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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*) POST-HEARING REPLY BRIEF OF INTERVENOR SMACNA-WW **REDACTED VERSION**

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I. INTRODUCTION

1 Most, if not all, of the arguments made by Puget Sound Energy (PSE or the Company) in its initial brief[1] have been proactively addressed by the various parties in their initial briefs. Accordingly, this reply brief of the Sheet Metal and Air Conditioning Contractors National Association – Western Washington (SMACNA-WW) will emphasize only a few points where PSE has overstated or misstated its claims and, in the Conclusion, recommend to the Commission that it reject PSE's proposed Lease Solutions tariff and describe what such rejection would and would not entail.

II. ARGUMENT IN RESPONSE TO PSE

A. Washington's Public Service Laws Do Not Authorize Public Service Companies to Operate "Rental Programs" of the Type Envisioned by PSE

2 As it did in earlier briefing on Commission Staff's Motion for Summary Determination, in its Initial Brief PSE relies on several provisions in the public service laws that mention "rentals" among the variety of charges that a public utility may have its tariffs.[2] However, as pointed out in our Initial Brief,[3] the references in the substantive sections of the public service laws to "rentals" appear only in the chapter relating to telecommunications. The term does not appear in the chapter relating to gas and electric companies. When the Legislature chooses to use certain terms in one provision, but not in another, it indicates that the Legislature intended different meanings.[4] Therefore, the Legislature did not intend "rentals" to be among the charges authorized for electric and gas companies. Of course, the Legislature included the terms "rental" in the general procedural sections, now codified in

[1] Initial Brief of Puget Sound Energy, UTC Dkt. Nos. UE-151871, UG-151872 (Aug. 30, 2016) (PSE Br.).
[2] PSE Br. ¶¶42-43.
[3] Initial Post-Hearing Brief of Intervenor SMACNA-WW, ¶¶13-18, UTC Dkt. Nos. UE-151871, UG-151872 (Aug. 30, 2016)(SMACNA Br.).
[4] *See, e.g., Densley v. Department of Retirement Systems*, 162 Wn.2d 210, 219, 173 P.3d 885 (2007).

RCW 80.04, but those sections of necessity apply to both the energy and telecommunications provisions and did not define the substantive scope of jurisdiction over electric and gas companies.

3 PSE seeks additional support for its position in recent legislation allowing utilities to deploy electric vehicle equipment, citing that legislation as evidence that "behind the meter" equipment is within the purview of a public service company.[5] However, in reality, that legislation cuts the other way. For electric vehicle equipment, the Legislature was specific in its grant of authority to public service companies to own and operate such equipment and regarding the parameters of Commission regulation of such activity.[6] The Legislature has not done that for appliance leasing programs.

4 PSE also cites several other programs it is engaged in, presumably to imply that this new leasing proposal is of the same nature. But a modest gas appliance servicing program, designed to ensure gas safety,[7] is different in kind and scope from the Lease Solutions proposal. And leasing of transformers is more in alignment with the definition of "electric plant."[8] In any event, there is not a robust competitive transformer lease or sales market.

B. PSE's Cited Premises for Its Proposed Leasing Program Are Not Valid

5 PSE relies on a "significant market need" for the service it proposes,[9] relying, as it has all along, on a "market gap." However, all parties, with the exception of PSE, interpret PSE's own data differently. While PSE reads the data to show that 40% of equipment is

[5] PSE Br. ¶57, *citing* RCW 80.28.360.
[6] In RCW 80.28.360, the Legislature was very precise on the conditions under which a utility could get into the electric vehicle supply equipment business.
[7] PSE Br. ¶10, n. 12.
[8] RCW 80.04.010(12).
[9] *E.g.*, PSE Br. ¶74.

