

**EXH. JLM-1CTr
DOCKETS UE-240004/UG-240005 et al.
2024 PSE GENERAL RATE CASE
WITNESS: JAMIE L. MARTIN**

**BEFORE THE
WASHINGTON UTILITIES AND TRANSPORTATION COMMISSION**

**WASHINGTON UTILITIES AND
TRANSPORTATION COMMISSION,**

Complainant,

v.

PUGET SOUND ENERGY,

Respondent.

**Docket UE-240004
Docket UG-240005
(consolidated)**

In the Matter of the Petition of

PUGET SOUND ENERGY

**For an Accounting Order Authorizing
deferred accounting treatment of
purchased power agreement expenses
pursuant to RCW 80.28.410**

**Docket UE 230810
(consolidated)**

PREFILED REBUTTAL TESTIMONY (CONFIDENTIAL) OF

JAMIE L. MARTIN

ON BEHALF OF PUGET SOUND ENERGY

REDACTED VERSION

SEPTEMBER 18, 2024

**REVISED
SEPTEMBER 26, 2024**

PUGET SOUND ENERGY

PREFILED REBUTTAL TESTIMONY (NONCONFIDENTIAL) OF JAMIE L. MARTIN

CONTENTS

I.	INTRODUCTION	1
II.	THE COST OF CAPITAL AND RATE OF RETURN RECOMMENDATIONS BY COMMISSION STAFF, PUBLIC COUNSEL, AWEC, AND JEA ARE UNBALANCED AND WOULD NEGATIVELY IMPACT PSE’S CREDIT METRICS AND IMPAIR PSE’S ABILITY TO TRANSITION TO CLEAN ENERGY WHILE ALSO PROVIDING SAFE AND RELIABLE GAS AND ELECTRICITY TO ITS CUSTOMERS	3
A.	Cost of Capital Proposals of Commission Staff, Public Counsel, and AWEC Are Inadequate and Should Be Rejected.....	3
B.	JEAs Proposal To Lower the ROE on New Gas Customer Connections and Capacity Expansions Is Unbalanced and Fails To Recognize PSE’s Obligation To Serve.....	28
III.	PSE CONTINUES TO UNDEREARN AND THE PROPOSALS OF INTERVENING PARTIES WILL ONLY EXACERBATE THE UNDEREARNING.....	30
IV.	COMMISSION STAFF’S TRACKER STANDARDS SHOULD BE REJECTED	35
V.	FURTHER CUTS TO O&M AS PROPOSED BY COMMISSION STAFF AND INTERVENING PARTIES WILL UNDERMINE PSE’S ABILITY TO TRANSITION TO CLEAN ENERGY WHILE PROVIDING SAFE AND RELIABLE SERVICE	42
VI.	THE COMMISSION HAS AUTHORITY TO AUTHORIZE AND SHOULD AUTHORIZE PSE TO EARN A RETURN ON PPAS	45
VII.	CWIP IN RATE BASE.....	50
A.	PSE’s Response to Public Counsel Testimony on CWIP in Rate Base	51
B.	PSE’s Response to AWEC’s Testimony on CWIP in Rate Base	55

C.	PSE’s Response to Commission Staff’s Testimony on CWIP in Rate Base	58
D.	PSE’s Response to JEA’s Testimony on CWIP in Rate Base	61
VIII.	WILDFIRE TRACKER AND INSURANCE COSTS.....	63
IX.	ACCELERATED GAS DEPRECIATION.....	67
A.	Response to The Energy Project Witness Stokes	67
B.	Response to JEA Witness Gehrke’s Gas Depreciation Proposal.....	68
X.	CONCLUSION.....	71

PUGET SOUND ENERGY

**PREFILED REBUTTAL TESTIMONY (NONCONFIDENTIAL) OF
JAMIE L. MARTIN**

LIST OF EXHIBITS

Exh. JLM-2	Professional Qualifications
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1 **PUGET SOUND ENERGY**

2 **PREFILED REBUTTAL TESTIMONY (NONCONFIDENTIAL) OF**
3 **JAMIE L. MARTIN**

4 **I. INTRODUCTION**

5 **Q. Please state your name, business address, and position with Puget Sound**
6 **Energy.**

7 A. My name is Jamie L. Martin, and my business address is Puget Sound Energy,
8 P.O. Box 97034, Bellevue, Washington 98009-9734. I am employed by Puget
9 Sound Energy ("PSE") as Senior Vice President and Chief Financial Officer.

10 **Q. Have you prepared an exhibit describing your education, relevant**
11 **employment experience, and other professional qualifications?**

12 A. Yes I have. It is Exh. JLM-2.

13 **Q. What is the purpose of your rebuttal testimony?**

14 A. My rebuttal testimony adopts the Prefiled Direct Testimony (Confidential) of
15 Daniel A. Doyle, Exh. DAD-1CT and supporting exhibits. Generally, in response
16 to testimony filed, I reiterate the importance to PSE customers of PSE being
17 financially healthy, which is not the case when PSE is unable to achieve its
18 allowed rate of return or when it risks credit downgrades. In addition, I provide
19 rebuttal on the following topics:

1 First, I respond to proposals from Commission Staff, Public Counsel, the Alliance
2 of Western Energy Consumers (“AWEC”), and the Joint Environmental
3 Advocates (“JEA”) with respect to PSE’s cost of capital, rate of return and return
4 on equity (“ROE”). Their proposals are very concerning on multiple fronts: their
5 proposals do not adequately address the cash flow needs for a healthy utility, and
6 would negatively impact PSE’s credit metrics and PSE’s ability to move forward
7 with the clean energy transition while providing safe and reliable electricity and
8 natural gas service to its customers.

9 Second, in response to proposals by intervening parties, I demonstrate the extent
10 and causes of PSE’s current under earning. The proposals by parties in this case
11 will only exacerbate this under earning.

12 Third, I respond to Commission Staff’s proposal to set standards for the use of
13 trackers in this proceeding. I demonstrate that assumptions underlying this
14 proposal are not financially sound.

15 Fourth, I respond to proposals to cut PSE’s operations and maintenance (“O&M”)
16 budget for the multiyear rate plan (“MYRP”). I discuss the reasonableness of
17 PSE’s O&M budget and how these proposals will undermine PSE’s ability to
18 transition to cleaner energy and provide safe and reliable core utility services.

19 Fifth, I respond to parties who challenge PSE’s proposal to earn a return on
20 certain power purchase agreements (“PPA”). PSE’s proposal is consistent with

1 Washington law, and allowing a return at the higher end of the statutory range is
2 appropriate for the PPAs at issue in this case.

