

BEFORE THE
WASHINGTON UTILITIES AND TRANSPORTATION COMMISSION

WASHINGTON UTILITIES AND
TRANSPORTATION COMMISSION,

Complainant,

v.

PUGET SOUND ENERGY, INC.,

Respondent.

Docket No. UE-090704

Docket No. UG-090705

INITIAL BRIEF OF NW ENERGY COALITION

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INTRODUCTION

1. The NW Energy Coalition (“Coalition”) submits this Brief related to Puget Sound Energy’s (“PSE”) general rate case.
2. We first recognize that PSE has been a leader over the past several years in acquiring cost-effective energy efficiency across all sectors of its service territory, and in supporting regional initiatives to promote this objective. The Coalition commits to work with PSE and other stakeholders to sustain and build upon the momentum that has occurred for cost-effective energy efficiency.
3. Our focus in this Brief is threefold. We address the Conservation Phase-In Adjustment (“Adjustment”) that PSE proposes. The issue here is whether the proposed Adjustment represents a proper pro forma ratemaking adjustment under the Commission’s applicable accounting rule (WAC 480-07-510(3)(e)(iii)). As discussed below, the Coalition does not take a position on this issue.
4. We then respond to PSE’s position regarding its Electric Conservation Incentive Mechanism (“Mechanism”). The Commission had authorized the Mechanism for a three-year pilot period ending December 31, 2009.¹ At hearing, however, PSE stated that it does not intend to seek continuation of the Mechanism or approval of other incentive-based approaches to increasing energy efficiency. We offer our thoughts on this decision.

¹ *WUTC v. Puget Sound Energy, Inc.*, Docket Nos. UE-060266 and UG-060267, Order 08 at ¶¶ 154-158 (January 5, 2007).

5. Finally, PSE distinguishes between regulatory mechanisms that create incentives for energy efficiency investments, and mechanisms that reduce or eliminate disincentives to making those investments (which include financial disincentives among others). We agree that this distinction exists. Though no one approach is perfect for all situations, both types of mechanisms offer the potential to increase the acquisition of cost-effective energy efficiency. We offer our perspective on how to consider these mechanisms.

**THE COALITION DOES NOT TAKE A POSITION ON WHETHER PSE'S
PROPOSED CONSERVATION ADJUSTMENT REPRESENTS A PROPER PRO
FORMA RATEMAKING ADJUSTMENT**

6. PSE's witness, Jon Piliaris, discusses the basis for the proposed Adjustment in his direct testimony. According to Mr. Piliaris, the Adjustment would, if approved, "restate the weather-normalized test year loads of the Company's retail natural gas and electric customers."² He argues that the Adjustment is a type of annualizing adjustment that the Commission generally accepts for ratemaking purposes.³

7. The issue in this proceeding is whether the proposed Adjustment represents a proper pro forma ratemaking adjustment under WAC 480-07-510(3)(e)(iii).⁴ Staff's witness,

² Piliaris, Exh. JAP-1T at 19:9-10.

³ *Id.* at 21:1-12.

⁴ In addition to his ratemaking argument, Mr. Piliaris asserts that RCW 80.28.260 provides "support" and "guidance" for the proposed Adjustment. Piliaris, Exh. JAP-1T at 23:3-9. The statute does permit the Commission to remove financial disincentives to increasing energy efficiency. But RCW 80.28.260 does not command the Commission to disregard its existing accounting rules when it evaluates a proposed regulatory mechanism. WAC 480-07-510(3)(e)(iii) remains the appropriate rule to apply in this proceeding.

Michael Parvinen, claims in his response testimony that the Adjustment does not qualify under the rule.⁵ Mr. Piliaris disagrees; he states on rebuttal that Staff's position is "novel, unsupported by existing statute, the Commission's rules or its prior orders."⁶ This dispute, then, turns on a narrow question of ratemaking accounting, *i.e.*, whether the Adjustment would give effect, under WAC 480-07-510(3)(e)(iii), to all known and measurable changes that are not offset by other factors (which is how the Commission defines a pro forma adjustment for ratemaking purposes).

8. In regulatory proceedings, the Coalition typically focuses less on the intricacies of ratemaking accounting (for which we profess no special expertise) and more on the advancement of regulatory measures that -- consistent with the Commission's established commitment to energy conservation⁷ -- serve to promote cost-effective energy efficiency and other clean and affordable energy services. Consequently, the Coalition does not take a position on whether the proposed Adjustment represents a proper pro forma ratemaking adjustment under the Commission's applicable accounting rule (WAC 480-07-510(3)(e)(iii)).

⁵ Parvinen, Exh. MPP-1T at 13:14-16.

⁶ Piliaris, Exh. JAP-5T at 2:17-19.