"beyond its useful life,"[10] Commission Staff, Public Counsel, and SMACNA-WW do the correct math.[11] PSE criticizes the other parties for spending "an inordinate amount of time at the hearing" in disputing PSE's calculations.[12] However, this is an important point. The erroneous 40% figure was used in the initial filing by PSE,[13] [redacted],[14] presumably was included in presentations to senior PSE management and to the PSE Board,[15] and permeates the prefiled testimony of several of PSE's witnesses.[16] The time spent by the parties critiquing PSE's analysis of its data is nothing compared to the emphasis PSE placed on the invalid 40% figure. And recall that the term "beyond its useful life" does not really capture the meaning of the whatever the actual percentage is. The equipment is still useful, and, according to PSE's lead witness Ms. Norton,[17] it is simply an "average" life of the equipment. Therefore, it only makes sense that some of the equipment

[10] PSE Br. ¶13.
[11] Initial Brief on Behalf of Commission Staff, UTC Dkt Nos. UE-151871, UG 151872 ¶¶54-57 (Aug. 30, 2016) (Staff Br.); Brief of Public Counsel, UTC Dkt Nos. UE-151871, UG 151872 ¶¶49-52 (Aug. 30, 2016) (Public Counsel Br.); SMACNA Br. ¶¶40-46.
[12] PSE Br. ¶13, n.17.
[13] Letter to Steven V. King, UTC, from Ken Johnson, PSE, UTC Dkt. No. UE-151871, at 2 (Nov. 6, 2015) (Advice No. 2015-23).
[14] [redacted]
[15] *See* Norton, Tr. 145:13-20.
[16] *E.g.*. Teller, Exh. JET-1T 7:9-12; Exh. JET-3; Norton, Exh. LYN-1T 10:16-21, 13:3-5; McCulloch, Exh. MBM-1T 4:3-10.
[17] Actually Mr. Jason Teller appeared to be the lead witness for PSE, but, for reasons not disclosed, Mr. Teller left the company in mid-case, leaving it to Ms. Norton to adopt his testimony.

would exceed the average. The modest percentage of equipment in use that is beyond the predicted "average life" for such equipment is not evidence of any market aberration.[18]

6 Likewise, the survey data that support the "interest" in rentals is weak at best. The survey questions assumed that the economics of a lease would be similar to those of a sale, but they are not.[19] PSE attempts to place the burden of proof on the other parties to show lack of demand by stating "[n]otably, no other party to this case has conducted or presented any other market analysis evaluating customer interest in an equipment leasing program comparable to PSE's proposed service."[20] But there is evidence, expert testimony, that there is no demand for the service.[21] And, "notably," there is a paucity of lease programs anywhere in the country.[22] One would think that if there are some willing lessees, there would be some willing lessors, but there are not.

7 Even if it is true that there is some need to replace some old, outdated equipment, and even if it is true that some of PSE's customers may want a lease option, the question remains whether such hypothetical facts would warrant governmental intervention to establish a lease program where one does not currently exist. Government regulation of monopoly utility services was important in 1911 when the Washington Legislature revamped the Railroad Commission into the Public Service Commission and gave it authority over electric, gas, water, and telephone companies.[23] That 1911 law addressed some serious public policy issues. The fact that there currently is not an unregulated lease

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[18] Regarding hot water heaters, some of the "beyond the useful life" equipment is attributable to the age of many 33,000 hot water heaters PSE currently leases. *See* Exh. MBM-12.
[19] SMACNA Br. ¶¶48-51.
[20] PSE Br. ¶33.
[21] Fluetsch, Exh. BF-1T 5:10-16; van den Heuvel, Exh. JvdH-1T 8:17-9:9.
[22] *See* SMACNA Br. ¶47.
[23] Laws of 1911, ch. 117.

market for appliances does not rise to the level of requiring substantial governmental intervention and ongoing oversight.

C. With Its Meager Product Offerings, the Proposed Lease Program Would Stifle Innovation

8 In his treatise *The Economics of Regulation* Alfred Kahn stated "it seems a fair generalization that regulation has on balance been obstructive both of competition and of the innovation it helps stimulate and justify."[24] Currently, in the unregulated sales market new and innovative appliances are coming into the market all the time, meeting customer demand for such products.[25] Indeed, Mr. Fluetsch, who operates a major equipment business in South Puget Sound, testified that he meets "with one or more sales representatives almost every week to discuss new products that are available."[26] There are literally hundreds of equipment options, with more coming all the time.[27]

