BEFORE THE WASHINGTON STATE
UTILITIES AND TRANSPORTATION COMMISSION

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

POST-HEARING BRIEF OF
NW ENERGY COALITION

March 16, 2012

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INTRODUCTION

1. More than twenty years ago, the Washington Utilities and Transportation Commission ("Commission") approved a decoupling mechanism for Puget Power, the forerunner of Puget Sound Energy ("PSE"). Much has changed in the last two decades, but not the fundamental proposition that, in order to achieve ambitious conservation goals, we must, as a society, not just encourage energy efficiency measures, but also remove mechanisms that discourage energy efficiency. The link between higher consumer energy use and utilities' financial health is one barrier to increased energy conservation recognized by the Commission. Indeed, in the context of this general rate case, the Commission specifically requested its Staff to "examine full decoupling, as discussed in the Decoupling Policy Statement, as an option for PSE." Notice of Bench Request (Oct. 5, 2011) at 2. In response to the Bench Request, intervenor NW Energy Coalition ("Coalition") used its testimony to:

> bring forward solutions to the barriers to energy efficiency progress that are fundamentally captured by the continuing reality for Puget, for Avista, for most of the electric utilities in the country, that their financial health is tied directly to kilowatt hour sales, that increases in sales are automatically more profitable than reductions, that there is implicit in our traditional form of utility regulation a throughput addiction which we would never have introduced consciously or deliberately if we had as an initial objective arming and encouraging our utilities to secure all cost effective energy efficiency.

Testimony of Ralph C. Cavanagh, TR. 430:2-14. The bulk of this post-hearing brief addresses the concept of decoupling, reasserting the need for it in Washington and responding to criticism of the Coalition's proposal—criticisms that might carry more weight if they were more than a reflexive "that's not the way we do things here" response.

2. Additionally, this brief addresses why PSE should not be penalized for its early renewable energy acquisition with the Lower Snake River wind project. Early acquisition of renewable energy sources not only makes sense for the company, but also provides regional

benefits. For these reasons, the Coalition supports PSE's investment in the Lower Snake River wind project. For similar reasons of promoting renewable energy sources and properly weighing the true costs of energy from more traditional sources, the Coalition also supports the Sierra Club's proposal for examination of Colstrip, particularly because no other forum, including the PSE Integrated Resources Planning ("IRP") process, allows for the exchange and analysis of confidential information. Finally, as an organization with a founding principle of ensuring low-income energy services, and as one of the negotiators of PSE's original low-income bill assistance program, Docket No. UE-011570/UG-011571, Settlement Stipulation, Exh. G (June 6, 2002), the Coalition supports The Energy Project's low-income proposal.

ARGUMENT

I. THE COMMISSION SHOULD ADOPT A FULL ELECTRICITY DECOUPLING MECHANISM FOR PSE.

3. Under traditional regulation, recovery of authorized nonproduction costs is directly linked to commodity sales, encouraging increased use and discouraging investments in energy efficiency programs, peak load pricing, and distributed generation that may reduce electricity throughput. Utilities are discouraged from investing in the best performing and lowest-cost resource—energy efficiency—because it hurts them financially. Utilities' interest in increasing sales conflicts with customers' interest getting more work out of less energy.

4. Full decoupling is a simple, effective, and proven way to remove that conflict. Full decoupling breaks the link between the utility's recovery of nonproduction costs and the amount of energy it sells, using modest periodic adjustments in rates to ensure that the utility collects no more and no less than its authorized nonproduction costs, regardless of changes in retail electricity sales. Combined with other policies to encourage energy efficiency, such "full decoupling" mechanisms free utilities to help customers save energy whenever it is cheaper than

producing and delivering it.

5. Full decoupling meets the legal standard before the Commission in this general rate case, in that it increases the extent to which the rates and charges proposed by PSE will be fair, just, reasonable, and sufficient. RCW 80.28.020; *People's Org. for Wash. Energy Res. v. WUTC,* 104 Wn.2d 798, 808 (1985).

6. In summary, the Coalition proposes "essentially that only those portions of nonproduction fixed costs that are captured in variable charges would be included in the decoupling mechanism. For a company with about a $2.1 billion revenue requirement, we're talking about roughly $500 million of nonproduction costs that are now being recovered in variable charges. The mechanism would use those costs in the same way basically that Puget does for its [proposed] conservation savings adjustment, except that unlike the Puget proposal, ours is a true-up mechanism that can move rates either up or down, depending on total consumption, [with] a rate cap of three percent a year, that's on the upside, no constraint on the down side reductions. And there will be both. The mechanism doesn't add costs to Puget's revenue requirement, it simply provides that the revenue requirement you [the Commission] adjudicate will be recovered independent of fluctuations in sales." Cavanagh, TR. 431:15-432:6.

A. A Brief History of Decoupling in Washington.

1. 1991 Puget Power Ruling

7. The Commission approved a decoupling mechanism based on a per-customer revenue cap mechanism for Puget Power in 1991. As the Commission determined at that time:

> [T]he revenue per customer mechanism does not insulate the company from fluctuations in economic conditions, because a robust economy would create additional customers and hence, additional revenue. Furthermore, the Commission believes that a mechanism that attempts to identify and correct only for sales reductions associated with company-sponsored conservation programs may be unduly difficult to implement and monitor. The company would have an

> incentive to artificially inflate estimates of sales reductions while actually achieving little conservation.