3 Sixth, I respond to opposition from Public Counsel, AWEC, Commission Staff,
4 and JEA to PSE's proposal to include construction work in progress ("CWIP") in
5 rate base rather than using the traditional, and more expensive, allowance for
6 funds used during construction ("AFUDC") for the Beaver Creek project.

7 Seventh, I respond to opposition to wildfire trackers by Public Counsel.

8 Finally, I respond to opposition to PSE's proposal to accelerate the depreciation
9 of PSE's gas plant.

10 **II. THE COST OF CAPITAL AND RATE OF RETURN**
11 **RECOMMENDATIONS BY COMMISSION STAFF, PUBLIC COUNSEL,**
12 **AWEC, AND JEA ARE UNBALANCED AND WOULD NEGATIVELY IMPACT**
13 **PSE'S CREDIT METRICS AND IMPAIR PSE'S ABILITY TO TRANSITION TO**
14 **CLEAN ENERGY WHILE ALSO PROVIDING SAFE AND RELIABLE GAS**
15 **AND ELECTRICITY TO ITS CUSTOMERS**

16 **A. Cost of Capital Proposals of Commission Staff, Public Counsel, and AWEC**
17 **Are Inadequate and Should Be Rejected**

18 **Q. Please summarize your understanding of the cost of capital**
19 **recommendations for AWEC witness Kaufman, Public Counsel witness**
20 **Woolridge and Commission Staff witness Parcell.**

21 A. AWEC witness Kaufman recommends a return on equity of 9.2 percent based on
22 a range of 8 percent to 9.5 percent and uses a 49.0 percent equity ratio to calculate

1 his recommended rate of return.¹ Public Counsel witness Woolridge recommends
2 a return on equity of 9.375 percent based on a range of 9 percent to 9.75 percent
3 (which is the midpoint of his overall range) and uses a 49 percent equity ratio to
4 calculate his recommended rate of return.² Commission Staff witness Parcell
5 recommends a rate of return of 9.5 percent based on a range of 9.5 percent to 10
6 percent and uses an equity ratio of 48.5 percent.³ It should be noted that Mr.
7 Parcell's testimony refers to the fact that PSE's current approved equity ratio is
8 48.5 percent.⁴ That is incorrect. PSE's current approved equity ratio is 49.0
9 percent.⁵

10 **Q. Does PSE have any concerns with respect to the return on equity, equity**
11 **ratio and resulting rate of return recommendations proffered by AWEC**
12 **witness Kaufman, Public Counsel witness Woolridge, and Commission Staff**
13 **witness Parcell?**

14 A. Yes, PSE has many concerns with their recommendations. With respect to the
15 return on equity ranges proposed in their testimonies, such ranges are constructed
16 from underlying studies which take into consideration various methodologies to
17 estimate returns on equity including, discounted cash flow models, risk premium
18 models, capital asset pricing models and the like. PSE witness Ann Bulkley

¹ Kaufman, Exh. LDK-1CT at 71:4–72:3.

² Woolridge, Exh. JRW-1CT at 6:16-19, 4:20-22.

³ Parcell, Exh. DCP-1T at 4:8-21.

⁴ Parcell, Exh. DCP-1T at 27:1-2.

⁵ *WUTC v. Puget Sound Energy*, Dockets UE-220066, UG-22067 (consolidated) Order 24/10 ¶ 122 (December 22, 2022) (“We accept the Revenue Requirement Settlement’s proposed capital structure of 49 percent equity and 51 percent debt for the duration of the MYRP. We find Public Counsel’s arguments for a lower equity ratio of 48.5 percent unpersuasive”).

1 addresses numerous concerns regarding the assumptions and methodologies
2 employed by AWEC, Public Counsel and Commission Staff. She has filed
3 separate rebuttal testimony to address her concerns and therefore they are not
4 repeated here.⁶

5 Additionally, PSE witness Cara Peterman also presents separate rebuttal
6 testimony to address errors and inconsistencies related to the assumptions and
7 calculations used by AWEC witness Kaufman, Public Counsel witness
8 Woolridge, and Commission Staff witness Parcell to arrive at their respective rate
9 of return recommendations.⁷ PSE witness Peterman's concerns address errors and
10 inconsistencies related to short and long-term debt assumptions and fees and
11 calculations for inclusion in PSE's capital structure, and Commission Staff
12 witness Parcell's error related to PSE's current approved equity ratio. I also
13 address concerns related to forecasted credit metric health given cost of capital
14 and other intervenor proposals.

15 PSE witness Todd Shipman provides rebuttal testimony directed at the return on
16 equity and capital structure recommendations, as well as interpretations of rating
17 agency perspectives, of Commission Staff and Public Counsel and opines that the
18 credit metrics resulting from their recommendations would fall well below ratings
19 agency expectations and in some cases below downgrade triggers.⁸ He further
20 discusses the issues that would result from regression in PSE's financial

⁶ Bulkley, Exh. AEB-19T.

⁷ Peterman, Exh. CGP-11T.

⁸ Shipman, Exh. TAS-5T.

1 performance due to regulatory outcomes if proposals by Commission Staff and
2 Public Counsel are accepted by the Commission.

3 **Q. What other concerns do you have with respect to the return on equity, equity**
4 **ratio and resulting rate of return recommendations proffered by AWEC**
5 **witness Kaufman, Public Counsel witness Woolridge, and Commission Staff**
6 **witness Parcell?**

7 A. I have several concerns. First, PSE disagrees with testimony from Public Counsel
8 witness Woolridge and Commission Staff witness Parcell that the risk reducing
9 nature of MYRPs eliminates the need for increased return on equity and equity
10 ratio as presented in PSE's request in this case. Public Counsel witness Woolridge
11 cites to

12 the passage of Senate Bill 5295 on May 3, 2021, which
13 transformed utility regulation into multiyear rate plan and
14 performance-based ratemaking. The legislation is expected
15 to reduce regulatory lag and cash flow volatility... PSE
16 recently got a decarbonization bill passed (March 2024)
17 that permits accelerated depreciation for gas assets, a return
18 on purchased power agreements, and construction while in
19 progress funding for decarbonization investment projects.
20 Credit rating agencies have historically reacted positively
21 to legislation like this with upgrades to credit ratings.⁹

22 Likewise, Commission Staff witness Parcell states:

23 It is apparent that SB 5295, as well as several other
24 favorable regulatory mechanisms (as cited by Moody's and
25 S&P) the company has access to, provides favorable risk
26 reducing attributes to PSE. The impact of these
27 mechanisms on both an individual and collective basis, is to

⁹ Woolridge, Exh. JRW-1CT at 107:14-23.

