EXHIBIT NO. \_\_\_\_\_ (RCC-6T)

DOCKET NO. UE-111048/UG-111049

2011 PUGET SOUND ENERGY, INC. GENERAL RATE CASE

WITNESS: RALPH C. CAVANAGH

BEFORE THE WASHINGTON STATE

UTILITIES AND TRANSPORTATION COMMISSION

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| WASHINGTON UTILITIES AND TRANSPORTATION COMMISSION,  Complainant,  vs.  PUGET SOUND ENERGY, INC.,  Respondent. | )  )  )  )  )  )  )  )  )  )  ) | DOCKET NOS. UE-111048  and UG-111049 (*Consolidated)* |

PREFILED CROSS-ANSWERING TESTIMONY (NON-CONFIDENTIAL) OF

RALPH C. CAVANAGH

ON BEHALF OF NW ENERGY COALITION

January 17, 2012

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**Q. Please state your name and business address**.

A. Ralph Cavanagh, c/o NRDC, 111 Sutter Street, 20th Floor, San Francisco, California 94104.

**Q. Are you still testifying for the NW Energy Coalition in this proceeding?**

A. Yes

**Q. Have there been any changes in the qualifications you reported in your direct testimony?**

A. No.

# I. SUMMARY OF TESTIMONY

**Q. Why are you filing rebuttal/cross-answering testimony in this proceeding?**

A. I am responding to the Washington Utilities and Transportation Commission (“UTC”) Staff Response to Bench Request on Full Decoupling (“Staff’s Response”), which outlines an approach to full decoupling that is in some respects different from that advocated in my Direct Testimony (although there are many similarities as well). I also explain my reasons for disagreeing with Staff witness Ken Elgin that more frequent rate cases would constitute a form of decoupling with less “complexity,” and I address the energy efficiency disincentives inherent in Kroger witness Kevin Higgins’s proposal to change rate design in order to recover more of Puget Sound Energy’s (“PSE”) fixed costs through non-volumetric charges.

**Q. Please summarize your testimony.**

A. On the issues involving design of a full decoupling mechanism, Staff’s Response to the Commission’s bench request represents a worthy effort that is in many respects consistent with my Direct Testimony. We disagree on a few issues involving PSE’s rate of return, per-customer revenue calculation, and off-system sales, but our areas of agreement are much more substantial than our differences.

Staff witness Elgin raises what I believe to be unjustified concerns about the “complexity” of decoupling, citing the Commission’s reference in its Policy Statement to the possibility of “unreasonable administrative burdens.” But the Commission was addressing potential joint applications for full and partial decoupling by dual fuel utilities, which are not an issue in this proceeding. I also argue that witness Elgin is incorrect in suggesting that more frequent rate cases would represent “a form of decoupling,” since this would do nothing to break the linkage between retail electricity use and recovery of a utility’s authorized nonproduction costs.

Finally, I show that the rate design changes advocated by Kroger witness Higgins as an alternative to decoupling could be justified only if the Commission concluded that utility customers currently had excessive incentives to save energy. This seems inconceivable in light of the Commission’s consistent and well-justified support for aggressive utility efforts to help customers improve the energy efficiency of their buildings and equipment.

# II. UTC STAFF RESPONSE TO BENCH REQUEST

**Q. What is your general reaction to the UTC Staff response to the Bench Request on Full Decoupling?**

A. I disagree strongly with Staff’s recommendation to substitute “a well-defended attrition adjustment” for full decoupling, but I appreciate Staff’s careful and good-faith effort to address the design issues associated with full decoupling. I see much common ground there with my own testimony.

**Q. Why do you disagree with the Staff’s preference for attrition adjustments over decoupling?**

A. As explained further below in my response to Ken Elgin’s testimony, I believe that more frequent rate cases (which is what Staff appears to mean by “a well-defended attrition adjustment”) would be much more complex than full decoupling, while achieving none of its principal objectives and sharing the deficiencies of PSE’s lost revenue recovery proposal. Assuming that the Commission does not choose this alternative to full decoupling, however, I believe that Staff has provided much of value on designing a full decoupling mechanism in the body of its response. I disagree with the Staff analysis on only a few points, as explained below.

**A. Summarize your areas of agreement with the Staff Response.**

Q. Staff describes a per-customer decoupling mechanism that would “remain in place until modified or cancelled by the Commission.”[[1]](#footnote-1) I agree. My testimony, like Staff’s Response, argues for a middle course between system-wide decoupling and class-by-class decoupling.[[2]](#footnote-2) Staff’s proposal is slightly more comprehensive in coverage than mine, but I certainly would not oppose Staff’s recommendation to “includ[e] all customers.”[[3]](#footnote-3) Staff’s recommended earnings test is essentially the same as mine.[[4]](#footnote-4) Staff and I agree that full decoupling will not reduce utility managers’ incentive to reduce costs.[[5]](#footnote-5) Staff’s approach to conservation achievement seems generally reasonable to me,[[6]](#footnote-6) although I hope that Staff would join also in my specific emphasis on “strong low-income savings results and implementation of energy efficiency programs across all sectors.”[[7]](#footnote-7) I appreciate Staff’s concerns about the lack of data to perform analysis of benefits to low-income customers from PSE conservation programs, and I note that my direct testimony proposes a specific remedy as part of an independent evaluation of the decoupling mechanism.[[8]](#footnote-8) Staff also offers what I view as reasonable recommendations on periodic reports to the Commission and service quality.[[9]](#footnote-9)