Docket No. UE-901183-T, Third Supplemental Order (Apr. 10, 1991), p. 10. *See generally* Prefiled Direct Testimony of Ralph C. Cavanagh, Exh. RCC-1T at 3. In its initial 1993 review of the mechanism, the Commission "accept[ed] the parties' representations" that the revenue-per-customer cap had "achieved its primary goal—the removal of disincentives to conservation investment," and concluded that "Puget has developed a distinguished reputation because of its conservation programs and is now considered a national leader in this area." Docket No. UE-920433, Eleventh Supplemental Order (Sept. 21, 1993), p. 10. Although this first decoupling mechanism lasted only a few years, its demise arose from other concerns. *See* Cavanagh, Exh. RCC-1T at 3-4; *see also* Cavanagh, TR. 438:17-439:3 ("CHAIRMAN GOLTZ: Okay. And isn't it a little bit of we've been there done that? … So what's different now? THE WITNESS [Mr. Cavanagh]: So first of all, Mr. Chairman, by consensus at the time, the decoupling mechanism itself, I think it's fair to say, was tremendously successful. And in the aftermath of my testimony in 1993 the Commission extended the mechanism. What was not successful and not popular were other elements to which the mechanism was attached.").

8. When the Commission terminated its 1991 system of rate adjustment mechanisms, the Commission expressly reserved the right of all parties to bring forward in the future "other rate adjustment mechanisms, including decoupling mechanisms, lost revenue calculations, [and] similar methods for removing or reducing utility disincentives to acquire conservation resources." Docket No. UE-921262, Joint Report and Proposal Regarding Termination of the Periodic Rate Adjustment Mechanism (April. 20, 1995), p. 4-5.

2. *The Commission's 2010 Decoupling Policy Statement*

9. The most important development, however, is the Commission's Report and Policy

Statement on Regulatory Mechanisms, Including Decoupling, to Encourage Utilities to Meet or Exceed Their Conservation Targets ("Decoupling Policy Statement"). Docket No. U-100522 (Nov. 4, 2010). The Decoupling Policy Statement expresses the Commission's commitment, "[i]n the context of a general rate case," to "consider a full decoupling mechanism for electric and natural gas utilities, which will allow a utility to either recover revenue declines related to reduced sales volumes or, in the case of sales volume increases, refund such revenues to its customers." *Id.* at 17. The Commission's Decoupling Policy Statement concludes that "while a close call, we believe that a properly constructed full decoupling mechanism that is intended, between general rate cases, to balance out both lost and found margin from any source can be a tool that benefits both the company and its ratepayers." *Id.* at 16. The Commission's Policy Statement also recognizes that Washington's adoption of I-937 and its conservation mandates does not moot the decoupling issue. *Id.* at 19 (concluding that the Commission welcomed full decoupling proposals as consistent with the I-937 mandate).

10. The Coalition's decoupling proposal is founded on the Commission's Decoupling Policy Statement. Cavanagh, TR. 429:15-23 ("And that's the context in which the NW Energy Coalition brings to you today a proposal for addressing a fundamental and long-standing obstacle to aggressively accelerated progress on energy efficiency. That proposal comes directly in the wake of this [C]ommission's November 2010 policy statement on regulatory mechanisms, including decoupling, to encourage utilities to meet or exceed their conservation targets. And every part of the proposal is informed by that statement.").

B. The Coalition's Decoupling Proposal

1. The Basics of the Coalition's Proposal

11. The Coalition proposes a straightforward form of per-customer decoupling based on the nonproduction costs approved in this proceeding (except for those covered in the Power Cost

Adjustment ("PCA") mechanism), with annual reconciliations of actual to authorized nonproduction cost recovery and subsequent rate true-ups for all participating customer classes. Any associated annual rate increases would be capped at 3 percent (no limit on reductions), with unrecovered balances carried forward. The Coalition also recommends that the Commission adopt two per-customer nonproduction cost revenue requirements, one covering the residential class and the other representing a weighted average for all other classes included in the mechanism. The Coalition's proposal does not treat new and existing customers differently, and the Coalition proposes to include all but a few classes of customers (with excluded classes providing only about 4% of the utility's nonproduction cost revenue requirement through their variable charges). *See* Cavanagh, Exh. RCC-1T at 9-10 (calculation of revenue per customer relies on PSE's calculations for its proposed Conservation Savings Adjustment); Cavanagh, TR. 431:21-432:6 (up or down nature of rates under decoupling's annual true-up); Cavanagh, Exh. RCC-1T at 11 (reasoning for two classes of revenue requirements); *id.* at 12-13 (explanation for 3% upward cap); *id.* at 13 (excluding only a few customer classes due to small number of class members); *id.* at 14 (new/existing customers treated the same).

2. *The Coalition's Proposal Does Not Contemplate a Reduction in PSE's Return on Equity Because There Is No Competent Evidence for Such an Up-Front Reduction.*

12. The Coalition's decoupling proposal does not include an up-front reduction in PSE's return on equity ("ROE"), instead proposing 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)." Cavanagh, Exh. RCC-1T at 19. The parties that oppose decoupling have asserted that a decoupling mechanism, because it may enhance PSE's ability to predict earnings (and thus lower risk to the company), should be accompanied by a reduction in ROE. Yet no party produced any evidence to support a specific

amount of ROE reduction, let alone counter the Coalition's proposal to revisit the ROE issue after decoupling has been in place and working for five years. Cavanagh, Exh. RCC-1T at 20-21. Chairman Goltz raised the lack of evidence for a ROE reduction with Mr. Gorman, witness for the Industrial Customers of Northwest Utilities ("ICNU"), at the hearing before the Coalition's decoupling witness took the stand:

> THE WITNESS [Mr. Gorman]: If you significantly modify regulatory mechanisms to stabilize earnings and cash flow, and that is produced by implementing regulatory mechanisms which throw more stability in the rates customers pay, I think a lower return on equity is fair.
>
> CHAIRMAN GOLTZ: And then is that two-tenths of one percent difference, is that just a kind of a gut level number, or is there something about some deeper analysis that you went through for that?
>
> THE WITNESS [Mr. Gorman]: It's largely a gut level reaction.

Gorman, TR. 424:9-18.