1 transfer a significant portion of PSE's risks from its
2 shareholders to its ratepayers. This risk transfer is not
3 voluntary from the rate payer perspective. I
4 correspondingly believe that ratepayers should receive
5 some benefit for their acceptance of this risk transfer.¹⁰

6
7 **Q. Does PSE agree that MYRP legislation is risk reducing and thus PSE's**
8 **requested increases in return on equity and equity ratio in this proceeding**
9 **should be denied?**

10 A. No. First, the existence of MYRPs is not risk reducing in and of itself as Public
11 Counsel witness Woolridge and Commission Staff witness Parcell claim. What
12 matters most is how MYRPs are implemented in practice. This fact was amplified
13 by S&P when commenting on Senate Bill ("SB") 5295 and MYRPs when they
14 stated, "We believe Washington's new law, *predicated on the commission*
15 *implementing it in a credit supportive way, could* improve the regulatory
16 environment."¹¹ This is an absolutely critical point that both Woolridge and
17 Parcell do not consider.

18 Second, PSE is currently in its first MYRP covering the years 2023 and 2024, and
19 it is noteworthy that PSE did not earn its allowed rate of return in 2023, and does
20 not expect to do so in 2024. Clearly, the use of MYRPs in the state of Washington

¹⁰ Parcell, Exh. DCP-1T at 22:21-27.

¹¹ See Parcell, Exh. DCP-1T at 21:4-14 (quoting S&P Global Ratings, "RatingsDirect, Research Update, Puget Energy Inc. And Subsidiary Outlooks Revised To Stable Following New Rate Plan Legislation; Rating Affirmed," (May 27, 2021) (emphasis added)).

1 are in a nascent, developmental state and, therefore, cannot be credibly viewed as
2 risk reducing in the context of setting returns on equity at this time.

3 **Q. Does PSE believe that recently passed legislation addressing CWIP in rate**
4 **base, accelerated gas depreciation, and returns on PPAs have risk reducing**
5 **attributes in the context of setting a regulated return on equity?**

6 A. No, not at this time. Here again, the mere passage of the recent legislation, which
7 further elaborates on the use of CWIP in rate base, accelerated gas depreciation,
8 and returns on PPAs does not in and of itself produce any risk-reducing attributes.
9 Again, any risk-reducing attributes related to these legislative provisions can only
10 be assessed based on how they are implemented. PSE has requested CWIP in rate
11 base treatment, accelerated gas depreciation, and returns on certain PPAs, based
12 on these legislative provisions, for the first time in this proceeding. Accordingly at
13 this time, there is no clear or definitive information available regarding how the
14 Commission will implement PSE's requests, including whether the Commission
15 will ultimately implement them. As a result, it is inappropriate for Public Counsel
16 witness Woolridge and Commission Staff witness Parcell to factor any risk
17 reducing attribute or element of these legislative provisions into their
18 determination of their respective returns on equity.

1 **Q. Does PSE have any other concerns regarding its requests for CWIP in rate**
2 **base, accelerated gas depreciation, and returns on certain PPAs?**

3 A. Yes. Several parties in this proceeding, through various witnesses, oppose, in
4 whole or in part, PSE's requests for CWIP in rate base, accelerated gas
5 depreciation, and returns on certain PPAs. Commission Staff witness McGuire
6 supports earning a return on certain PPAs based on PSE's cost of debt rather than
7 based on PSE's full rate of return, and he supports shortening depreciation lives,
8 but only in the event aspects of House Bill ("HB") 1589 are not repealed in the
9 November 2024 elections.¹² JEA witness Gehrke supports a portion of
10 accelerated gas depreciation.¹³ Public Counsel opposes these proposals in their
11 entirety.¹⁴ AWEC witness Bradley Mullins opposes CWIP in rate base treatment
12 and PSE's proposal to earn a return on PPAs.¹⁵

13 **Q. What specifically is PSE's concern?**

14 A. PSE's specific concern is that Public Counsel witness Woolridge and Commission
15 Staff witness Parcell incorporate what they perceive are the risk reducing
16 attributes of CWIP in rate base, accelerated gas depreciation, and returns on
17 certain PPAs into the determination of their recommended returns on equity. In
18 this testimony above, PSE rebuts the notion that these legislative positions, in the
19 absence of implementation, result in any risk reducing attributes. That said, on the

¹² McGuire, Exh. CRM-1Tr at 80:1-4 (discussing PPAs); 24:1-29:2 (discussing HB 1589).

¹³ Gehrke, Exh. WAG-1T at 4:12-16, 7:8-15.

¹⁴ Gorman, Exh. MPG-1CT at 18:12-23:7 (CWIP); 25:20-26:13 (PPAs); *see generally* Garrett, Exh. DJG-1T (depreciation).

¹⁵ Mullins, Exh. BGM-1T at 25:4-27:14 (CWIP); 29:10-31:16 (PPAs).

1 other side of the equation, Public Counsel, Commission Staff, and AWEC present
2 witnesses whose testimonies oppose PSE's requests for CWIP in rate base,
3 accelerated gas depreciation, and returns on certain PPAs, in whole or in part. It
4 is at minimum troubling and at worst disingenuous for these parties, through their
5 various witnesses, to claim what they believe to be risk reducing attributes of
6 CWIP in rate base, accelerated gas depreciation, and returns on certain PPAs as
7 "offsetting phenomena" in the determination of their recommended returns on
8 equity and then challenge and oppose the very implementation of these legislative
9 positions in other parts of their cases. If the Commission ultimately denies PSE's
10 request for CWIP in rate base, accelerated gas depreciation, and returns on certain
11 PPAs, Public Counsel witness Woolridge and Commission Staff witness Parcell
12 will have erroneously included and considered what they perceived to be risk
13 reducing attributes in their recommended returns on equity. The Commission
14 should be mindful of this ratemaking and regulatory dynamic when considering
15 the return on equity recommendations of Public Counsel witness Woolridge and
16 Commission Staff witness Parcell.