9 In contrast, PSE offers only one or two options for each type of equipment, and much of the equipment is just "standard efficiency."[28] New efficient and innovative options, such as ductless heat pumps and zoned systems are not part of PSE's service offering, even though such products are in great demand.[29]

10 PSE suggests that its tariff offers a "reasonable selection of equipment options that would provide a practical equipment solution for most customers."[30] The limited menu, according to PSE, would allow its customers to avoid the more complex selection among multiple products in favor of a "straightforward selection of options" preselected by the

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[24] 2 A. Kahn, *The Economics of Regulation* 247 (1988 ed.).
[25] *See* Fluetsch, Exh. No. BF-1T 6:3-7:7; van den Heuvel, Exh. No. JvdH-1T 4:6-8:15.
[26] Fluetsch, Exh. No. BF-1T 8:23-9:1.
[27] van den Heuvel, Exh. No. JvdH-1T 5:3-6:10.
[28] Cebulko, Exh. BTC-1HCT 38:1-3.
[29] van den Heuvel, Exh. No. JvdH-1T 6:12-8:15; Fluetsch, Exh. No. BF-1T 6:13-7:7.
[30] PSE Br. ¶21.

Company for the consumer.[31] And this is not like leasing a car for a finite period of time in which a potential car buyer can sample options. (And it is not like PSE's legacy leasing program, which is month-to-month.) These are long term leases, for the anticipated life of the equipment. During that term, the customer would not be able to switch to more efficient, or more innovative, equipment. As highlighted by Public Counsel, there would be "lost opportunities" for innovation and substantial energy efficiency if customers are committed to less than optimal equipment for such long periods of time.[32]

11 PSE argues that its "leasing platform" could accommodate other equipment.[33] But that would be in the future, and innovative equipment is in the present. If PSE's ambitious market share hopes were to come to fruition,[34] and "most customers" are channeled into the limited product array of the PSE proposed tariff, the public interest would be harmed.

D. PSE's Rates Are Not Fair, Just, and Reasonable As They Are Not Based on Costs and They Include Exorbitant Levels of Profit

12 We discussed the many flaws of PSE's proposed lease rates in our Initial Brief.[35] However, PSE in its Initial Brief makes several assertions that are simply wrong and merit a further focused response.

13 First, PSE alleges that its rates are fair, just and reasonable in part because they are based on "actual market equipment costs submitted by bidders responding to PSE's RFQs."[36] That is incorrect and misleading. The responders to PSE's RFQs were not "bidders" as that term is commonly understood. It was not a competitive process. PSE

[31] PSE Br. ¶21.
[32] Public Counsel Br. ¶¶61-62.
[33] PSE Br. ¶3.
[34] *See* Exh. No. BTC-2HC, at 4.
[35] SMACNA Br. ¶¶53-69.
[36] PSE Br. ¶92.

asked for information on costs of equipment, and 15 of the hundreds of contractors in PSE's service territory responded. But the dollar figures that the responders quoted were not offers from which PSE could choose to accept and thereby set the lowest price that PSE would actually pay. Rather, they were figures that PSE used to calculate an average of all the responders. That average then became the "cost" that went into PSE's pricing model. But that "cost" for pricing purposes is not PSE's actual "cost." That would be determined later, perhaps through a competitive process.[37] As pointed out in our Initial Brief, there is a wide discrepancy between the "low" submission by the responders to the RFQs and the "average" of the submissions.[38] So, if the ultimate actual cost to PSE is toward the lower end, PSE's actual costs will be lower, perhaps much lower, than the costs that would be passed onto the lease customers via the pricing model.