13. As explained by Mr. Cavanagh, rate impacts as modest as those associated with full decoupling for PSE do not imply appreciable consequences for company-wide cost of capital. Cavanagh, Exh. RCC-1T at 20; *see also* Lesh, Pamela G. *Rate Impacts and Key Elements of Gas and Electric Utility Decoupling* (June 30, 2009), Exh. RCC-5 at 4 (summary); Cavanagh, TR. 437:13-16 ("decoupling mechanisms have minimal effect in practice, because they don't move enough money to matter much from the standpoint of the entire utility's finances."). However, the Coalition's proposal ensures that any actual savings are passed through to customers if, as others predict, decoupling helps lay a foundation for cost-reducing changes in PSE's capital structure.

3. The Coalition's Proposal Follows the Commission's Decoupling Policy Statement and Washington State Policy Concerning Efficiency and Transportation.

14. The Coalition's decoupling proposal is the only proposal before the Commission that

responds to and incorporates the elements of the Commission's Decoupling Policy Statement.[1] In opposition, PSE asserts that this alignment is inconsequential because the Decoupling Policy Statement is non-binding. Prefiled Rebuttal Testimony of Tom DeBoer, Exh. TAD-4T at 5. While the Commission's Decoupling Policy Statement is clearly not a formal rule or order, it represents the direction the Commission has decided to go. The Coalition has not blindly argued that the Commission disapprove PSE's Conservation Savings Adjustment ("CSA") proposal because it does not comply with the Commission's policy; for the various reasons highlighted in Mr. Cavanagh's testimony, Cavanagh, Exh. RCC-1T at 23-24, the Coalition does not support lost margin recovery mechanisms.[2] Simply put, the Commission should adopt the Coalition's proposal because full decoupling will further the Commission's energy conservation goals.

15. PSE also argues that Washington's 2012 State Energy Strategy, which stresses a need to reduce fossil fuel use generally and in transportation in particular, would be harmed by decoupling. DeBoer, Exh. TAD-4T at 9-10. There are at least three fundamental flaws with this argument. First, there is no evidence in the record or elsewhere that decoupling would make PSE reluctant to sell more electricity for electric vehicles should that sector start to expand. Indeed, there is no real expectation of increased electricity sales for electric vehicles in the near future:

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[1] Commission Staff also discussed the mechanics of a full decoupling mechanism in Staff's response to the Commission's Bench Request on decoupling, although Staff did not propose that the Commission adopt such a mechanism. *See* UTC Staff Response, Bench Exh. 3 (also admitted as Exh. JAP-40 CX). Like the Coalition's proposal, Staff's mechanism incorporates many elements from the Commission's Decoupling Policy Statement—indeed, Staff and the Coalition appear largely to agree on how many elements of a decoupling mechanism should be structured for PSE. *See generally* Prefiled Cross-Answering Testimony of Ralph C. Cavanagh, Exh. RCC-6T at 3.

[2] Nor, apparently, does the Commission for electric utilities. *See* Decoupling Policy Statement at 7-8.

> COMMISSIONER JONES: Can you share with me any of your projections for electric vehicles in your service territory, either by vehicle numbers or percent of load for the next five, ten years?
>
> THE WITNESS [DeBoer]: No, I don't have those numbers, but—in a quantitative sense. In qualitative, we don't expect it to be a huge load builder, as far as electric load in the near future.

Testimony of Tom DeBoer, TR. 546:22-547:4; *see also* Cavanagh, TR. 446:16-447:11 (reviewing PSE projections that under the most aggressive scenario, vehicle electrification is not expected to constitute even one percent of systemwide load before 2030). The Coalition hopes to promote energy efficiency for all uses, and its decoupling proposal is fully consistent with Washington State policy. Cavanagh, TR. 445:21-25 ("Decoupling certainly will not penalize Puget for supporting vehicle electrification any more than it penalizes Puget for promoting efficiency in any other end use. We support this. We're not against vehicle electrification."). There is no reason to give PSE a financial stake in minimizing the operating efficiency of electric vehicles connected to its system, which is precisely what would result in the absence of full decoupling. Indeed, without full decoupling, increased vehicle electrification is like all other uses: the less efficient it is (and the more energy it uses), the more PSE profits.

16. Second, PSE's argument about electric vehicles explicitly exposes what had been an implicit PSE argument before—that PSE opposes decoupling because it wants to keep the found margin from greater electricity sales:

> CHAIRMAN GOLTZ: Right. The problem is that when people go out and buy a big screen TV, or multiple appliances, and their use per customer increases, the problem is that under Mr. Cavanagh's proposal that would end up with a lowering of the rates to customers. In other words, you wouldn't get what's sometimes called found margin.
>
> THE WITNESS [DeBoer]: Correct.
>
> CHAIRMAN GOLTZ: Is that the nub of the concern of Mr. Cavanagh, the decoupling mechanism?

> THE WITNESS [DeBoer]: Yes. Because it breaks sort of the historical pact between why rate making—as I covered in my testimony, in order for historical rate making to work, *you had to have that increasing use and use per customer* in order to match the revenues that you have in the historical test year to allow you the opportunity to earn your rate of return in the rate year.

DeBoer, TR. 527:9-528:1 (emphasis added). Mr. DeBoer's testimony highlights precisely the reason why the Commission should adopt full decoupling for PSE—decoupling eliminates the admitted incentive for the utility to *increase* electricity use per customer. Allowing PSE to keep found margin from increased electricity sales simply reaffirms the incentive to sell more per customer and not conserve. *See also* Cavanagh, TR. 473:17-25 ("Historically utilities have done very well by linking their financial health to increases in electricity use. You are taking that away. You are eliminating—this is—the howls of anguish about vehicle electrification are in part an echo of this; an understanding that, my gosh, maybe something will happen to boost electricity sales, wouldn't it be best to have a piece of that action.").