17 **Q. Do AWEC witness Kaufman, Public Counsel witness Woolridge, and**
18 **Commission Staff witness Parcell adequately assess PSE's risk profile across**
19 **its proposed 2025 and 2026 MYRP?**

20 **A. No.**

Q. What are PSE's specific concerns as it relates to their assessments of PSE's current risk profile?

A. In prefiled direct testimony, covering several witnesses, PSE provides the Commission with an in-depth and comprehensive view of PSE's increasing risk profile due to the enactment and implementation of both CETA and CCA, as well as the increasing risk of wildfire.¹⁶ This is in addition to continuing to provide safe and reliable service to customers. PSE documents and supports for the Commission's consideration how CETA and CCA have dramatically impacted PSE's financial and operational risk profile. Specifically, PSE made the following key points:

1. Due to the enactment and implementation of CETA and CCA, PSE is now confronted with a dual mandate: It must continue to focus on providing safe and reliable energy service to customers as it has in the past, but must now partner with the state of Washington and this Commission to achieve the public policy goals of decarbonization and reduction in emissions. Indeed, SB 5295, which established the MYRP, also allows the Commission to consider greenhouse gas emissions reductions in determining the public interest.¹⁷
2. To meet and comply with the provisions of CETA and CCA, PSE estimates that over the calendar years 2024 to 2028 it will invest approximately \$ [REDACTED] billion in capital expenditures. This is a [REDACTED]

¹⁶ See generally Doyle, Exh. DAD-1CT; Peterman, Exh. CGP-1CT; Marcelia, Exh. MRM-1T.

¹⁷ Doyle, Exh. DAD-1CT at 14:10–16:8.

1 [REDACTED], that will affect PSE both
2 financially and operationally.¹⁸

3 3. To fund this increased level of capital expenditures to meet PSE's
4 responsibilities under CETA and CCA, PSE estimates that over the calendar
5 years 2024 to 2028 it will require incremental financing from the following
6 categories:

- 7 a. \$ [REDACTED] billion of debt securities
- 8 b. \$ [REDACTED] billion of incremental equity
- 9 c. and retain approximately \$ [REDACTED] billion of net income and retained
10 earnings and related cash flow from operations.¹⁹

11 4. This level of capital expenditure and resulting financing will increase PSE's
12 balance sheet from \$ [REDACTED] billion to \$ [REDACTED] billion or approximately [REDACTED] percent.
13 In addition, the financing plan set forth above would cause PSE's outstanding
14 debt to increase to \$ [REDACTED] billion or an increase of about [REDACTED] percent and PSE's
15 outstanding common equity to grow to \$ [REDACTED] billion, an increase of about [REDACTED]
16 [REDACTED] over the calendar years 2024 to 2028.²⁰

17 5. While the rating agencies initially viewed SB 5295, which enabled the filing
18 of MYRPs, as generally positive, PSE expects that it will perform below

¹⁸ Doyle, Exh. DAD-1CT at 57:18–58:8.

¹⁹ *Id.*

²⁰ Doyle, Exh. DAD-1CT at 14:1-9.

downgrade thresholds of credit rating agencies in both 2023 and 2024. The rating agencies are now aware that MYRPs in and of themselves are not a complete solution for Washington utilities to earn their allowable rates of return nor manage their credit metric performance above downgrade thresholds with an appropriate margin of cushion.²¹

6. The Tax Cuts and Jobs Act (“TCJA”), which was enacted more than five years ago, resulted in a reduction of PSE’s cash flow of approximately \$156 million.²² The TCJA remains the tax law in effect for corporations until it is changed by Congress. As a result, PSE’s credit metrics have decreased significantly from 2018 – 2024, from above downgrade thresholds to below downgrade thresholds as a result of the loss of cash flow from the passage of the TCJA. Figure 1-4 that I provide later in my testimony show this troubling decline. If PSE’s proposals to improve cashflow are not adopted, [REDACTED], [REDACTED], and PSE will be less likely to fund clean energy and reliability investments on reasonable terms, all of which will adversely impact PSE’s customers.

7. During the period 2018 to 2023, PSE under earned its authorized return on equity within a range of 2.1 to 3.0 percentage points, or 23 percent to 32 percent below allowed returns on an actual basis. On an estimated basis for

²¹ Doyle, Exh. DAD-1CT at 19:19–20:3; Peterman, Exh. CGP-11T.

²² Marcelia, Exh. MRM-1T at 24:8-11.

2024, PSE estimates that [REDACTED] as shown in Table 4 below. This means that PSE would under earn its authorized rate of return by more than [REDACTED] percent. A failure to earn close to the authorized return is a downgrade trigger for S&P and a key consideration for all rating agencies, as discussed in the Prefiled Rebuttal Testimony of Todd A. Shipman.

PSE's testimony in this regard presents evidence that both its operational and financial risk profile have shifted dramatically in response to the dual mandate.

Q. Do AWEC witness Kaufman and Public Counsel witness Woolridge recognize and consider the obvious impacts of CETA and CCA on PSE's operational and financial risk profile in the determinations of their recommendations for return on equity, equity ratio and overall rate of return?

A. Unfortunately, they do not. AWEC witness Kaufman mentions "PSE specific risk," but his testimony is lacking any specific analysis of PSE's existing or increasing risk profile due to the enactment and imposition of CETA and CCA on PSE's continuing financial and operational risk profile.²³ Public Counsel witness Woolridge considers various factors that contribute to his assessment, but he presents no specific analysis of his considerations in his recommendation for return on equity nor does he address any of the risk increasing aspects imposed by

²³ See Kaufman, Exh. LDK-1CT at 37:12-13.

1 the enactment and implementation of CETA and CCA on PSE's overall risk
2 profile.²⁴

3 **Q. How does Parcell consider the impacts of CETA and CCA on PSE's**
4 **operational and financial risk profile in the determination of his**
5 **recommendations for return on equity, equity ratio and overall rate of**
6 **return?**

7 A. Parcell's treatment of the issue is a bit more complex than that of AWEC and
8 Public Counsel. First, Parcell states "PSE's ratings are generally similar to most
9 electric utilities in the U.S.... PSE's ratings are also generally similar to the
10 ratings of the proxy groups selected by company witness Bulkley (also shown on
11 exhibit DCP-8)."²⁵ PSE disagrees with the broad and unsupported proclamations
12 in this regard, and PSE witness Peterman provides separate rebuttal testimony on
13 these points.²⁶ Commission Staff witness Parcell then proceeds to again tout the
14 risk reducing benefits of MYRPs and recently passed legislation in the state of
15 Washington, more specifically CWIP in rate base, accelerated gas depreciation,
16 and returns on certain PPAs.²⁷ In doing so, he selectively picks language from
17 various rating agency reports to support his contentions, and he fails to consider
18 that it is not the existence of MYRPs or the aspects of recently enacted legislation
19 that reduces risk; rather, it is how these tools and mechanisms are implemented by

²⁴ Woolridge at times incorrectly cites PSE's S&P issuer credit rating as BBB+, when in actuality it is BBB. See Woolridge, Exh. JRW-1CT at 107:3-5.

²⁵ Parcell, Exh. DCP-1T at 17:18-18:2.

²⁶ Peterman, Exh. CGP-11T.

²⁷ Parcell, Exh. DCP-1T at 18:4-23:17.

