

**EXHIBIT NO. ___(RCC-1T)
DOCKET NO. UE-12___/UG-12___
JOINT DECOUPLING ACCOUNTING
PETITION
WITNESS: RALPH C. CAVANAGH**

**BEFORE THE
WASHINGTON UTILITIES AND TRANSPORTATION COMMISSION**

In the Matter of the Petition of

**PUGET SOUND ENERGY, INC.
and NW ENERGY COALITION**

**For an Order Authorizing PSE To Implement
Electric and Natural Gas Decoupling
Mechanisms and To Record Accounting
Entries Associated With the Mechanisms**

**Docket No. UE-12___
Docket No. UG-12___**

**PREFILED DIRECT TESTIMONY (NONCONFIDENTIAL) OF
RALPH C. CAVANAGH
ON BEHALF OF NW ENERGY COALITION**

OCTOBER 25, 2012

**PREFILED DIRECT TESTIMONY (NONCONFIDENTIAL) OF
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1 **NW ENERGY COALITION**

2 **PREFILED DIRECT TESTIMONY (NONCONFIDENTIAL) OF**
3 **RALPH C. CAVANAGH**

4 **I. INTRODUCTION**

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

6 A. I am Ralph Cavanagh, and my address is c/o Natural Resources Defense Council,
7 111 Sutter Street, 20th Floor, San Francisco, California 94305.

8 **Q. In what capacity are you submitting this testimony?**

9 A. I am a witness for the NW Energy Coalition (“the Coalition”).

10 **Q. What are your qualifications?**

11 A. I am a graduate of Yale College and Yale Law School, and I joined the Natural
12 Resources Defense Council (“NRDC”) in 1979. I am a long-time member of the
13 faculty of the University of Idaho’s annual Utility Executive Course, and I have
14 taught courses on utility regulation as a Visiting Professor at Stanford and the
15 University of California, and as a Lecturer on Law at Harvard. From 1993-2003,
16 I served as a member of the U.S. Secretary of Energy’s Advisory Board, and I am
17 now a member of the Secretary’s Electricity Advisory Board. My current board
18 memberships include the Bonneville Environmental Foundation, the Center for
19 Energy Efficiency and Renewable Technologies, the Bipartisan Policy Center, the
20 Renewable Northwest Project, and the Coalition. I have received the Heinz
21 Award for Public Policy (1996) and the Bonneville Power Administration’s

1 Award for Exceptional Public Service (1986). My first testimony to the
2 Washington Utilities and Transportation Commission (the “Commission”) was
3 submitted in 1986 on the issue of Puget Power’s energy efficiency investments,
4 and my first article on revenue decoupling for utilities was published in 1988.¹ I
5 recently submitted testimony on revenue decoupling in the Avista rate proceeding
6 and the Puget Sound Energy, Inc. (“PSE”) rate proceeding.

7 **II. SUMMARY OF TESTIMONY**

8 **Q. Please explain the purpose of your testimony.**

9 A. My testimony supports a joint proposal by the Coalition and PSE for electric and
10 natural gas revenue decoupling for PSE. That proposal is entirely consistent with,
11 and in some ways an improvement upon, the revenue decoupling mechanism
12 proposed in my original testimony in PSE’s 2011 general rate case Docket No.
13 UE-111048/UG-111049. In Order 08 in that proceeding, the Commission stated
14 that it would be open to considering such a proposal if the Company withdrew its
15 opposition.²

16 **Q. Please briefly explain the circumstances leading up to this filing.**

17 A. In PSE’s recently-completed general rate case, the Coalition submitted a full
18 decoupling proposal for PSE retail electricity sales, which I supported in prefiled

¹ R. Cavanagh, Responsible Power Marketing in an Increasingly Competitive Era, 5 Yale Journal on Regulation (July 1988); more recently, see R. Cavanagh, Reinventing Competitive Procurement of Electricity Resources, ElectricityPolicy.com (Oct. 2010).