⁷ See generally *WUTC v. Avista Corporation, d/b/a Avista Utilities*, Docket Nos. UE-090134, UG-090135, and UG-060518, Order 10 (December 22, 2009) at ¶ 237 ("the policy of this state promotes the advancement of conservation resources"), ¶ 239 ("it is difficult to overstate the importance of conservation measures"), and ¶ 289 ("conservation is one of our cornerstone missions"); *In re Review of PURPA Standards in the Energy Independence and Security Act of 2007*, Docket No. U-090222, Order 01 at ¶ 18 (September 14, 2009) (conservation represents a "priority resource" in Washington State).

INCENTIVES REMAIN IMPORTANT TOOLS TO PROMOTE ENERGY CONSERVATION, DESPITE PSE'S DECISION NOT TO PURSUE THEM

9. The Mechanism “provides a financial incentive to the Company for energy savings from conservation programs that meet or exceed annual baseline targets set by PSE in consultation with the Conservation Resources Advisory Group (“CRAG”).”⁸ According to Mr. Piliaris, PSE earned additional revenue of \$3.45 million in 2007 and \$4.34 million in 2008 due to the Mechanism.⁹

10. At hearing, however, Mr. Piliaris indicated that PSE will not seek continuation of the Mechanism. Nor does the company intend to pursue other incentive-based approaches to the acquisition of energy efficiency. Instead, PSE will focus on recovering the costs associated with its conservation efforts.

11. The Coalition supports a utility's decision to seek timely cost recovery for energy efficiency expenditures that are prudent and cost-effective. The issue of cost recovery is important and must be resolved. But the Coalition has made clear repeatedly that a utility may need more than cost recovery in order to put energy efficiency on an equal footing with other utility expenditures and to ensure acquisition of all cost-effective energy efficiency. This is particularly important when resource acquisition levels reach substantial levels as they have with PSE.

⁸ Piliaris, Exh. JAP-5T at 14:9-12. Mr. Piliaris refers to the Mechanism in the present tense because he filed his rebuttal testimony on December 17, 2009, when the Mechanism was in effect. It expired two weeks later.

⁹ *Id.* at 14:14-16.

12. Among other measures, state policy strongly supports the use of incentives to promote energy conservation. The Washington Legislature has declared that incentives that promote conservation benefit the state’s citizens by encouraging efficient energy use.¹⁰ In approving the Mechanism, the Commission stated that “state law and policy clearly support the use of financial incentives to promote a broad array of conservation measures.”¹¹

13. Consistent with this policy direction, the Coalition advocates for regulatory strategies that, at a minimum, make utilities neutral to increases or decreases in their customers’ energy use, and ideally motivate them to support sustained investment in all cost-effective energy efficiency. Incentives that promote energy efficiency investment and reward superior performance should be considered to help level the playing field with regard to incentives that may exist for supply-side resources.

14. Our point here is that a utility decision to pursue cost recovery need not be made to the exclusion of other approaches -- including incentive measures -- that may advance energy conservation in certain situations. We encourage the Commission to continue to support the use of incentives, where appropriate, in order to promote this important objective.

¹⁰ RCW 80.24.024; *see also* RCW 80.28.260 (support for policies that provide financial incentives for energy efficiency programs) and RCW 19.285.060(4) (the Commission may consider positive incentives for a utility to exceed the conservation targets established under RCW 19.285.040).

¹¹ *WUTC v. Puget Sound Energy, Inc.*, Docket Nos. UE-060266 and UG-060267, Order 08 at ¶ 153 (January 5, 2007); *see also WUTC v. Avista Corporation, d/b/a Avista Utilities*, Docket Nos. UE-090134, UG-090135, and UG-060518, Order 10 at ¶ 237 (December 22, 2009) (the policy of Washington State “encourages the Commission to consider incentives for investment in [conservation] resources”).

**THE COALITION ENCOURAGES THE COMMISSION TO INITIATE A
RULEMAKING OR OTHER PROCEEDING, FOR THE SPECIFIC PURPOSE OF
EXAMINING DISINCENTIVES TO ENERGY CONSERVATION**

15. Mr. Piliaris distinguishes between mechanisms that create incentives for energy efficiency investments, and mechanisms that reduce or eliminate disincentives to those investments. The Mechanism was established to “*provide an incentive to conservation, but there were no illusions that it would remove disincentives. These are apples and oranges.*”¹²

16. The Coalition agrees that a distinction exists between incentive and disincentive-based mechanisms. Though no one approach is perfect for all situations, both types of mechanisms offer the potential to increase the acquisition of cost-effective energy efficiency. As we discussed earlier, there is ample reason why utilities and regulators should consider multiple approaches to enhancing energy conservation.