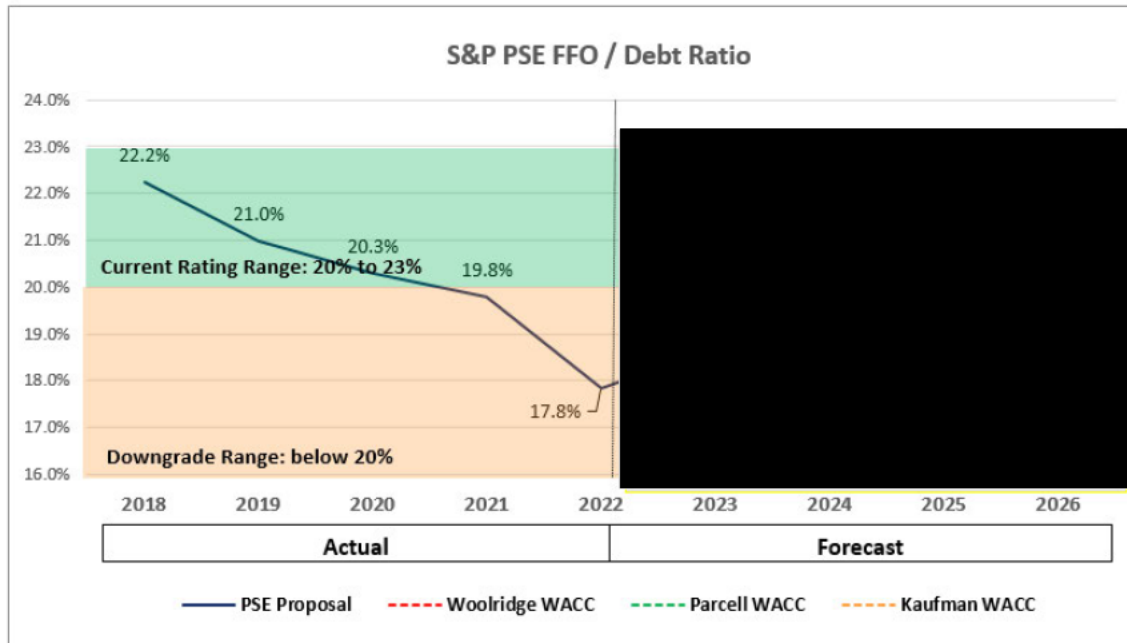
1 the Commission that could be risk reducing. Parcell's analysis of PSE's risk
2 profile is incomplete and misplaced due to his overreliance on the risk reducing
3 benefits of MYRPs and the provisions of recently passed legislation and lack of
4 consideration of the risk-increasing aspects of CETA and CCA in his analysis.

5 **Q. What credit metric analysis did AWEC witness Kaufman, Public Counsel**
6 **witness Woolridge, and Commission Staff witness Parcell present in support**
7 **of their recommended returns on equity, equity ratio, and weighted cost of**
8 **debt, collectively, the weighted cost of capital ("WACC")?**

9 A. It is not apparent from a detailed review of their respective testimonies that they
10 did any credit metric analysis in support of their respective recommendations for
11 the WACC. To analyze the credit metric impacts of their respective
12 recommendations for the WACC, PSE made the calculations as shown below:

1

Figure 1 – S&P Key Credit Metric Based on WACC Proposals

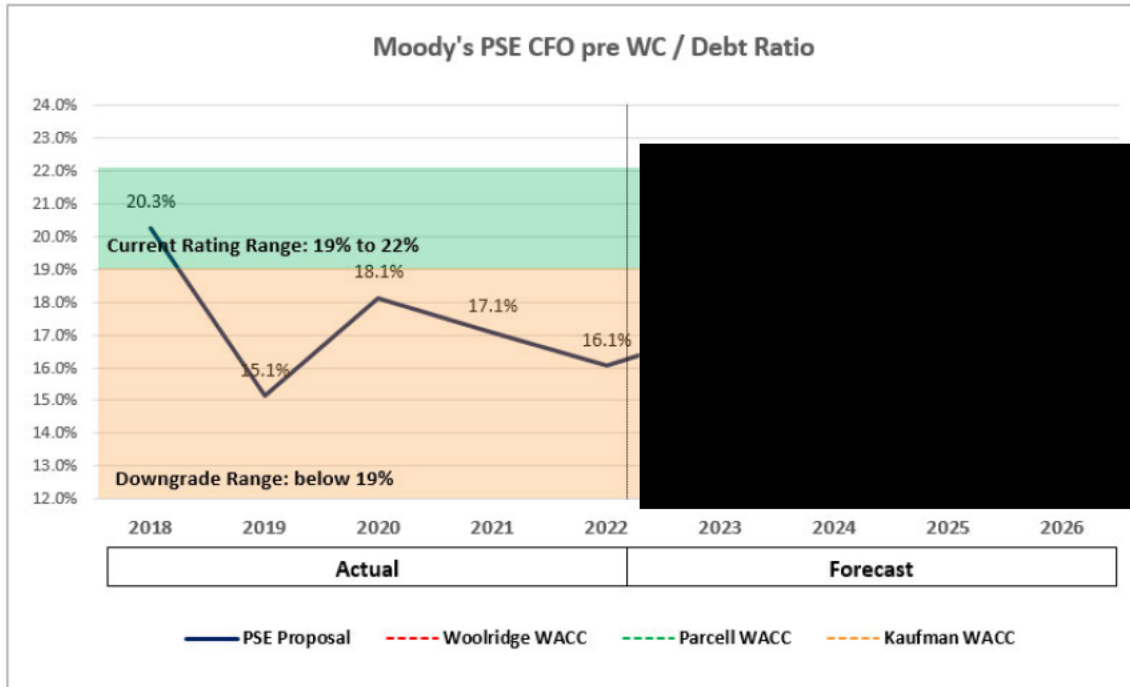


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Figure 2 – Moody's Key Credit Metric Based on WACC Proposals



2

3

Table 1 – Key Credit Metrics for WACC Proposals for MYRP

(A)	(B)	(C)	(D)	(E)	(F)	(G)
	Woolridge		Parcell		Kaufman	
	<u>2025</u>	<u>2026</u>	<u>2025</u>	<u>2026</u>	<u>2025</u>	<u>2026</u>
	<u>RP</u>	<u>RP</u>	<u>RP</u>	<u>RP</u>	<u>RP</u>	<u>RP</u>
<u>PSE Key Credit Metrics (PSE Proposal)</u>						
S&P FFO/Debt (20% downgrade threshold)						
Moody's CFO pre WC/Debt (19% downgrade threshold)						
<u>PSE Key Credit Metrics (WACC Change Only)</u>						
S&P FFO/Debt (20% downgrade threshold)						
Moody's CFO pre WC/Debt (19% downgrade threshold)						
<u>Key Credit Metrics Variance (BPS) (WACC Change Only)</u>						
S&P FFO/Debt						
Moody's CFO pre WC						