14 Second, PSE states that the rates are based on costs of "known products."[39] While it is true that the responders to the RFQs assigned prices to specific products, the identity of specific products stopped there. In the tariff, there is no identify of the brand or even specifics about the product other than general information about size or efficiency. To the customer, the products are not "known" and would not be until after the customer signs a lease. Though PSE asserts that brand is not important,[40] that simply is not true, according to Mr. Fluetsch, who has had a long career in the industry.[41]

15 PSE defends the use of "averages" of the prices submitted as part of the RFQ process, stating that average costs are frequently used in ratemaking.[42] PSE misapplies

[37] *See* McCulloch TR 306:18-21; 227:24-228:2.
[38] SMACNA Br. ¶¶53-57.
[39] PSE Br. ¶¶91-92 (heading).
[40] *Id*. ¶93.
[41] Fluetsch, Exh. No. BF-1T 10:1-8.
[42] PSE Br. ¶¶101-103.

concepts of average cost pricing in ratemaking. Of course, costs of service vary customer by customer. It may cost less to serve a customer in a densely populated area than one in a more suburban setting, but the tariffed prices are the same to each. In standard ratemaking, tariffed prices for a given service are set by dividing the utility's costs of service by the number of customers to get an average. Therefore, the sum of all the average costs will equal the utility's total cost. The utility will not receive a windfall nor suffer a deficiency. However, the averages PSE uses in its lease proposal are not the same as averages used in general ratemaking. Instead, they are cost submissions by a handful of responders that are not the actual costs to PSE. Presumably, if PSE would really try to pay least costs, it would not pay the average of the submissions, but pay the lowest possible price, which would be below, perhaps substantially below, the average of the submissions.

16 Finally, PSE states that "[n]o party has challenged PSE's use of its weighted cost of capital in calculating its rate of return."[43] In its opening case, PSE simply asserted that its existing cost of 7.77% is appropriate and now implies that because no other party offered expert testimony in opposition that factor in the pricing model should stand. Not only does that inappropriately shift the burden of proof to those contesting the rates, but, for reasons described in our Initial Brief, it results in an excessive level of profit for the Company.[44] That 7.77% rate does not reflect the risk appropriate to a lease proposal under which PSE would not acquire equipment until after it enters into a lease for that equipment; it would be applied not to PSE's actual investment but to the average cost developed from the RFQ responders; and, in any event, PSE has stated that it will finance the program through debt,

[43] *Id*. ¶105, n.263.
[44] SMACNA Br. ¶¶61-64.

not investment. Therefore, a cost of capital based in substantial part on the cost of equity is inappropriate.[45]

17 In sum, process by which PSE has set its proposed tariff prices is flawed, with the result that the prices would be excessive. PSE may argue that the price does not matter, so long as PSE is not subsidizing its costs from its other regulated activities. Such an argument may be valid if PSE were to operate this program on an unregulated basis, and it could charge what the market would bear. But PSE did not choose that option. It seeks a Commission imprimatur that the lease rates are "fair, just, and reasonable" as a selling point to customers who PSE would seek to lock in for a 17-year lease term. Customers rely on the Commission for assurance that they are getting the least cost services from their utilities. That is not the case here.

18 The flaws in the pricing are not something that can be remedied by "refreshing" the rates after a compliance filing, as PSE suggests. Getting to rates that are fair, just and reasonable is not something done by a few key strokes on the computer. The Commission should simply reject the filing.

E. PSE's Proposed Lease Program Would Have Competitive Advantages Over Unregulated Competitors

19 In our Initial Brief, we articulated reasons why PSE's proposal, if approved, would result in a skewed and unfair appliance market.[46] That argument was based in part on the legal reality that by offering its lease service as a regulated service, PSE would be immune

[45] SMACNA Br. ¶¶61-64.
[46] *Id*. ¶¶29-38.

from application of the Consumer Protection Act (CPA) and related statutes.[47] In its Initial Brief, PSE attempts to argue that its lease program will be subject to "robust consumer protection provisions that meeting or exceed protections required under the consumer protection laws."[48] Its primary argument is that "regulated companies are required to publish and file with the Commission all rates and charges."[49] That argument ignores the realities of tariff transparency, particularly the transparency of this particular tariff.