17. Mr. Piliaris focuses most of his rebuttal, however, on just a single regulatory approach – the removal of *financial* disincentives to utility-sponsored conservation. He argues that, “in keeping with the fundamental doctrine of setting rates to cover appropriate costs, the Commission should authorize full recovery of [PSE’s] lost margin resulting from the requirements of RCW 19.285.”¹³ Mr. Piliaris asks the Commission to “formulate clear

¹² Piliaris, Exh. JAP-5T at 16:6-8. (Emphasis added)

¹³ *Id.* at 17:17-19. The Commission has stated that, through approved conservation tariffs, it provides PSE with “timely recovery of energy efficiency-related costs in rates.” *In re Review of PURPA Standards in the Energy Independence and Security Act of 2007*, Docket No. U-090222, Order 01 at ¶ 26 and citations to PSE’s conservation tariffs at n. 38 (September 14, 2009). These tariffs provide PSE with funding for programmatic conservation efforts.

written policy and approve permanent mechanisms” that promote conservation investment and “address the issue of lost margin due to conservation.”¹⁴

18. The Coalition has several comments in response. Our first concerns are procedural. It is unclear precisely what PSE requests from the Commission. The company does not state what the “clear written policy” should encompass. Nor does PSE indicate how this policy should operate, *e.g.*, retroactively or prospectively and for what recovery amount. Except for the proposed Adjustment, the company does not define the “permanent mechanisms” that it asks the Commission to approve.

19. It is also unclear whether PSE has appropriately “teed up” the lost margin recovery issue. The other parties could not present testimony on this issue because Mr. Piliaris raised it for the first time on rebuttal. Further, the company seeks a formal policy that applies not just to PSE, but to “all jurisdictional utilities.”¹⁵ Given the dynamic that surrounds the recovery issue and the strong opinions that exist, the Commission may wish to hear from multiple utilities and stakeholders rather than just the parties to this proceeding.

20. Though PSE couches the disincentive issue as strictly a financial one, *i.e.*, the recovery of lost margin due to conservation, there is much more to the issue. Utilities face other, significant disincentives to achieving energy efficiency, most notably regulatory measures that reward increased sales, penalize sales below accepted levels, and thereby

¹⁴ Piliaris, Exh. JAP-5T at 20:12-21.

¹⁵ *Id.* at 20:15-16.

create a throughput incentive and a disincentive to utility investment in conservation. A policy that seeks to remove disincentives to conservation should address *all* potential disincentives and not just the matter of lost margin recovery.¹⁶

21. Further, there are multiple factors to consider when structuring a mechanism that removes disincentives, including financial disincentives. As one example,¹⁷ any such mechanism should be linked to a utility commitment to pursue significant energy efficiency savings. Moreover, a mechanism that permits lost margin recovery should not, in the process, erode the utility's incentive to control costs or to improve operational efficiency.

22. We raise these concerns not to make the financial disincentive issue go away, but to put the issue in proper perspective. It is one thing for PSE to argue conceptually that the Commission should adopt a policy and mechanisms that authorize full recovery of lost margin due to conservation. Ultimately, though, "the devil is in the details." The financial disincentive issue – indeed, the issue of *all* disincentives to conservation -- requires a complete review in an appropriate forum so that the Commission can flesh out these details and decide how best to proceed.

¹⁶ Decoupling can help remove the throughput incentive, for example. Recently the Commission authorized Avista to continue a partial and limited decoupling mechanism that applies to service to residential gas customers. *WUTC v. Avista Corporation, d/b/a Avista Utilities*, Docket Nos. UE-090134, UG-090135, and UG-060518, Order 10 at ¶¶ 290, 321 (December 22, 2009). PSE is free at this time to request a decoupling mechanism for residential gas and electric service. *In the Matter of the Joint Application of Puget Holdings LLC and Puget Sound Energy, Inc. For an Order Approving Proposed Transaction*, Docket No. U-072375, Order 08, Appendix A to Multiparty Settlement Stipulation (Attachment A to Order 08) at ¶¶ 62-63 (December 30, 2008) (merger commitments that apply to decoupling).

¹⁷ The factors in this paragraph are illustrative, not exhaustive. Other factors may apply depending on the nature and scope of a particular mechanism.