As can be seen in Figures 1 and 2, and Table 1 above, AWEC witness Kaufman, Public Counsel witness Woolridge, and Commission Staff witness Parcell, individually and collectively, recommend a WACC that [REDACTED], as I discussed above.²⁸ At a time when PSE must increase its cash flows and resulting credit metric performance to meet its responsibilities under the dual mandate and improve its credit metric performance to retain its current issuer ratings, it is clear that their recommended WACC will:

1. Keep PSE at or near the fourth quartile of returns on equity and equity ratio measured against its peers,²⁹ which will only detract from PSE's ability to attract and compete for both debt and equity capital on reasonable terms as it works to implement, finance, and operationalize its customer benefiting, operational risk reducing, CETA supportive [REDACTED] capital expenditure program over the next five years. Further, as discussed in Ms. Bulkley's rebuttal testimony, the parties in this proceeding have recommended ROEs that are approximately 20 to 50 basis points below the average of recently authorized ROEs across the country.³⁰

2. Undermine PSE's ability to [REDACTED]

[REDACTED]³¹

²⁸ See Peterman, Exh. CGP-11CT.

²⁹ See Doyle, Exh. DAD-1CT at 40:6-21, 41:1-9.

³⁰ See Bulkley, Exh. AEB-19T.

³¹ See Peterman, Exh. CGP-1CT at 33:7-15.

3. Be viewed as materially credit unsupportive, which will negatively impact the rating agencies' qualitative view of the state of regulation in Washington. This,

[REDACTED]

[REDACTED]

[REDACTED].³² This is discussed in more detail in the Prefiled Rebuttal Testimony of Todd A. Shipman, Exh. TAS-5T.

In the final analysis, the returns on equity, equity ratios, and weighted cost of debt recommended by AWEC witness Kaufman, Public Counsel witness Woolridge and Commission Staff witness Parcell, [REDACTED] [REDACTED] to the detriment of our customers, and must be rejected, if PSE is to have any viable chance to implement, finance, and operationalize its duties and responsibilities under the dual mandate.

Q. Did PSE perform any additional credit metric analysis based on the positions of the intervening parties in this proceeding?

A. Yes. As was stated earlier in this testimony, several intervening parties request that the Commission completely deny PSE's requests to include Beaver Creek CWIP in rate base and to accelerate gas depreciation. Additionally, Public Counsel and Commission Staff recommend reductions to PSE's O&M forecast, as discussed later in my testimony and in the Prefiled Rebuttal Testimony of Theresa R. Huizi, Exh. TRH-1T. Witness Peterman performed the analyses in the tables below to determine what the credit metric impact would be if the Commission

³² See generally Shipman, Exh. TAS-1T.

1 accepted the intervening parties' recommendations set forth above including the
2 already negative credit impacts of the returns on equity and equity ratios
3 recommended by AWEC witness Kaufman, Public Counsel witness Woolridge,
4 and Commission Staff witness Parcell. Tables 2 and 3, and Figures 3 and 4 below
5 illustrate PSE's calculations and results on key credit metrics:

Table 2 – Total Impact on Cash Flow for Credit Metrics

(A)	(B)	(C)	(D)	(E)	(F)	(G)
	Woolridge		Parcell		Kaufman	
	<u>2025</u> <u>RP</u>	<u>2026</u> <u>RP</u>	<u>2025</u> <u>RP</u>	<u>2026</u> <u>RP</u>	<u>2025</u> <u>RP</u>	<u>2026</u> <u>RP</u>
Total Rate Base	\$9,990	\$10,813	\$9,990	\$10,813	\$9,990	\$10,813
WACC Change due to Cost of Debt Correction	0.06%	0.10%	0.05%	0.11%	0.05%	0.10%
WACC Change due to ROE and Equity Ratio Proposal	-0.38%	-0.76%	-0.32%	-0.70%	-0.47%	-0.85%
Resulting Cash Flow Impact due to WACC Proposal	(\$32)	(\$72)	(\$27)	(\$64)	(\$41)	(\$81)
Impact of Removing Beaver Creek CWIP in Rate base Proposal	(22)	3	(22)	3	(22)	3
Impact of Accelerated Gas Depreciation Proposal	(70)	(67)	(70)	(67)	(70)	(67)
O&M Adjustments Proposal	(71)	(73)	(23)	(24)	0	0
Total Impact on Cash Flow for Key Credit Metrics	(\$195)	(\$208)	(\$142)	(\$152)	(\$133)	(\$145)