17. PSE's belief in an "historical pact" that balances the alleged downside of historical test period use with the upside of found margin, *see* DeBoer, Exh. TAD-1T at 13-14, is unjustified. Staff witness Kenneth Elgin defined PSE's complaints about its rate of return as attrition: "the term typically [] used to refer [to] the erosion of a company's rate of return over time when the historical test period relationship in revenues, expenses, and rate base accepted by the Commission in a rate case does not hold during a future rate year." Prefiled Testimony of Kenneth L. Elgin, Exh. KLE-1T at 64. Mr. Elgin detailed a long history of attrition issues being brought before the Commission, *id.* at 64-68, as well as describing inherent problems with future test period use, *id.* at 68-69, and rejecting the contention that the effects of attrition are always "bad." *Id.* at 70-71. The picture painted by Mr. Elgin is not one of an historical pact where the "minus" of historical test year use is balanced by the "plus" of found margin.

18. And even if such an implicit pact existed, two wrongs simply do not make a right, and

those supposed wrongs do not add up to a reason to reject decoupling. A full decoupling proposal does not, and is not meant to, address PSE's attrition concerns. Decoupling is not a magic bullet for all of a company's financial concerns, a fact recognized by the Commission in its Policy Statement when it explicitly noted that other mechanisms, including an attrition adjustment, could be appropriate to address lost margin for reasons *beyond* costs due to energy efficiency measures:

> The guidance provided in this policy statement does not imply that the Commission would not consider other mechanisms in the context of a general rate case, including an appropriate attrition adjustment designed to protect the company from lost margin due to any reason.

Decoupling Policy Statement at 22. Instead, decoupling breaks the link between increased electricity sales and a company's financial health; decoupling removes the structural disincentive against increased energy conservation. As the only true decoupling proposal on the table, the Coalition's proposal "wouldn't widen any such [revenue] gap compared to the status quo, because … the company's customer growth rate has been about the same as its rate of growth in retail sales over the last decade (and [this] proposal substitutes customer count for retail sales as the basis on which nonproduction cost recovery changes between rate cases)." Cavanagh, Exh. RCC-1T. at 10.

19. Finally, the 2012 State Energy Strategy, issued after the Commission's Decoupling Policy Statement, explicitly acknowledges the Policy Statement and yet in no way suggests that it is inconsistent with the Strategy's various recommendations about electric vehicles. *See* 2012 Washington State Energy Strategy, *available at* http://www.commerce.wa.gov/site/1327/default.aspx, at 148. PSE's argument that decoupling is contrary to Washington State policy is simply incorrect.

4. *Decoupling Can Help Stabilize and Enhance Pursuit of Energy Efficiency as Required by the Energy Independence Act.*

20. The Energy Independence Act requires qualifying utilities to "pursue all available conservation that is cost-effective, reliable, and feasible."[3] RCW 19.285.040(1) To fully achieve the goals of the Act, financial barriers to utility pursuit of energy conservation must be removed. Cavanagh, Exh. RCC-1T at 8-9. This conclusion was underscored during PSE's 2010-2011 biennial conservation target filing. Docket No. UE-100177. Initially, PSE proposed a ten-year conservation potential and two-year target range (69-90 aMW) consistent with its analysis in its IRP. One month later, PSE filed a substantially reduced target based on its share of the Northwest Power and Conservation Council's Fifth Power Plan (43 aMW). PSE argued that there were four drivers motivating the Company to use the Council's Fifth Plan, including uncertainty about its ability to recover lost margins from conservation. DeBoer, TR. 518:19-20 (admitting that one of the reasons for the change in 2010 was concern over lost revenues due to conservation); Docket No. UE-100177, PSE Motion for Summary Determination at 4, ¶ 14 (April 6, 2010). *See also* Cavanagh, TR. 460:2-461:19 ("COMMISSIONER OSHIE: And I know that that was what they believed to be achievable. In other words, that was a safe target for them to meet, and I would assume based on your testimony that if we employed your mechanism, that we would get closer in that particular situation to a result of 72 average

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[3] This standard pushes utilities in Washington to constantly improve their energy conservation efforts. *See* Cavanagh, TR. 458:16-22, 459:5-18 ("COMMISSIONER OSHIE: [I] wanted you to talk about the relationship between conservation, which has the impact—all cost effective conservation. Perhaps I'm not satisfied that it's one percent of any utility's load, that it can be more, particularly with what the Power Council describes as its potential for the Northwest. … THE WITNESS [Mr. Cavanagh]: Oh, I think that's right. In the sixth power plan, for example, the Council proposes to meet 85 percent of regional load growth through cost effective efficiency and the rest with renewables. … I think it's the ultimate objective embedded in many parts of Washington state energy policy. But what is I think appealingly different about the way we've always handled efficiency, we've never set a quota. … We said all cost effective energy efficiency. I think that's the right objective from a public policy perspective.").

megawatts, not at the low—I believe it was actually average of 42 average megawatts during that particular year. THE WITNESS [Mr. Cavanagh]: And, Commissioner, I remember this vividly. And I'm glad you raised it. The NW Energy Coalition had a fight with Puget two years ago over targets. And the target that Puget proposed—Puget didn't adopt the Council's sixth power plan target. Puget tried to go back to the fifth power plan. It made a difference of 50 percent in the target. I would argue that that's at least in part a function, I bet Puget would agree, of the incentives being out of alignment….").

21. The Commission ultimately approved a 2010-2011 conservation target of 71 aMW based on PSE's IRP. Yet PSE's financial barriers have yet to be addressed. While PSE is a recognized leader in conservation, *see* DeBoer, Exh. TAD-1T at 2-3, the Company will not be fully motivated to sustain this leadership unless and until it has more certainty about its ability to recover lost margins due to conservation. The Coalition's decoupling proposal is geared towards overcoming this barrier and ultimately ensuring that the policy goal of the Energy Independence Act to increase energy conservation is realized.

5. Any Decoupling Order From the Commission Should Include a Requirement to Evaluate the Mechanism, Including Impacts on Low-Income Consumers.

22. Finally, the Coalition's decoupling proposal includes a strong recommendation for an independent evaluation of the mechanism in year five, based on the first four years of data.[4] Cavanagh, Exh. RCC-1T at 18-19. That evaluation should include a detailed analysis of the positive and negative impacts of the decoupling mechanism on low-income customers.