23. The Coalition has identified several possible avenues for this review. PSE could present the disincentive issues in its next general rate case, perhaps with guidance from the Commission resulting from the final order in this proceeding. This would address some of our procedural concerns and permit a more focused examination of the issues. By the same token, however, a delay until PSE's next rate case means that resolution of the issues may not occur for some time (which creates the potential for unnecessary regulatory lag). Further, a rate case process that is specific to PSE carries the risk that other jurisdictional utilities might not be heard. Thus, the company's next rate case may not be the ideal forum, by itself, in which to conduct a timely and global examination of disincentive issues.¹⁸

24. The Commission could also examine these issues in the three proceedings that it recently opened to consider PacifiCorp's, Avista's, and PSE's reports regarding the utilities' ten-year conservation potential and biennial conservation targets.¹⁹ The dates that the Commission scheduled in early March -- for comment and an open meeting -- suggest that the proceedings may be resolved relatively quickly.²⁰ The new proceedings are also

¹⁸ There are other potential problems with using a general rate case to conduct a focused review of disincentive issues. A rate case typically involves several "big ticket" issues including rate of return, rate base, and operating expenses. These issues are often very technical and contentious, which may serve to overshadow other issues in the case (such as energy efficiency).

¹⁹ The three proceedings are Docket Nos. UE-100170 (PacifiCorp), UE-100176 (Avista), and UE-100177 (PSE). The reports are required by RCW 19.285.040(1)(a)-(b) and WAC 480-109-010.

²⁰ See, e.g., *Notice of Opportunity to Comment and Notice of Open Meeting*, Docket No. UE-100177 (February 2, 2010) (in the case of PSE, setting March 5, 2010 as the due date for written comments on the company's report and March 11, 2010 as the date to receive oral comments). The Coalition asks the Commission to take official notice, under WAC 480-07-495(2), of the Notices that it issued on February 2, should it determine that such notice is appropriate in this proceeding.

conservation-specific; they could thus be structured to receive evidence regarding disincentives that may affect the companies' conservation estimates. Still, we are concerned that the introduction of new issues and evidence into the proceedings could delay their resolution, which in turn could delay consideration of the utilities' reports.

25. A third possibility is a rulemaking or other proceeding tailored just to disincentive issues. In such a proceeding, the Commission could seek informed comments from a variety of stakeholders. Depending on how the proceeding develops, these comments could aid the Commission in establishing specific guidelines of general applicability that are designed and intended to reduce or eliminate disincentives to energy conservation. On balance, we believe that this type of proceeding is the best way to proceed.

26. We are aware that the Commission recently terminated a rulemaking regarding energy utility standards under the Public Utility Regulatory Policies Act of 1978 ("PURPA").²¹ That rulemaking had been initiated to consider whether to implement new standards to carry out PURPA's purposes, including rate design that promotes energy efficiency investment.²² One standard (Standard 17) states in part that regulatory authorities shall, in promoting energy efficiency investments, "consider removing the throughput incentive and other regulatory and management disincentives to energy efficiency."²³

²¹ *In re Review of PURPA Standards in the Energy Independence and Security Act of 2007*, Docket No. U-090222, Order 01 at ¶ 57 (September 14, 2009).

²² *Id.* at ¶¶ 3-4.

²³ *Id.* at p. 8.

27. In Docket No. U-090222, the Commission determined that, because it had previously considered the policy options in Standard 17 – including the question of disincentive removal -- it was unnecessary to adopt the standard.²⁴ The Commission may thus decide that another rulemaking to consider disincentive issues is unnecessary. As we view last year’s decision, however, the Commission acted simply to determine whether further regulatory standards were appropriate under PURPA. The decision does not preclude another rulemaking or other proceeding for the specific purpose of assessing disincentives to conservation and developing solutions to them, in the context of the current economic and regulatory climate in Washington State. Such an outcome would help address and settle the disincentive issues that PSE raises in this proceeding.

CONCLUSION

28. The Commission has affirmed that conservation represents a “priority resource” and that “it is difficult to overstate the importance of energy conservation measures.”²⁵ To fully achieve the benefits of conservation, however, it is necessary to consider different regulatory approaches – including measures that incent increases in energy efficiency *and* remove disincentives to conservation investment. These approaches are important in order to (1) promote policy objectives in Washington State; (2) increase the acquisition of energy

²⁴ *Id.* at ¶¶ 25, 27.

²⁵ *Id.* at ¶ 18; *WUTC v. Avista Corporation, d/b/a Avista Utilities*, Docket Nos. UE-090134, UG-090135, and UG-060518, Order 10 at ¶ 239 (December 22, 2009).

efficiency; (3) help utilities meet and exceed their obligations to obtain available conservation; and (4) ensure that customers benefit by receiving the most cost-effective resources to meet their energy needs.

29. The Coalition has attempted, in this Brief, to take a fair and balanced approach to the issues that PSE has raised. They merit a complete review in an appropriate proceeding. We urge the Commission to consider the procedural options we have laid out so that these issues can be heard, developed, and resolved at the earliest opportunity. It is critically important that this process occur so that PSE and other utilities can build upon their successes, and energy conservation can continue to flourish in Washington State.

Dated this 19th day of February, 2010.

NW ENERGY COALITION

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