with more capacity or features than the average product receives a preference: by paying for the average product, the customer does not pay for the extra capacity or features his or her leased product has.[233] Conversely, a customer that leases a product with less capacity or fewer features than the average product is prejudiced: by paying for the average product, the customer pays for capacity or features his or her leased product does not have.[234]The mismatch between the product that PSE charges for and the products that it actually offers means that customers will "invariably" receive either a better or worse deal than peers leasing a different product in the same class.[235] PSE's proposed service would unduly discriminate against similarly situated customers.

67 Exacerbating this problem is the fact that each customer's rate would be fixed for the entire contract term; any future rate change that better reflects the true cost of the proposed service would apply only to customers that enter a contract after the new, changed rates go

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[231] McCulloch, TR. 223:20-225:2.
[232] *See* O'Connell, Exh. No. ECO-1T at 20:1-18 21:13-21; O'Connell, Exh. No. ECO-8HC at 1(summarizing the various bids for residential heat pumps of between two-and three-ton capacity, all of which PSE averaged to produce the tariff, and how much the cost of each product and associated services deviate from the average cost).
[233] O'Connell, Exh. No. ECO-1HCT at 20:1-18, 21:13-21.
[234] *Id.*
[235] *Id.* at 18:15-19:3; *see* Exh. No. ECO-8HC at 1.

into effect.[236] PSE offers to address the speculative nature of its proposed rates with a compliance filing, if the Commission so orders. That filing would change the tariff rates to reflect the actual prices agreed to during the contracting process,[237] but would not apply to customers who had already signed leases before the filing.[238] The filing—and every subsequent rate change—therefore creates further problems of undue preference or prejudice between generations of the proposed service's participating customers because similarly situated customers would pay different rates for the same products and services.[239] Similarly situated customers would thus pay different rates for the same product and service, and neither rate would necessarily reflect the actual aggregate cost of the product and service they receive. In other words, fixed-rates based on averages of cost estimates virtually guarantee that cross-generational subsidies within each class of participating customers will occur.[240]

68 The discrimination against similarly situated customers is undue and unreasonable: nothing justifies the preference or prejudice. PSE could (and should) have proposed rates based on the actual cost of the particular products and services it intends to offer. It could have, for example, at a minimum, selected the equipment it plans to offer, or sought firm offers for that equipment,[241] or signed contracts effective only upon the Commission's

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[236] McCulloch, Exhibit No. MBM-1T at 11:1-10.
[237] McCulloch, Exh. No. MBM-7T at 9:10-13; Norton, Exh. No. LYN-1T at 9:1-3, TR. at 129:10-13; Englert, Exh. No. EEE-3T at 12:11-14.
[238] O'Connell, Exh. No. ECO-1THC at 16:21-17:6, 23:3-13; McCulloch, Exh. No. MBM-1T at 20:14-21:2.
[239] O'Connell, Exh. No. ECO-1HCT at 16:21-17:6; *see* RCW 80.28.090.
[240] Cebulko, Exh. No. BTC-1HCT at 24:13-14.
[241] *See* RCW 62A.2-205.

approval of the proposed tariff.[242] By failing to do so, PSE risks cross-subsidization between participating customers in the same product class.[243]

69 PSE testified that its proposed tariffs would not cause some customers to "vastly" over- or under-pay.[244] By doing so, the Company implicitly concedes that customers will inevitably under- or over-pay. In essence, PSE argues it can permissibly bury preferential or prejudicial rates for particular products with the estimated costs of the service it bundles those products with. The Commission should reject PSE's attempts to make discriminatory rates lawful by hiding preferential or prejudicial rates under other bundled charges.[245] The Commission should reject the tariff as violating the public service laws.[246]

D. The Leasing Service Raises Numerous Consumer Protection Concerns

70 As stated above, the Legislature has exempted actions or transactions "permitted, prohibited, or regulated" by the Commission from Washington's Consumer Protection Act (CPA).[247] Accordingly, the Commission has jurisdiction over all consumer protection complaints arising from a utility's regulated activities, like the utility's operations under the terms of a filed tariff.[248] The Commission should reject the proposed tariff because of the consumer protection concerns it raises.