23. In line with the Decoupling Policy Statement, the evaluation should also assess whether,

[4] An evaluation of the first four years of data ensures an opportunity for the Commission to consider extending the decoupling mechanism after its initial 5-year life without a potentially confusing temporary break in application of the mechanism.

for the duration of the mechanism, PSE's conservation programs provided benefits to low-income customers roughly comparable to other customers. Staff Witness Deborah Reynolds acknowledged the lack of information available to address decoupling's effect, if any, on low-income customers. *See* Testimony of Deborah J. Reynolds, TR. 762:2-10 ("I would agree that there's limited or no information available." Q. "Thank you. Given that there is a lack of information currently, would you agree that if the Commission were to order some sort of decoupling or limited decoupling, that we should also evaluate those impacts on low-income consumers after the mechanism is in place?" A. "I would agree with that."); *see also* Prefiled Cross-Answering Testimony of Deborah J. Reynolds, Exh. DJR-3T at 17:13-14. The evaluation should assess whether increases in energy efficiency program budgets for low-income customers were at least roughly proportional to increases in funding for energy efficiency programs for other residential customers. Cavanagh, Exh. RCC-1T at 18. Because comparable spending may not equate to comparable benefits in part because "low-income customers may respond differently to conservation programs than other residential customers," Prefiled Cross-Answering Testimony of Andrea C. Crane, Exh. ACC-5T at 6-7, the proposed evaluation should look beyond solely program budgets when determining proportional benefits. Cavanagh, TR. 435:8-19 ("I don't think we have a record based on the current reporting for energy efficiency programs, certainly for Puget, to determine whether there are currently proportional benefits being delivered, and our proposal includes a specific element aimed at overcoming that problem and making sure that we get that information as quickly as possible. And I want on that point to be clear [that the Coalition] strongly supports the Commission's objective of proportional benefit for low income customers and is eager to see that objective achieved.").

C. No Other Party Submitted a Decoupling Proposal.

24. The Coalition is the only party that has responded to the Commission's Policy Statement

and Bench Order with a full decoupling proposal that breaks the link between the company's sales and its financial health. *See generally* Cavanagh, TR. 428-433. Other parties have proposed a variety of different mechanisms to address, at least in part, PSE's lost revenue due to energy efficiency, including Staff's expedited rate case mechanism, Kroger's straight fixed cost variable design, and PSE's CSA, but none of these mechanisms alter the fundamental problem that decoupling seeks to address: the disincentive to conserve created by a throughput-based cost recovery system and the importance of eliminating it without reducing customers' rewards for saving energy. While PSE is an acknowledged leader in energy efficiency efforts, it is not immune to throughput incentives. Cavanagh, TR. 460-461 (exchange with Commissioner Oshie about prior conservation targets being low-balled by PSE). Accordingly, each of these proposals fails to address the issue that is at the heart of the Commission's Policy Statement: the need to remove barriers to increased energy efficiency. Decoupling Policy Statement at 1-2. Additionally, each of the proposals either creates additional and unintended adverse impacts on conservation or sweeps in issues beyond the effects of energy efficiency on company revenue.

1. Kroger's Straight Fixed Cost Variable Design Proposal

25. Kroger proposes to change the company's rate design so that all nonproduction costs are recovered in a fixed charge, with the variable charge including only the incremental cost of additional energy sold. Prefiled Response Testimony of Kevin C. Higgins, Exh. KCH-3T at 22-23. The failing of this proposal, however, is that it reduces customers' incentives to save because efficiency improvements will have a substantially lower effect on their bill. Full decoupling, on the other hand, leaves intact customers' incentive to conserve[5] while also

[5] The Coalition's decoupling proposal preserves customers' incentive to save because lower use will result in lower charges. While rates will fluctuate under this proposal, these fluctuations will be minor—no more than 3% in either direction. Minor rate fluctuations will not break the relationship between consumer savings and total charges: consumers who save will still be

removing the company's disincentive to promote energy efficiency.

2. *Staff's Attrition/Yearly Rate Case Proposal*

26. Staff's proposed expedited rate case mechanism is likewise inadequate. Cavanagh, RCC-6T at 6-7. Staff's proposal does nothing to break the link between the company's sales and profits, and so leaves in place a powerful financial disincentive for the company to increase its energy efficiency efforts. And while Staff suggests that its proposal is simpler to implement than full decoupling, precisely the converse is true: as the Commission well knows, rate cases involve a tremendous commitment of time and resources from the company, the Commission, and all parties—even a rate case that addresses fewer issues still would be a substantial and complex undertaking. To adopt a plan that increases the frequency of rate cases would significantly drain the resources of all involved. Full decoupling, on the other hand, requires no such resource commitment to implement.

27. Staff's expedited rate case mechanism also addresses much more than just the effects of energy efficiency—instead, such a mechanism would correct for all causes of attrition. *See* Elgin, Exh. KLE-1T at 81. By sweeping so broadly, Staff's proposal misses the fact that breaking the throughput incentive is essential for energy efficiency, though not for other causes of attrition. If, as PSE and Staff assert, other causes of attrition merit attention in this rate case, they can and should be addressed separately from energy efficiency—for example, through a carefully constructed attrition adjustment that does not include the effects of energy efficiency, *see id.* at 79. There is no need to address energy efficiency and other possible causes of attrition in one mechanism, and every reason not to—because only full decoupling removes the throughput incentive.

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rewarded with a lower bill.