20 Let us examine the alleged transparency of PSE's prices by picking one of the dozen appliances in PSE's proposed tariff: a Two Stage Residential Furnace. The proposed tariff describes the product and the "monthly lease charge" as follows[50]:

Fuel	Type	Size	Efficiency	Monthly Lease Charge
Natural Gas	Furnace	40-60k Btu	≥80%	$58.19

While it is true that this description and charge is included in the published tariff on file at the Commission, to the average consumer that does not enhance transparency over and above the prices on appliances in a contractor's showroom, at Home Depot, or on a website. Indeed, the fine print in the tariff also states that "[r]ates in this Schedule are subject to adjustment by such other schedules of the Company's Electric Tariff as may apply and by applicable taxes."[51] So, for a PSE customer to realize the touted transparency, the customer would have to scour other schedules "as may apply." Home Depot does not so treat its customers; it has price stickers right on the equipment.[52] In addition, there is the added, and

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[47] RCW 19.86.170. We say "related statutes" because some other consumer protection statutes, outside RCW 19.86, state that violation of them is also a violation of the Consumer Protection Act. *See, e.g.*, RCW 63.10.050 (violation of statute regulating consumer leases is also a violation of the Consumer Protection Act).
[48] PSE Br. ¶¶119-120 (heading).
[49] *Id*. ¶122.
[50] Proposed Schedule 75, Or. Sheet 75-B.
[51] *Id*.
[52] An unregulated company hide the ball on other charges. Failure to disclose an element of the price, such as an added fee, would subject the company to a claim under the CPA. *See, e.g., Robinson v. Avis Rent a Car*

unknown, cost of "nonstandard" installation charges. Rather than being part of the initial negotiations, as is the case in the unregulated sales market,[53] in the PSE proposal, such nonstandard costs unknown at the time of entering into the lease and ultimately are the responsibility of the lessee.[54] At the point the customer is informed of non-standard costs, that customer's options are to accept the additional charges, whatever they may be, or to walk away from the lease and start over.[55]

21 Beyond the transparency challenges in the filed tariffs, and in the non-standard installation costs, just how much information is contained in the tariff? It has the lease rate, so the customer would know how much the monthly charge would be (subject to additions caused by other tariffs "as may apply"). However, the tariff does not state what the monthly lease rate gets the customer. Imagine an auto dealer who advertised as follows:

AUTOMOBILE FOR SALE
Mileage: ≥ 25 mpg
Size: ≥ 4 passengers
$29,900

This would be transparent on price ($29,900) and give some basic information on the range of efficiency and size, but it would not provide information on make or model. Customers would not find this transparent, yet that is precisely the type of information contained in

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Systems, 106 Wn.App. 104, 116, 22 P.3d 818 (2001) (failure to disclose a "concession fee," a material fact, "would be deceptive").

[53] *See* Fluetsch, Exh. BF-1T 9:15-10:8.

[54] Proposed Schedule 75, Or. Sheet No. 75-L, Lease Terms and Conditions ¶6 states in part:

> Customer will be responsible for payment of installation costs for any non-standard conditions, as discovered by PSE or its contractor upon inspection of the Premises. . . . Non-standard conditions which may result in excess installation charges include, but are not limited to: installations which require additional equipment or modifications as required by code, additional man-power or special equipment . . . or installations which require structural changes or non-standard prep work, such as adding or removing walls or drywall, or adding, moving or extending electrical wiring, changing the electrical panel, venting, plumbing or natural Gas lines. . . .

[55] Schedule 75, Or. Sheet No. 75-L, Lease Terms and Conditions ¶6 states that the customer "may elect at that time to cancel the installation without cost and this Agreement shall not become effective."

PSE's proposed tariff. The fact that PSE would file a tariff with the dollar lease price is not an "extensive consumer protection provision[]" as it alleges.

22 Though PSE cites some of the regulatory provisions as providing protection for consumers, it overlooks the fact that PSE is attempting to opt out of one of the larger regulatory protections for consumers: the statutory obligation to serve.[56] PSE says it is bound by the statutory prohibition against discrimination,[57] but, in reality, it can indiscriminately avoid serving any customer or set of customers through the escape clauses in the tariff that forgive any obligation if the equipment is not available or a contractor is not available. And PSE can terminate its obligation any time on thirty days notice.[58]