Figure 3 - S&P Key Credit Metric Based on WACC and Other Proposals

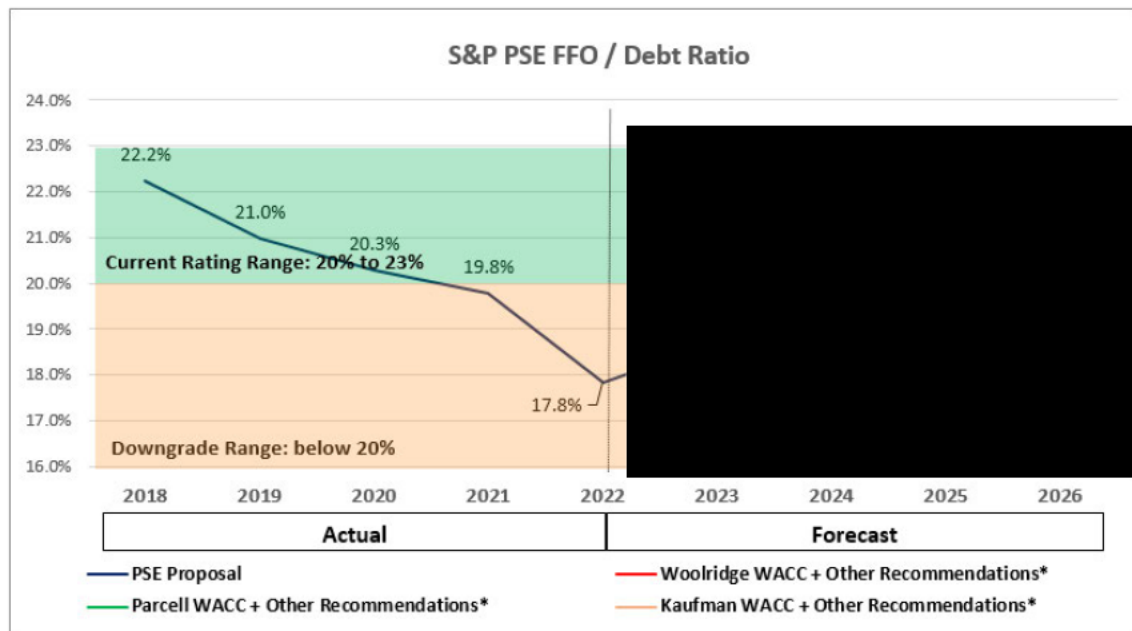
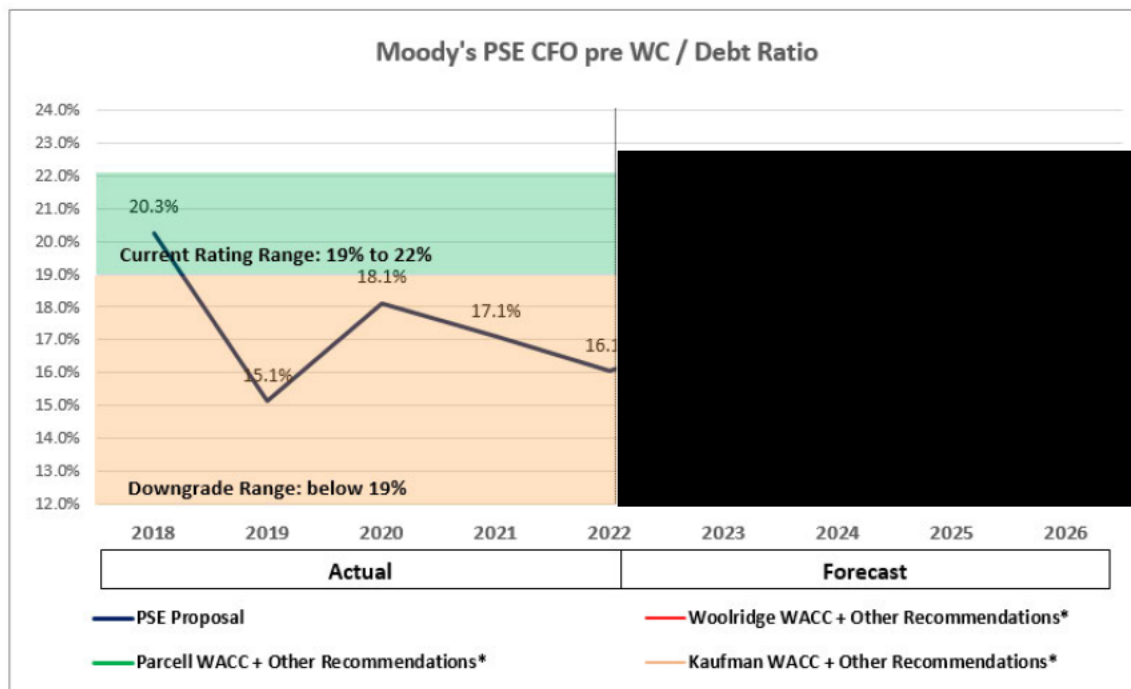


Figure 4 - Moody's Key Credit Metric Based on WACC and Other Proposals



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Table 3 – Key Credit Metrics with WACC and Other Proposals

(A)	(B)	(C)	(D)	(E)	(F)	(G)
	Woolridge		Parcell		Kaufman	
	<u>2025</u> <u>RP</u>	<u>2026</u> <u>RP</u>	<u>2025</u> <u>RP</u>	<u>2026</u> <u>RP</u>	<u>2025</u> <u>RP</u>	<u>2026</u> <u>RP</u>
<u>PSE Key Credit Metrics (PSE Proposal)</u>						
S&P FFO/Debt (20% downgrade threshold)						
Moody's CFO pre WC/Debt (19% downgrade threshold)						
<u>PSE Key Credit Metrics (WACC Change + Other Recommendations*)</u>						
S&P FFO/Debt (20% downgrade threshold)						
Moody's CFO pre WC/Debt (19% downgrade threshold)						
<u>Credit Metrics Variance (BPS) (WACC Change + Other Recommendations*)</u>						
S&P FFO/Debt						
Moody's CFO pre WC						

*Other Recommendations include: 1) No CWIP in rate base; 2) No accelerated gas depreciation; 3) O&M adjustments

The results of the above analyses demonstrate the material adverse impacts on PSE's credit metrics that would result from these proposals. In his Prefiled Rebuttal Testimony, PSE witness Shipman, a credit metric and analysis expert, concludes (based on the analysis above) that were the Commission to accept any of the recommended returns on equity and equity ratios proposed by the intervening parties, and simultaneously deny PSE's request for Beaver Creek CWIP in rate base and accelerated gas depreciation, and accept recommendations to reduce O&M expense, the rating agencies

1 [REDACTED] ³³ Such a result would have
2 material consequences for PSE and PSE's customers.

3 **Q. Commission Staff witness Parcell asserts in his testimony that the TCJA**
4 **passed by Congress in 2017, and the results of PSE's 2019 general rate case,**
5 **are "dated" events that provide improper justification for either a higher**
6 **return on equity or higher equity ratio in this proceeding.³⁴ Do you wish to**
7 **comment?**

8 A. Yes. With respect to TCJA, Parcell errs in his analysis. While it is true that TCJA
9 was enacted by Congress in 2017, Parcell overlooks the fact that TCJA has been
10 in force since that time and remains the governing tax code up to the present.
11 Accordingly, any assertion that TCJA is irrelevant for the purpose of selecting
12 returns on equity and equity ratios is incorrect and disregards important facts
13 regarding the significant, negative, cash flow impact of the TCJA on PSE, as
14 discussed in more detail in the Prefiled Rebuttal Testimony of Matthew R.
15 Marcelia, Exh. MRM-4T. In fact, PSE witness Marcelia documents in his prefiled
16 direct testimony that TCJA has an estimated \$156 million cash flow reducing
17 impact on PSE, due to the reduction of the corporate tax rate from 35 percent to
18 21 percent, which reduces cash flow for deferred taxes collected in rates, the loss
19 of bonus depreciation, and the return of excess deferred taxes to customers.³⁵
20 Furthermore, PSE witness Peterman documents in her prefiled direct testimony

³³ Shipman, Exh. TAS-5T.

³⁴ Parcell, Exh. DCP-1T at 60:16–61:17.