3. PSE's Lost Margin Recovery Mechanism

28. The Commission should not approve PSE's CSA because it is admittedly not a decoupling mechanism; the CSA does nothing to remove the throughput incentive associated with energy sales. Simply put, the CSA will pay PSE the nonproduction costs it determines to have been lost as a result of electricity savings achieved by its energy efficiency programs. Prefiled Direct Testimony of Jon A. Piliaris, JAP-1T at 32-43.[6] PSE's CSA would result in automatic penalties, in the form of reduced nonproduction cost recovery, for all cost-effective electricity savings not directly associated with "the load reducing impacts of Company-sponsored energy efficiency." *Id.* at 32. Most importantly, the CSA would leave unimpaired strong utility incentives to promote increased electricity use, since unlike the Coalition's full decoupling proposal, PSE would keep any nonproduction cost recovery in excess of that authorized by the Commission (except to the extent that the resulting gains exceeded PSE's proposed earnings limit). *See* Response to ICNU Data Request No. 02.17, Exh. TAD-13 CX (PSE's CSA "could reasonably be characterized as a lost revenue adjustment mechanism"). "Paying utility bonuses for both increases in its retail electricity sales and its programmatic electricity savings is the metaphorical equivalent of encouraging the CEO to drive with one foot on the brake and the other on the accelerator." Cavanagh, Exh. RCC-1T at 24. Finally, the CSA would yield an automatic rate increase whenever it was applied, whereas rate adjustments under full decoupling can be either positive or negative. Cavanagh, TR. 454:11-16 ("I think the other

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[6] PSE's CSA proposal was surely not named with an eye toward accurately reflecting its purpose to consumers. Under PSE's proposal, consumers would see a regular, reoccurring charge on their bill for "conservation savings," no matter how much energy they themselves saved. Indeed, the adjustment for conservation savings would never go down; more energy saved by consumers would result in higher bills to consumers. Cavanagh, TR. 454:3-16 ("COMMISSIONER OSHIE: [I]s your proposal better than Puget's because if you accept that if people understand that if because of the CSA if they invest in conservation their rates are going to go up directly because of their savings? THE WITNESS [Mr. Cavanagh]: Yes….").

perhaps decisive difference is that Puget's proposal is an automatic rate increase every year, assuming that Puget is minimally meeting its conservation goals, and our proposal can move rates in either direction.").

29. Moreover, PSE's CSA apparently suffers from the same limitations that PSE cites when attacking decoupling. PSE claims to be losing money due to its conservation efforts, but it also submits that it is losing money because its costs per customer are increasing faster than its revenue requirement. Response to Public Counsel Data Request No. 242, Exh. JAP-45 CX ("…PSE's energy efficiency programs are not the sole cause of expense per customer growing faster than revenue per customer…."). Decoupling does not address the latter problem, and yet apparently neither does the CSA. Witnesses for PSE made it clear that the CSA was designed to address only financial harm caused by its conservation efforts. *See* Testimony of Jon A. Piliaris, TR. 635:1-4 (Q. "Is the CSA designed to address financial harm to Puget Sound Energy caused by factors beyond its conservation efforts?" A. "No."); *id.* at 635:10-13 ("the CSA "only addresses the reductions in revenue associated with Company-sponsored conservation. It does not in any way take into consideration the growth and expenses for the Company outside of the earnings test.").

30. In sum, only the full decoupling mechanism proposed by the Coalition removes structural barriers to increased energy efficiency while leaving intact customer incentives to save and allowing the company the opportunity to earn its authorized rate of return. PSE's CSA, Staff's yearly rate case mechanism, and Kroger's straight fixed variable rate design all fail to align incentives to promote energy efficiency, either by leaving in place the throughput incentive or by removing customer incentives to conserve. To the extent that the company is experiencing attrition due to causes other than increased efficiency, such rising costs per customer can and

should be dealt with separately. Accordingly, the Commission should approve the Coalition's decoupling proposal and require PSE to submit a compliance filing that takes into account the final revenue requirement approved in this case.

II. EARLY ACQUISITION OF WIND RESOURCES, SUCH AS PHASE 1 OF THE LOWER SNAKE RIVER WIND PROJECT, OFFERS SIGNIFICANT BENEFITS TO PSE AND CUSTOMERS.

31. PSE has invested in early acquisition of wind resources to take advantage of significant federal incentives, secure compliance with state renewable portfolio standards ("RPS"), and reduce its exposure to the substantial financial risks associated with fossil-fuel-fired electricity generation. In this proceeding, PSE has requested a determination from the Commission that its investment in Phase 1 of the Lower Snake River wind project ("LSR 1") was prudent.

32. Commission Staff and most of the intervening parties agree that it was; only Public Counsel and ICNU challenge PSE's decision. Witnesses for the Coalition, Sierra Club, and other parties have demonstrated, however, that PSE's assumptions underlying its decision to invest in the early acquisition of wind were entirely reasonable.[7]

33. Public Counsel and ICNU's challenge to PSE's acquisition of Phase 1 of the Lower Snake River wind project rests on the testimony of Scott Norwood. In his pre-filed testimony, Mr. Norwood criticized the assumptions underlying PSE's decision to acquire LSR 1 and attempted to show that reliance on a different set of assumptions would have led PSE to the conclusion that acquisition of LSR 1 was not warranted. *See* Prefiled Direct Testimony of Scott Norwood, Exh. SN-1CT. As numerous other witnesses demonstrated, however, the assumptions underlying PSE's decision to acquire LSR 1 were reasonable at the time they were made and

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[7] The Coalition has not taken a position on PSE's rate request, but the Coalition supports the early acquisition of renewables. To that end, the Coalition submitted testimony demonstrating that the assumptions underlying PSE's decision to acquire LSR 1 were reasonable. *See* Prefiled Cross-Answering Testimony of Megan Walseth Decker, Exh. MWD-1T.

were consistent with the assumptions made by other utilities in the same time period. *See generally* Prefiled Cross-Answering Testimony of Megan Walseth Decker, Exh. MWD-1T; Prefiled Direct Testimony of Ezra D. Hausman, Exh. EDH-1T; Prefiled Cross-Answering Testimony of David Nightingale, Exh. DN-2T.