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[242] *See Chem. Bank v. Wash. Pub. Power Supply Sys.*, 102 Wn.2d 874, 691 P.2d 524 (1984) (citing RESTATEMENT (SECOND) OF CONTRACTS, § 224 (1981)) (condition precedent to contract enforceability).
[243] Cebulko, Exh. No. BTC-1HCT at 24:13-25:20; O'Connell, Exh. No. ECO-1HCT at 21:13-21; Pinkey, Exh. No. WEP-1T at 4:5-7.
[244] McCulloch, MBM-7T at 19:6-11.
[245] RCW 80.28.090.
[246] *See id.*
[247] RCW 19.86.170.
[248] *D.J. Hopkins v. GTE NW, Inc.*, 89 Wn. App. 1, 7, 947 P.2d 1220 (1997).

1. The proposed tariff contains a number of grossly unfair terms.

71 The plain terms of PSE's proposed tariff raise a number of consumer protection concerns. Several of these are mentioned below, but the list is not exhaustive. Rather, the list serves to illustrate the myriad ways in which the Company shelters itself from risk by shifting the risk onto its customers.

72 First, PSE retains the right to both accelerate all payments due and repossess its property under the lease if a customer defaults.[249] These terms raise the possibility that a customer who defaults shortly into the lease would owe the total cost of the 10 to 18 year contract and would lose its right to receive the bundled product and service.[250] The customer thus would gain nothing for their payment.

73 Second, while the tariff locks PSE's customers in for approximately a 10- to 18-year term, PSE may terminate the lease at its discretion on 30 days' notice,[251] which would allow PSE to walk away from a "lemon" that it would otherwise have an obligation under the lease to repair.[252] PSE could also theoretically use the provision to terminate a lease and then enter into a new lease to obtain higher rates.[253] Customers, however, can only terminate the lease by exercising their purchase option.[254]

74 Third, the tariff restricts customer remedies and may preclude Commission action, potentially leaving customers without any legal recourse. For example, once leased equipment is inoperable for more than 48 hours, PSE must give customers a bill credit equal

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[249] McCulloch, TR. 347:13-348:9; Subst. Proposed Sched. 75, Sheet No. 75T at § 5.11.a.iii.
[250] McCulloch, TR. 347:25-348-:9.
[251] McCulloch, TR. 350:19-351:10; Subst. Proposed Sched. 75, Sheet No. 75U at § 5.12.b.
[252] McCulloch, TR. 351:12-353:22.
[253] McCulloch, TR. 353:23-354:20.
[254] Subst. Proposed Sched. 75, Sheet No. 75U at § 5.12.c.

to one thirtieth of the monthly bill for every successive 24-hour period.[255] Staff found that credit, worth as little as sixty cents per day, woefully inadequate.[256] This provision also provides PSE with interests contrary to those of its customers. For example, in the event of an outage on Thanksgiving, PSE might decide to wait past the weekend and simply pay around $2 rather than pay overtime for its contractors to fix equipment on a holiday. Worse still, PSE takes the position that the tariff and lease terms spell out its obligations, meaning that the Commission could be limited in pursuing enforcement actions related to the service.[257]

75 Fourth, the tariff limits PSE's liability in the event of equipment failure. To enter into the lease, the customer must "indemnif[y] and hold[] PSE harmless from and against any and all losses, damages, injuries, or liabilities arising from the Customer's lease, use or operation of the Equipment."[258] Therefore, if the leased equipment malfunctions and causes damage through no fault of the customer, they nonetheless cannot seek any remedy from PSE for damage caused by PSE's property.

2. The leasing service allows for significant extra-tariff charges

76 The Company's proposed tariff leaves open significant opportunities to charge customers outside of the filed rates. This is a problem of necessity: the proposed rates do not include non-standard installation costs.[259] Such installations will likely make-up a "significant percentage" of installations involved with the leasing service.[260] Ensuring that

[255] Roberts, Exh. No. AR-1T at 8:3-5 Subst. Proposed Sched. 75, Sheet No. 75P at § 5.7.f.
[256] Roberts, Exh. No. AR-1T at 8-5-8.
[257] Englert, TR. 407:7-408:8.
[258] Subst. Proposed Sched. 75, Sheet No. 75U at § 5.13.
[259] Cebulko, Exh. No. BCT-1HCT at 23:7-9.
[260] *Id.* at 23:3-5.