**Q. Where do you disagree with Staff?**

A. Staff believes that full decoupling justifies a prospective reduction in PSE’s authorized rate of return, and I strongly disagree,[[10]](#footnote-10) although I hope that Staff would join my recommendation that “the company should pass through to customers any cost savings associated with changes in its capital structure following adoption of the decoupling mechanism (e.g., a shift in the equity/debt ratio).”[[11]](#footnote-11) I also don’t agree with Staff that it is appropriate to include in the mechanism an automatic reduction in authorized revenue per customer after three years,[[12]](#footnote-12) given my conclusion that PSE gains no inherent advantage from substituting per-customer revenue decoupling for “the status quo, which effectively allows PSE’s annual fixed-cost revenue requirement to grow in proportion to its retail sales instead of its customer count.”[[13]](#footnote-13) Staff’s proposal here would inflict an automatic penalty for adoption of per-customer decoupling, whereas my aim is relative neutrality. Finally, Staff proposes to include in full decoupling a complex new system of accounting for off-system sales and power costs,[[14]](#footnote-14) effectively amending PSE’s Power Cost Adjustment (“PCA”), whereas my recommendation is to limit the decoupling mechanism to nonproduction costs, and to let an unadjusted PCA continue to “strike a reasonable balance between shareholder and customer interests in allocating risks associated with power supply costs and cost recovery at both wholesale and retail levels.”[[15]](#footnote-15)

# III. KEN ELGIN’S TESTIMONY

**Q. Please respond to Ken Elgin’s concern that “decoupling in all its varied forms creates unnecessary complexity.”**

A. My direct testimony does not advocate “decoupling in all its varied forms.” I have presented a specific proposal that is broadly consistent with Staff’s Response to the Bench Request in this proceeding. I note that my proposal is far less “complex” than Mr. Elgin’s proposal for multiple expedited rate cases as what he calls “a form of decoupling.”[[16]](#footnote-16) My proposal does not require the Commission to reexamine any cost-of-service issues between rate cases, and it involves only an annual true-up in rates that would not exceed three percent, designed to ensure that the utility recovered no more and no less than a Commission-approved per customer revenue requirement notwithstanding fluctuations in retail sales volumes.

**Q. Do you agree with Mr. Elgin that “the Commission recognized the potential for decoupling to create unreasonable administrative burdens” in its Decoupling Policy Statement?**

A. The Commission identified the potential for unreasonable administrative burdens from decoupling only in contexts wholly unrelated to my proposal. In the passage that Mr. Elgin cites, the Commission was referring to the possibility that “a dual fuel utility may propose full decoupling for its electric utility and limited decoupling for its gas utility,” using as an example “different returns on equity for the natural gas and electric utilities under common ownership.”[[17]](#footnote-17) My direct testimony proposes no such bifurcation; it is limited to full decoupling for PSE’s electric utility.

**Q. Do you agree with Mr. Elgin that his proposal for more frequent rate cases involves “a form of decoupling since rates will be adjusted in a timely manner to capture the effects of DSM”?**

A. No. From my perspective, the central purpose of decoupling is to break the link between retail electricity use and utilities’ recovery of authorized nonproduction costs; merely adjusting rates to capture estimated DSM effects does not accomplish this, and shares all the deficiencies of PSE’s proposal for a lost revenue recover mechanism, which my direct testimony addresses in detail.[[18]](#footnote-18) In my disagreement with Mr. Elgin, I am in full accord with the Regulatory Assistance Project, which responds as follows to the contention that “the use of frequent rate cases using a future test year eliminates the need for decoupling”:

A future test year may have the effect of causing a utility’s “revenue requirement” to more closely track a utility’s revenue requirement over time. A future test year does not, however, have the effect of constraining *allowed revenues* to a utility’s revenue requirement. In addition, a future test year does not address the throughput issue, which is one of the primary reasons for using decoupling. The

term ”decoupling” itself is rooted in the notion of separating the utility’s incentive to increase profits through increased sales by breaking the link between – that is, by decoupling – revenues from sales.”[[19]](#footnote-19)

# IV. KEVIN HIGGINS’S TESTIMONY FOR KROGER CO.

**Q. What is your response to Kevin Higgins’s opposition to revenue decoupling?**

A. Mr. Higgins simply recites traditional objections to revenue decoupling, without citing or addressing the Commission’s Policy Statement, which takes those same objections fully into account.[[20]](#footnote-20) The Commission has moved past Mr. Higgins’s reflexive opposition in its conclusion that “a properly constructed full decoupling mechanism . . . can be a tool that benefits both the company and its ratepayers.”[[21]](#footnote-21) And his specific objections to decoupling for nonresidential customers fly in the face of the Commission’s conclusion that “[g]enerally, a full decoupling proposal should cover all customer classes.”[[22]](#footnote-22)