23 However, the main flaw in PSE's claims its leasing program would be subject to greater consumer protection laws is that it overlooks the fact that the vast body of case law under the Consumer Protection Act would not apply to PSE. Unregulated actors may not hide the price or other material terms,[59] misrepresent that the sales price is lower than what other competitors charge,[60] or misstate a material fact to induce a person to enter into a contract.[61] PSE is immune from that body of law. And while, under the CPA, competitors may take action to police the deceptive acts of others, that is not so for unregulated actors seeking a level playing field with PSE.[62] Instead, PSE argues that it is subject to

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[56] RCW 80.28.110.
[57] PSE Br. ¶122.
[58] *See* SMACNA Br. ¶37 (citing provisions in the proposed tariff). In its Initial Brief, PSE boldly, and inaccurately, states "[t]hus, the leasing service will be available to all customers." PSE Br. ¶65. But, given the limitations and exit ramps in the tariff, that is not true as a matter of right for the customer (as it would be, for example, with basic electricity service). It would only be true if PSE, at its discretion wants it to be available and is able to make appropriate arrangements with an adequate number of contractors.
[59] *See, e.g., Robinson v. Avis Rent a Car Systems*, 106 Wn.App. 104, 116, 22 P.3d 818 (2001)
[60] *State v. Ralph Williams' North West Chrysler Plymouth, Inc.*, 87 Wn.2d 298, 305, 553 P.2d 423 (1976).
[61] *Id.* at 306.
[62] *See* SMACNA Br. ¶¶29-35.

Commission rules. But Commission rules do not address the type of deceptive practice issues that are the crux of many CPA claims. While the Commission rules regulate forms of bills, and the like, and provide for consumer complaints, they do not articulate a set of standards relating to deceptive practices, actions to reduce competition, or acts that restrain trade or commerce, all of which are covered in the CPA.[63] If the Commission wishes to let regulated utilities enter competitive markets through the tariff process and protect consumers in the process, it would have to first adopt substantial consumer protection rules.

24 These consumer protections are important, and PSE should not be able to escape them. Assume for a moment that PSE would be operating the lease program on an unregulated basis. Recall that PSE misstated the "market gap."[64] If that false representation were made to a contractor and that contractor then entered into a contract to participate in the leasing program to the exclusion of its other business and it turns out that the leasing market was not as robust as promised, then there could be a CPA issue. Likewise, if PSE were to suggest to potential customers that the economics of a lease "would be similar to" the economics of a sale,[65] and the customer entered into a lease based on that representation that may be a false statement that would implicate the CPA.

25 Contrary to PSE's contentions, its proposed leasing program would operate in a relative consumer protection vacuum to the detriment of consumers and the market. The Commission should reject the proposal on this ground alone.

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[63] *See* SMACNA Br. ¶30.
[64] *See id*. ¶¶40-43.
[65] *See id*. ¶¶47-49.

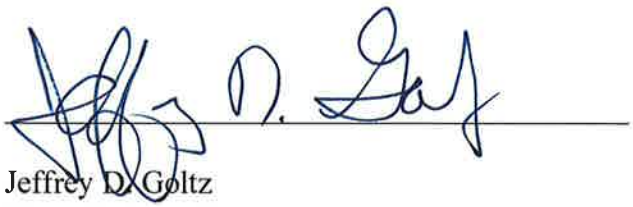
III. CONCLUSION

26 The Commission should reject the Lease Solutions tariff. It is unlawful and contrary to sound regulatory policy. If PSE wishes to operate a leasing program, it should do so on an unregulated basis and compete fairly with other players in the marketplace.

27 Rejection of the proposed tariff should not hinder PSE's efforts to pursue a status as a "utility of the future." Should PSE wish accept the invitation of the Commission to pursue other business opportunities, such as energy storage, rooftop solar generation, or electric vehicle charging,[66] then some of the work it has undertaken to in this leasing matter should transfer to such efforts. However, the Commission should make clear that among the potential "utility of the future" endeavors for regulated utilities, appliance leasing is not among them.

DATED this 19th day of September, 2016.

Respectfully submitted,



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[66] *Interpretive Statement Concerning Commission Jurisdiction and Regulation of Third-Party Owners of Net Metering Facilities*, Dkt. No. UE-112133 ¶77, n.100 (July 30, 2014)