"PSE and its contractors apply non-standard installation costs consistently and appropriately will be a great challenge for the Commission."[261]

3. PSE has not committed to necessary disclosures

77 PSE will not provide critical information to leasing customers. PSE plans to "disclose the 'Total Lease Payment over Lease Term,'" as well as any non-standard installation costs before its service partners install any equipment.[262] PSE does not intend to "provide all customers with a detailed breakdown of specific rates, net present value of leased equipment, standard installation costs, or [the] manner in which the approved tariff schedule rates are calculated."[263] Nor would PSE even inform its leasing service customers of the basic information of what brands and specific models it offers in the leasing service.[264] The lack of information may hamstring customers' attempts to negotiate with PSE or make informed choices about participating in the leasing service.

4. The tariff does not address a number of foreseeable issues, likely requiring Commission action to adjudicate complaints

78 PSE's tariff fails to address foreseeable issues. The tariff, for example, has no provisions governing marketing of the leasing service to PSE's customers. That omission means that the Commission may need to deal with customer disputes about pressure sales, upselling of products, or other sales techniques.[265] Nor does the tariff contain provisions dealing with the resolution of customer disputes or payments.[266] Although the tariff contains provisions requiring customers to notify PSE of a home sale to facilitate transfer of the

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[261] *Id.* at 23:9-10.
[262] McCulloch, Exh. No. MBM-27 at 1.
[263] *Id.*
[264] McCulloch, Exh. No. MBM-60.
[265] Roberts, Exh. No. AR-1T at 3:21-4:9.
[266] *Id.* at 4:11-21.

equipment, the tariff does not explain what happens to customers who fail to notify PSE.[267] Nor does the tariff specify the consequences for customers who fail to fulfill their maintenance commitments.[268] The Commission may bear a heavy burden investigating and resolving any disputes that might arise from PSE's failure to spell out all the necessary terms.[269]

5. The leasing service will not generate sufficient regulatory fees to pay for its administration, requiring cross-subsidization from PSE's general ratepayers

79 Regulatory fees generated by the service should cover the regulatory supervision of the consumer protection issues created by the proposed service.[270] Those fees, however, would be paltry over the first three years of implementation: $1,365 the first year and $20,485 in the third year.[271] The burdens placed upon Staff by the service, however, are quite significant.[272] PSE has acknowledged that, despite it claims of fencing the leasing service off from its non-leasing customers, any overage in Commission investigation of those consumer protection issues would be borne by PSE's general ratepayers.[273]

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[267] *Id.* at 5:4-13; *but see* Proposed Sched. 75, Sheet 75-S, at 5.10.b.
[268] Roberts, Exh. No. AR-1T at 5:4-5.
[269] *E.g.*, *Id.* at 4:11-21.
[270] *See* Englert, TR. 439:14-440:3.
[271] *Id.* 439:1-9.
[272] Cebulko, TR. 480:10-481:11.
[273] Englert, TR. 439:22-440:3.

E. PSE's Filing Has Been a Moving Target, Which Raises Concerns About Fundamental Fairness

80 PSE's filing has also been a moving target[274] from the day it was filed[275] through the close of the record.[276] Commission Staff and the intervenors have devoted precious time and resources to analyzing PSE's proposals, only to find PSE later modifying those proposals. PSE, for example, radically changed its initial tariff filing after Staff criticism of the fact that it lacked rates and potentially included sales revenue in PSE's rate base. Even more concerning, PSE added substantial new features on rebuttal without providing necessary detail and support,[277] and it changed key assumptions used to develop its rates and benefit forecast after the hearing.[278]

81 Our society uses adversarial proceedings to produce the truth.[279] Proceedings are not meaningfully adversarial where one side cannot examine and challenge opposing evidence submitted to the tribunal.[280] In contrast to civil trials, administrative adjudications generally are governed by liberal evidentiary rules that allow for the admission of questionable or challenged evidence. Administrative adjudications also require complex litigation to be resolved expeditiously. Accordingly, the Commission requires that the Company present the