**Q. Do you support Mr. Higgins’s recommendation to substitute rate design changes for full decoupling?**

A. No. Mr. Higgins wants to shift more fixed cost recovery into charges that do not vary with electricity consumption.[[23]](#footnote-23) But that is tantamount to arguing that PSE’s current rate structure creates excessive rewards for saving energy. Certainly Mr. Higgins’s proposal would reduce those rewards, at a time when the Commission and the legislature are clearly on record in support of more, not less, energy efficiency effort and investment across the PSE system.[[24]](#footnote-24)

**Q. Does this conclude your testimony?**

A. Yes.

1. See Exhibit No. \_\_\_\_ (Staff Response to Bench Request on Full Decoupling), pp. 7-8. [↑](#footnote-ref-1)
2. Compare Staff Response, p. 9 with Exhibit No. \_\_\_\_ (RCC-1T), p. 11. [↑](#footnote-ref-2)
3. My proposal excludes less than 140 very large customers accounting for only about 4 percent of Puget’s projected revenues from energy charges. Exhibit No. \_\_\_\_ (RCC-1T), p. 13: 9-15. [↑](#footnote-ref-3)
4. Compare Exhibit No. \_\_\_\_ (Staff Response to Bench Request on Full Decoupling), pp. 10-12 with Exhibit No. \_\_\_\_ (RCC-1T), pp. 16:1-5. [↑](#footnote-ref-4)
5. Compare Exhibit No. \_\_\_\_ (Staff Response), pp. 12-13 with Exhibit No. \_\_\_\_ (RCC-1T), p. 27:13-22. [↑](#footnote-ref-5)
6. Exhibit No. \_\_\_\_ (Staff Response), pp. 13-14. [↑](#footnote-ref-6)
7. Exhibit No. \_\_\_\_ (RCC-1T), p. 11:4-5. [↑](#footnote-ref-7)
8. Compare Exhibit No. \_\_\_\_ (Staff Response), p. 15 with Exhibit No. \_\_\_\_ (RCC-1T), pp. 18-19. [↑](#footnote-ref-8)
9. Exhibit No. \_\_\_\_ (Staff Response), pp. 19-21. On the issue of service quality, I agree also with the additional approaches identified by the Regulatory Assistance Project, Exhibit No. \_\_\_\_ (RCC-7), p. 49. [↑](#footnote-ref-9)
10. Compare Exhibit No. \_\_\_\_ (Staff Response), pp. 9-10 with Exhibit No. \_\_\_\_ (RCC-1T), pp. 19-20. [↑](#footnote-ref-10)
11. Exhibit No. \_\_\_\_ (RCC-1T), p. 19:15-17. [↑](#footnote-ref-11)
12. Exhibit No. \_\_\_\_ (Staff Response), p. 6. [↑](#footnote-ref-12)
13. Exhibit No. \_\_\_\_ (RCC-1T), p. 12. [↑](#footnote-ref-13)
14. Exhibit No. \_\_\_\_ (Staff Response), pp. 16-19. [↑](#footnote-ref-14)
15. Exhibit No. \_\_\_\_ (RCC-1T), p. 16:10-12. [↑](#footnote-ref-15)
16. Exhibit No. \_\_\_\_ (KLE-1T), p. 81:16-18. [↑](#footnote-ref-16)
17. Docket No. U-100522, Commission’s Report and Policy Statement on Regulatory Mechanisms, Including Decoupling, to Encourage Utilities to Meet or Exceed Their Conservation Targets (Nov. 4, 2010) (“Policy Statement”), p. 19. [↑](#footnote-ref-17)
18. Exhibit No. \_\_\_\_ (RCC-1T), pp. 23:11 – 24:16 (unlike full decoupling, lost revenue recovery mechanisms are automatic rate increases that create perverse incentives to promote programs that look good on paper but deliver little or no savings in practice, while leaving unimpaired strong utility incentives to promote increased electricity use and creating automatic penalties for cost-effective savings associated with efficiency standards and effective public education campaigns). [↑](#footnote-ref-18)
19. Exhibit No. \_\_\_\_ (RCC-7), Regulatory Assistance Project, Revenue Regulation and Decoupling: A Guide to Theory and Application (June 2011), p. 49. [↑](#footnote-ref-19)
20. Exhibit No. \_\_\_\_ (KCH-3T), pp. 19-25. [↑](#footnote-ref-20)
21. Policy Statement, p. 16. [↑](#footnote-ref-21)
22. Compare Exhibit No. \_\_\_\_ (KCH-3T), p. 21:7-18 with Policy Statement, p. 18, item 1. [↑](#footnote-ref-22)
23. Exhibit No. \_\_\_\_ (KCH-3T), pp. 22-23. [↑](#footnote-ref-23)
24. See, e.g., Policy Statement, pp. 1-9, and sources cited there. [↑](#footnote-ref-24)