² WUTC v Puget Sound Energy, Inc., Dockets UE-111048/UG-111049, Order 08 (May 7, 2012) at 456 p. 167.

1 testimony and at the hearing. In its final order in that case, the Commission
2 commended the Coalition for its decoupling proposal and determined that the
3 Coalition's proposal largely followed, and was consistent with the purpose of, the
4 Commission's Decoupling Policy Statement.³ However, the Commission
5 declined to require PSE to implement full decoupling, as set forth in my
6 testimony, in the face of PSE's opposition.⁴ PSE contended that the Coalition's
7 decoupling proposal did not adequately address the financial consequences of
8 PSE's energy efficiency programs.⁵

9 Although the Commission did not implement the Coalition's decoupling proposal,
10 in its final order the Commission stated that it remained open to proposals for a
11 full decoupling mechanism, even to one that varied somewhat from the
12 Commission's Decoupling Policy Statement.⁶ In response, PSE and the Coalition
13 worked intensively together to craft a decoupling proposal that is consistent with
14 the Coalition's proposal in PSE's 2011 general rate case and the Commission's
15 Decoupling Policy Statement, and that better addresses PSE's concerns regarding
16 the effects of conservation and decoupling on PSE's ability to recover its costs of
17 service.

18 My testimony supports the joint proposal of PSE and the Coalition for electric and
19 gas revenue decoupling. Also in support of the joint proposal, I am providing as

³ Id., ¶¶ 453, 455 (hereafter "PSE GRC Final Order").

⁴ Id., ¶ 453.

⁵ PSE GRC Final Order, ¶¶ 453-54.

⁶ PSE GRC Final Order, n. 617.

1 Exhibit No. ____ (RCC-2), my prefiled testimony in PSE's 2011 general rate case,
2 which among other things provides a brief history of revenue decoupling in
3 Washington state, a discussion of the recommended elements of a full decoupling
4 program, and the broader case for revenue decoupling.

5 **Q. Why isn't this decoupling proposal being presented in the context of a**
6 **general rate case filing, in accordance with the preference expressed in the**
7 **Commission's Decoupling Policy Statement?**

8 A. It is my understanding that PSE does not intend to file a general rate case in the
9 near future, and the Commission has previously approved decoupling mechanisms
10 outside of a general rate case. For example, in 2006 Avista filed a petition for a
11 gas decoupling mechanism, and although the proposal was not included in a
12 general rate case, the Commission approved decoupling for Avista. One factor
13 that the Commission considered was that Avista had recently filed a general rate
14 case, which is also the case here. The Commission completed a review of PSE's
15 2011 general rate case only a few months ago, and as a part of that case, the
16 Coalition presented a decoupling mechanism that is very similar to that in this
17 petition. Moreover, in that case the Commission not only thoroughly analyzed the
18 Coalition's decoupling proposal, it also sought, received, and considered input
19 from Commission Staff and other parties about decoupling in general. In sum, the
20 Commission has recently completed a full analysis of decoupling in general and
21 for PSE specifically, including a decoupling proposal that included most of the
22 elements of the one that PSE and the Coalition are presenting in this case. The

1 decoupling proposal in this petition is based on the non-power costs approved by
2 the Commission in its general rate case order. In this context, it is appropriate for
3 the Commission to consider and approve the joint proposal for decoupling
4 presented by the Coalition and PSE.

5 **III. THE JOINT COALITION/PSE DECOUPLING PROPOSAL**

6 **Q. Why do you support this petition?**

7 A. It builds on, and in some ways improves, the revenue decoupling proposal in my
8 earlier testimony. Sometimes negotiations produce imperfect compromises of
9 incompatible positions, but here it was clear from the outset that the Coalition and
10 PSE had common objectives that were entirely consistent with the Commission's
11 extensive prior guidance on revenue decoupling and utility-sector energy
12 efficiency leadership. The result is an electricity and natural gas decoupling and
13 energy efficiency proposal that I view as a model for the entire utility industry,
14 and a tribute to the regulatory leadership exemplified in the Commission's Policy
15 Statement.