34. For example, Mr. Norwood argued that PSE did not need to acquire LSR 1 to comply with the Renewable Portfolio Standard of Washington's Energy Independence Act, RCW 19.285.040(2)(a). But even if it might have been feasible for PSE to meet its obligations under the Energy Independence Act by purchasing unbundled renewable energy credits ("REC") or by relying on carry-over provisions, such a strategy offered PSE only temporary compliance and carried the risk that a later acquisition of eligible renewable resources would come at a significantly higher price. More importantly, the core mandate of the RPS requirement in the Energy Independence Act focuses on long-run physical compliance with annual targets, requiring sufficient generating resources or REC contracts to be in place as of January 1 of each target year. Decker, Exh. MWD-1T at 4. The REC carry-over provision was not intended to allow utilities to delay compliance with the law; rather, it allows utilities some flexibility to respond to uncertain load growth or other needs. It was entirely reasonable for PSE to seek to achieve the Act's core goal by increasing renewable generation capacity. *See* Decker, Exh. MWD-1T at 3-5. Similarly, PSE's assumptions regarding the potential expiration of the federal production tax credit and carbon prices were reasonable at the time they were made. *See id.* at 11-20.

35. PSE's decision to acquire renewable resources provided another significant benefit that Mr. Norwood failed to recognize: increasing renewables in PSE's portfolio reduced its reliance on coal-fired power, thereby reducing the substantial financial risks to customers that accompany

such reliance. *See* Decker, Exh. MWD-1T at 10. As even PSE concedes, the cost of compliance with just two of the recently promulgated environmental regulations that require reductions in the emissions of numerous harmful pollutants from coal-fired power plants will certainly be substantial. Testimony of Michael L. Jones, TR. 908:5-25; 910:2-7; 914:2-14. In addition to the costs of compliance with the Mercury and Air Toxics Standards and the Regional Haze Rule, it is likely—though still uncertain—that additional future rules will require still more substantial expenditures. *See* Decker, Exh. MWD-1T at 19-20. Over-reliance on coal-fired power exposes PSE to the very real risk that coal ash regulations, greenhouse gas regulations, and other environmental rules will require substantial expenditures to maintain PSE's existing resource base. By shifting its resource portfolio to rely more on renewables and less on coal, PSE mitigates this risk, to the benefit of consumers.

36. Finally, PSE's transition to a lower-carbon resource portfolio furthers Washington's laudable "commitment to reduce emissions of greenhouse gases . . . [and] goals to grow the clean energy sector and reduce the state's expenditures on imported fuels." RCW 70.235.005. It is appropriate for PSE to consider the well-established environmental and public health threats posed by fossil-fuel-fired electric generation and to favor resource acquisition that reduces those harms because it is the "right thing to do," even beyond the measurable benefits of early acquisition of wind and reduction of the economic risks posed by reliance on fossil fuels. *See* Testimony of Scott Norwood, TR. 381:21 (question from Chairman Goltz). And it is equally appropriate for the Commission to consider such factors in its prudency analysis, as even Mr. Norwood conceded:

> CHAIRMAN GOLTZ: That was exactly my question. My question was focused on just basically is there room in the prudency analysis—again, if you want to say this is a legal issue—is there room in the prudency analysis for the utility, and for

> us in reviewing the utility's judgment, for us to say, you know, more carbon-free energy is a good thing, so we're going to error on that side.
>
> THE WITNESS [Mr. Norwood]: Yeah, absolutely. I just—the only thing I wanted to make clear to you is that's not the determining factor.

Norwood, TR. 382:23-383:8.

37. In sum, PSE's assumptions underlying its decision to acquire LSR 1 were entirely reasonable at the time they were made, and Mr. Norwood's assertions to the contrary lack merit. Moreover, PSE's early acquisition of wind reduces PSE's exposure to financial risk due to new fossil fuel regulations and furthers Washington's "environmental stewardship" and "air quality protection" goals. RCW 70.235.005 (Limiting Greenhouse Gas Emissions, Findings-Intent).

III. PSE SHOULD CONDUCT A FORWARD-LOOKING STUDY OF THE CONTINUED COSTS OF OPERATING COLSTRIP OUTSIDE THE IRP PROCESS.

38. PSE's dependence on coal-fired electric generation, specifically its ownership interest in the four Colstrip units, poses substantial financial risks because the cost of compliance with new environmental and public health rules is likely to be very high for these units. Accordingly, as the Commission already recognized in its acknowledgement letter in response to PSE's 2011 IRP filing, it is critical that PSE conduct a long-term, forward-looking assessment of the cost of continuing the operation of Colstrip. *See* UTC Commission Comments on PSE's 2011 IRP, Docket Nos. UE-100961/UG-100960, Exh. No. JHS-35 CX at 6 ("PSE should conduct a broad examination of the cost of continuing the operation of Colstrip over the 20-year planning horizon, including a range of anticipated costs associated with federal EPA regulations on coal-fired generation.").

39. A series of new regulations applicable to coal-fired power plants will require PSE to invest substantial amounts in the near future to bring the Colstrip units into compliance, starting as early as 2013. The precise costs of compliance are uncertain, both because some of these

rules are not yet finalized and because even for rules that are finalized, PSE has not yet determined exactly what measures will be necessary to comply. It is feasible, however, to forecast a range of likely future compliance costs; such a range could include lower- and higher-cost scenarios based on different regulatory schemes and compliance measures. While there is some uncertainty as to the precise costs of compliance, there is no uncertainty that substantial additional expenditures will soon be required for Colstrip. *See* Jones, TR. 908:5-25; 910:2-7; 914:2-14; *see also* Hausman, Exh. EDH-1T at 6-21.