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[274] *See* Dockets UE-151871 & UG-151872, Staff Motion for Summary Determination, at ¶¶ 3-7 (July, 13, 2016).
[275] Dockets UE-151871 & UG-151872, Advice No. 2015-23 (Sept. 18, 2015) (PSE did not provide any pre-filed testimony to substantiate its proposed leasing service; only a cover letter that broadly described the proposal accompanied the tariff sheets, which contained terms, but not rates.).
[276] *See* Dockets UE-151871 & UG-151872, Staff Response to PSE Response to Bench Request 1, from Sally Brown (Aug. 10, 2016); Response to Puget Sound Energy's Response to Request No. 1 and Motion to Strike on Behalf of Public Counsel, from Lisa W. Gafken (Aug. 15, 2016).
[277] Norton, TR. 122:10-129:24.
[278] Puget Sound Energy's Response to Bench Request No. 1, Docket Nos. UE-151871 and UG-151872, at 1 (Aug. 9, 2016).
[279] *Jugan v. Pollen*, 253 N.J. Super. 123, 134, 601 A.2d 235, 241 (N.J. Super. Ct. App. Div. 1992).
[280] *See Chevron Corp. v. Sheffitz*, 754 F.Supp.2d 254, 265 n. 84 (D. Mass. Dec. 2010).

full scope of its evidentiary case in its pre-filed direct testimony.[281] This facilitates review by enabling a robust vetting of the evidence and the issues.

82 PSE's constant shifting of the terms of its tariff undermines the parties' ability to meaningfully vet the Company's case, thwarting the Commission's search for truth and inhibiting its ability to make wise policy. The parties had no opportunity to review the data underlying the new features PSE offered on rebuttal, the details of which are likely to warrant an entirely new case given the breadth and scope of those features and the lack of detail about them. The parties also had no opportunity to present testimony about those new features. Indeed, no party had the chance to cross-examine PSE's witnesses about a change in a key assumption given that PSE made the change after the hearing. PSE's alarmingly deficient and constantly shifting case is tantamount to a request for preapproval, which the Commission does not grant.[282] Fundamental fairness dictates that the Commission to reject PSE's tariff.

V. CONCLUSION

83 The Commission should reject PSE's proposed service as an unlawful extension of PSE's public service obligations into a robust functional market. The proposed service represents a distinct departure from Commission precedent, state law and policy, as well as the historical circumstances that have justified economic regulation as a substitute for competition. The proposed service also does not comport with traditional regulatory principles and lacks any public purpose connection to the Company's principle regulated

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[281] *Utils. & Transp. Comm'n v. Puget Sound Energy, Inc.; In re the Petition of Puget Sound Energy, Inc. for an Order Authorizing Deferral of Certain Electric Energy Supply Costs*, Dockets UE-011163 and UE-011170 (*consolidated*), Sixth Supplemental Order, ¶ 15 (Oct. 4, 2001).

[282] *In re Regulation of Electric Utilities in the Face of Change in the Electric Industry*, Docket No. UE-940932, at 27 (April 22, 1998) ("[T]he Commission does not support any recommendation that would constitute any form of preapproval of utility expenditures . . . .").

service—the sale of electricity and natural gas. The proposed service is nothing more than a merchandising and financing service that would make PSE a rate-regulated retailer of appliances, which is expressly prohibited by statute.

84 PSE further failed to meet its most basic burdens of proof. The Company failed to establish that customers need or want the proposed service, or that the proposal could serve customers cost-effectively. The Company's proposed rates are not fair, just, or reasonable. Rather, they are discriminatory. In addition, the consumer protection issues raised by PSE's unfair tariff are numerous and insurmountable. The problems with this filing are legion. The Commission should not give credence to PSE's unprecedented filing. In sum, the Commission should emphatically reject and summarily dismiss the entirety of PSE's case.

DATED this 30th day of August 2016.

Respectfully submitted,

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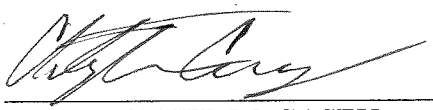

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