16 **Q. Which aspects of your initial proposal were sacrificed to achieve agreement?**

17 A. None. The petition, in fact, offers a more comprehensive proposal with greater
18 assurance of incremental energy efficiency benefits.

19 **Q. Explain why you view the petition as an improvement on your initial**
20 **proposal.**

21 A. It is more comprehensive in its coverage of customer classes (although it retains

1 my recommendation for two separate residential and nonresidential per-customer
2 revenue requirements and it excludes retail access customers) and it applies to
3 both electricity and natural gas. I note that the Commission’s Policy Statement
4 recommends inclusion of all customer classes. The petition includes a specific
5 commitment by PSE to voluntarily achieve electricity conservation that exceeds
6 its statutorily-required I-937 targets by five percent, which is equivalent to setting
7 a pace for achieving its ten-year conservation potential over a period of roughly
8 9.5 years, and it also proposes to increase funding of its low-income conservation
9 programs by twenty percent over levels currently budgeted for 2013. These
10 commitments directly respond to the Commission’s request in its Policy
11 Statement for “evidence describing any incremental conservation the company
12 intends to pursue in conjunction with the mechanism.”⁷ There is also specific
13 assurance for an opportunity, within three to five years, for the Commission to
14 reassess any impacts of the proposal on the company’s cost of equity. And the
15 petition includes a more comprehensive set of evaluation parameters, with
16 particular attention to impacts on low-income customers.

17 **Q. How can PSE increase its I-937 conservation targets if it is already pursuing**
18 **all cost-effective, achievable energy efficiency?**

19 A. RCW 19.285.040(1) requires PSE to pursue all available conservation that is cost-
20 effective, reliable, and achievable. PSE must identify its 10-year achievable cost-

⁷ Docket No. U-100522, Report and Policy Statement on Regulatory Mechanisms, Including Decoupling, to Encourage Utilities to Meet or Exceed Their Conservation Targets (“Decoupling Policy Statement”), p. 18.

1 effective conservation potential, and establish a near-term biennial acquisition
2 target. For its most recent biennial target, PSE elected to rely on the 20-year
3 conservation potential assessment contained in its 2011 Integrated Resource Plan
4 (IRP).⁸ That IRP reaffirmed the cost and risk reduction benefits of demand side
5 resources (DSR): “DSR is the only resource that reduces cost and risk—and the
6 sooner it’s acquired, the more cost-effective it is.”⁹ PSE’s IRP analysis
7 accelerated its conservation acquisition, applying a 10-year ramp rate for retrofit
8 measures.¹⁰ As noted in the IRP, experience from the 2010-2011 DSR acquisition
9 programs demonstrated that accelerated conservation ramp rates are feasible. In
10 the context of this decoupling proposal, the Coalition and PSE are jointly
11 proposing to further accelerate PSE’s acquisition of energy efficiency, thereby
12 securing additional cost and risk reduction benefits for PSE’s customers. As
13 noted in its 2012-2013 Biennial Conservation Plan, PSE already must overcome
14 considerable challenges to conservation acquisition efforts for 2012.¹¹ Increasing
15 its conservation target further will be a stretch, but we believe that PSE can rise to
16 the challenge.

17 **Q. Will the 20% funding increase in funding for low-income weatherization**
18 **yield significant benefits?**

19 A. Yes. Funding for weatherization comes from multiple sources (federal, state,

⁸ Docket No. UE-111881, Order 01, ¶ 5.

⁹ Docket No. UE-100961, PSE’s Integrated Resource Plan, pp. 5-42.

¹⁰ *Id.*, pp. 5-43.

¹¹ Docket No. UE-111881, Biennial Conservation Plan, p. 2.