40. A study of the continuing cost of operating Colstrip over the 20-year planning horizon is essential to ensure that these costs are considered as a whole and compared to alternative resource scenarios. However, this study should take place under a separate docket number and should precede the IRP process. Creating a separate docket for the Colstrip study will allow the protections of discovery and confidentiality for the study, which the IRP process does not provide. As PSE itself has conceded, there is a wide range of possible costs to bring Colstrip into compliance with new environmental regulations, and in at least some instances, these widely varying estimates are all confidential. Jones, TR. 914:11. PSE, however, has indicated that it plans to publicly present all parts of the IRP process and so will attempt not to include confidential information in that process. Jones, TR. 919:13-16. But if the assumptions underlying PSE's analysis of the continued costs of operating Colstrip are hidden, there will be no opportunity for intervenors to test the validity of those assumptions. Moreover, requiring the study on the costs of continued operation of Colstrip to precede the IRP process is consistent with the approach taken by other Commissions. Decker, Exh. MWD-1T at 20-21. In fact, such a study coming before the IRP process ensures a "fair fight" amongst competing options.

> I think our experience in Oregon has been that when you establish the playing field for a fair fight, and you really looked at all the costs, there were some

> benefits to customers in moving away from coal, and I would just submit that it's becoming kind of industry standard for utilities that have significant coal fleets to really dig down and show people what the likely future costs related to environmental regulations and other forms of capital investment in existing coal generation are, and just really have the discussion.

Testimony of Megan Walseth Decker, TR. 486:9-18. *See also* Testimony of Ezra D. Hausman, TR. 489:10-17 ("…the policy issues and the number of different kinds of risks and future regulations that have to be taken into account is a subject of a considerable complicated national debate, and I think it's worth getting that debate started sooner rather than later, so that when you get to the IRP stage, the Commission has had an opportunity to review what its approach should be….").

41. The Commission's response to PSE's 2011 IRP filing does not moot this issue, as explained by Ms. Decker when answering Commissioner Goltz:

> THE WITNESS: I don't think [the Commission's letter makes the issue moot], Chairman Goltz. I don't know exactly what kind of procedural postur[e] the Commission should look at this whole study that we're asking for in, but the analysis that goes forward within the IRP process may not have sort of the transparency and rigor that we're seeing Commissions require of utilities in other contexts.

Decker, TR. 482:23-483:4.

42. By creating a separate docket for the Colstrip study that precedes the IRP process, the study itself may include confidential information, and that docket may include discovery of such information by intervening parties. For the IRP process, a redacted, public version of the study can be used. Accordingly, the Commission should order PSE to conduct the study of Colstrip in a separate docket and should establish a time line for that docket that will allow the final study to inform the IRP process.

IV. PSE SHOULD INCREASE FUNDING TO ITS LOW INCOME ASSISTANCE PROGRAM.

43. "[B]asic energy and utility service is a necessity and … income and expense

circumstances of lower income households often make that service unaffordable." Prefiled Direct Testimony of John G. Howat, Exh. JGH-1T at 4. PSE's low-income bill assistance program, HELP, is designed to help customers secure basic and necessary energy and utility services through bill payment assistance that supplements federal assistance programs. *Id.* at 6-7. Currently, however, only a fraction of PSE's income-eligible customers participate in HELP, and there is a substantial need for additional funding to cover additional eligible customers. *Id.* at 10.

44. To reach additional eligible customers and to offset expected reductions in federal assistance, PSE should increase funding for its HELP program by a percentage that exceeds the residential rate increase that results from this case. *Id.* at 17-18; *see also* Testimony of John G. Howat, TR. 505:13-25; Cavanagh, Exh. RCC-1T at 18. Specifically, PSE's HELP program funding should increase to $20,175,000, an amount more consistent with the level of assistance provided by comparable utilities (including Avista). This increase in funding will allow PSE to serve additional customers even in light of the expected federal shortfall. Howat, Exh. JGH-1T at 20. *See also* Cross-Answering Testimony of Deborah J. Reynolds, Exh. DJR-3T at 19 ("Increasing the funding as the Energy Project recommends is reasonable at this time.").

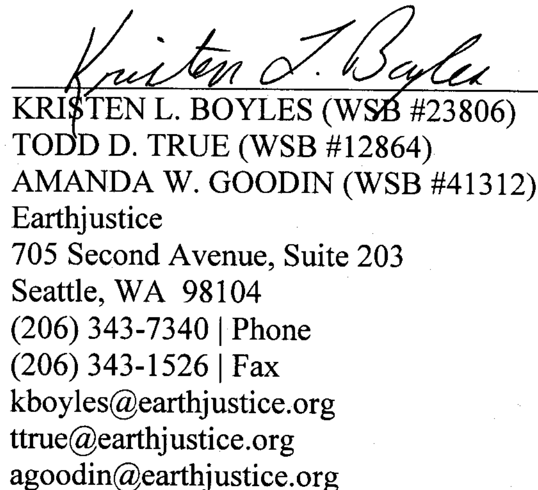
CONCLUSION

45. The Commission's 2010 Decoupling Policy Statement has yet to be translated into an order in a general rate case. Although all parties were specifically invited to address the Policy Statement by Bench Order in this proceeding, the Coalition presented the only full decoupling proposal before the Commission. The Coalition's proposal meets the terms of the Commission's Decoupling Policy Statement; it would be effective in achieving the Commission's stated goals; and it can be implemented. Ordering full decoupling for PSE would begin to put the Commission's policy into action, and it would remove the current structural disincentive against

increased energy conservation. We can do more to increase and stabilize acquisition of energy conservation in Washington, and decoupling is an essential step to further this goal, a goal we all share. The issue is not PSE's commitment to conservation; it is the existence of a disincentive, and now is the time to remove it.

46. For the reasons set forth above and in the evidence before the Commission, NW Energy Coalition respectfully asks the Commission to order full electric decoupling, as described in the submitted expert testimony, for PSE. The Coalition supports PSE's investment in the Lower Snake River wind project as a reasonable early acquisition of renewable energy sources, and the Coalition supports the Sierra Club's proposal for examination of the true costs of Colstrip operation in a separate docket that proceeds and informs the IRP. Finally, the Coalition supports The Energy Project's low-income proposal.

Respectfully submitted this 16th day of March, 2012.



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