1 utilities) and they all leverage each other. The increased commitment comes at a
2 crucial time, when federal weatherization funding is in decline and the need for
3 weatherization services is higher than ever. I am confident that Puget will
4 continue to work with local community agencies to ensure that they can use the
5 additional funding effectively. It will likely be important for all involved to
6 secure more clarity on program cost-effectiveness; coordination of audits,
7 inspections and contractors; and flexibility in managing expenditures (including,
8 e.g., those involving the structural repairs and health and safety issues that often
9 must be addressed as part of weatherization projects).

10 **Q. Why is the evaluation section of the joint petition more detailed than in your**
11 **initial testimony?**

12 A. I consider this section another improvement on the original proposal. It reflects
13 guidance in the Commission's Policy Statement, which outlines a number of
14 requirements and criteria that the Commission will consider when deciding on
15 whether to adopt and retain a proposed mechanism. The proposal for an
16 independent third-party evaluation prior to the next general rate case will help the
17 Commission and all parties assess whether this mechanism is achieving its goals.
18 In addition, the joint petition provides specifically for a detailed examination of
19 changes in the programs offered to Puget's low-income customers and other
20 potential impacts on this customer segment.

21 **Q. What about the K-factor element of the joint proposal, which was not**
22 **included in your initial testimony?**

1 A. In that testimony, in explaining how revenue per customer could be calculated, I
2 used an illustration based on nonpower costs from Puget’s 2009 rate case, while
3 cautioning that “[t]his calculation is illustrative only, since the revenue
4 requirement approved in this case is likely to differ.”¹² I did not take a position
5 then on what the revenue per customer should be. I support the K-factor
6 methodology proposed in the petition, which adjusts revenue per customer to
7 what it would have been absent company-sponsored energy efficiency efforts.

8 **Q. Is the use of a “K-factor” consistent with other decoupling mechanisms**
9 **adopted across the nation?**

10 A. Yes. Every Commission has its own approach to setting authorized revenue
11 requirements, and Commissions often effectively or explicitly take into account
12 the impact of utilities’ energy-efficiency programs on consumption when
13 establishing the assumptions about energy use and non-fuel costs that are used to
14 set retail rates. Also, in contrast to the joint petition’s more limited scope, many
15 decoupling mechanisms incorporate fixed costs of power production as well as
16 non-power costs; in every instance, these fixed generation costs far exceed any
17 potential impact of the K-factor as a fraction of total revenue recovery under the
18 mechanisms in question. The principle underlying the K-factor is that PSE should
19 not be penalized, for purposes of its authorized per-customer revenue
20 requirement, by the impact on consumption of its energy efficiency programs. I

¹² Exhibit No. ____ (RCC-2), pp. 12:4-5.

1 know of no Commission that has found to the contrary in approving any
2 decoupling mechanism.

3 **Q. Will the K-factor mean higher earnings for PSE?**

4 A. No, I agree with PSE that the K-factor merely prevents the company's energy
5 efficiency programs from eroding earnings below where they would be without
6 the programs.

7 **Q. Do any recent regulatory precedents outside Washington State provide**
8 **support for the joint Coalition/PSE proposal?**

9 A. Yes. I note that in Oregon, on October 2, 2012, the parties in Northwest Natural
10 Gas's Application for a General Rate Revision (including the Coalition) filed with
11 the Commission a stipulation supporting continuation of the company's full
12 decoupling mechanism for natural gas.¹³ On that same day, the Los Angeles City
13 Council approved a full electric decoupling mechanism for the nation's largest
14 municipal utility, which became effective with the mayor's signature three days
15 later.¹⁴

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

17 A. Yes.

¹³ In re Northwest Natural Gas Company's Application for a General Rate Revision, Second Partial Stipulation, UG221, Item 15, pp. 2-3 (Oct. 2, 2012).

¹⁴ City of Los Angeles, Ordinance No. 182273 (Oct. 5, 2012), pp. 85-87. For more background, see http://switchboard.nrdc.org/blogs/rcavanagh/la_utilitys_historic_energy_ef.html.