³⁵ Marcelia, Exh. MRM-1T at 21:10–24:15.

the impacts of lost cash flows due to TCJA on PSE's credit metric performance from the time TCJA became effective.³⁶ PSE witness Peterman's testimony in this regard demonstrates that TCJA has had a harmful impact on PSE's credit performance and those impacts persist to the present. For these reasons, the negative and persistent cash flow reducing aspects of TCJA are entirely relevant to the determination of PSE's return on equity and equity ratio in this proceeding.

With respect to the relevance of PSE's 2019 general rate case in the context of setting PSE's return on equity and equity ratio in this proceeding, Commission Staff witness Parcell errs in his response. First, he continues to explain the benefits of MYRPs. PSE's rebuttal of these contentions have been covered and the same points apply here: it is how MYRPs are *implemented* by the Commission that will ultimately determine if they are risk-reducing. That said, it is important to note that Parcell ignores Mr. Doyle's prefiled direct testimony which states,

"PSE expects that it will perform [REDACTED] [REDACTED]."³⁷ He further states, "PSE has not been able to earn its authorized ROE... PSE has consistently under earned its authorized ROE throughout the 2018 – 2022 period and expects to [REDACTED], [REDACTED]."³⁸ This troubling profile demonstrates that MYRPs or the implementation thereof are not, in and of itself, the risk reducing, financial stabilizing solution that Parcell would

³⁶ Peterman, Exh. CGP-1CT at 27:11-16; 28:9-14.

³⁷ Doyle, Exh. DAD-1CT at 19:19–20:3.

³⁸ Doyle, Exh. DAD-1CT at 24:1-6.

1 have us believe. Last, as Ms. Peterman testifies, the outcome of PSE's 2019
2 general rate case resulted in several negative actions by the rating agencies.³⁹
3 More specifically, S&P placed PSE on credit watch negative and Fitch reduced
4 PSE's Outlook from stable to negative.⁴⁰ Moody's cited the outcome of the 2019
5 general rate case as "unfavorable."⁴¹ This is an important fact and a stark
6 reminder that regulatory outcomes matter greatly to the rating agencies. In this
7 connection, the outcome of PSE's 2019 general rate case and the rating agency
8 actions that ensued are relevant and appropriate considerations in setting PSE's
9 return on equity and equity ratio in this proceeding.

10 **Q. Do you wish to comment on Section II of Public Counsel witness Gorman's**
11 **testimony titled "Financial Integrity"?**

12 A. Yes. In similar fashion to Commission Staff witness Parcell's testimony, Gorman
13 over relies on the risk reducing and financial stabilizing benefits of MYRPs and
14 concludes erroneously that because PSE's current issuer credit ratings are
15 accompanied by a stable outlook, PSE's risk profile is apparently unaffected by
16 the dual mandate.⁴² As PSE has stated elsewhere in this testimony, PSE did not
17 earn its allowed return on equity in 2023 and on a forecasted basis does not expect
18 to do so in 2024. MYRPs are in the developing stages of implementation and are
19 not the risk reducing and financial stabilizing solutions that Gorman describes in

³⁹ Peterman, Exh. CGP-1CT at 26:1–27:8; 30:14–31:9.

⁴⁰ Peterman, Exh. CGP-1CT at 28:1–7.

⁴¹ Peterman, Exh. CGP-9 at 48.

⁴² Gorman, Exh. MPG-1CT at 8:1–10:3.

1 his testimony. Further, Gorman misuses the concept of rating agencies stable
2 outlooks. They are not a measure of risk or rating agency concern as he asserts;⁴³
3 rather, they are simply an indication, at a specific point in time, that rating
4 agencies are not aware of any material impacts to a company's current issuer
5 rating that would cause a rating agency to change its current outlook to either
6 positive or negative depending upon the circumstances.

7 **Q. Does Public Counsel witness Gorman accurately characterize the S&P global**
8 **ratings study as it pertains to the assessment of regulation in the state of**
9 **Washington?**

10 A. Partially. On page 10 of his testimony, Gorman accurately states that S&P Global
11 Ratings rates Washington regulation as "very credit supportive".⁴⁴ However, on
12 page 11 of his testimony Gorman states, "As outlined in the figure above,
13 Washington has a rating of "very credit supportive" which places it among the
14 highest rating credit supportive categories of the 50 U.S. jurisdictions".⁴⁵ This
15 assertion is incorrect and is addressed in more detail in the Prefiled Rebuttal
16 Testimony of Todd A. Shipman, Exh. TAS-5T.

⁴³ Gorman, Exh. MPG-1CT at 8:1-5.

⁴⁴ Gorman, Exh. MPG-1CT at 10:16-20.

⁴⁵ Gorman, Exh. MPG-1CT at 11:1-3.

1 **B. JEA's Proposal To Lower the ROE on New Gas Customer Connections and**
2 **Capacity Expansions Is Unbalanced and Fails To Recognize PSE's**
3 **Obligation To Serve**

4 **Q. Do you agree with JEA witness Cebulko's proposal to reduce PSE's return**
5 **on equity for new gas customer connection and capacity expansions?**

6 A. No. JEA witness Cebulko proposes to reduce PSE return on equity for new gas
7 customer connection and capacity expansions to 0.75 percent lower than PSE's
8 approved return on equity for other gas capital investments.⁴⁶ If the Commission
9 took such a piecemeal approach to return on equity, then it should also allow a
10 higher return for clean energy resources that PSE acquires to meet its clean energy
11 targets and goals. The Commission has not awarded incremental return on equity
12 for rate base that promotes public policy; accordingly, it should not decrement
13 PSE's return on equity based on public policy objectives.

14 **Q. Do you have other concerns with Cebulko's proposal?**

15 A. Yes. Cebulko frames his proposal as a performance-based ratemaking incentive
16 that is consistent with current Commission policy. It is not a performance-based
17 ratemaking incentive. In reality, it is an unnecessary and inappropriate return on
18 equity penalty.

19 **Q. Please explain further.**

20 A. Certainly. At the present time, PSE has a legal obligation to serve gas customer
21 growth and incur project spending to serve customer requests in this regard. PSE

⁴⁶ Cebulko, Exh. CEG-1T at 4:15-17.

1 has no choice but to do so. However, Cebulko disregards that fact and proposes
2 as follows:

3 The company would continue to earn the same return for all
4 other categories of investments [i.e., non-growth related
5 investments] including emergency repair, mandatory
6 relocations and reliability projects. Furthermore, the
7 company would still earn a return on its equity for
8 investments that makes in the affected categories [i.e.,
9 growth-related investments], albeit at a slightly lower
10 profit. The idea is to incentivize the company to consider if
11 it could better deploy its funding to other projects that have
12 a higher ROE.⁴⁷

13 There are two problems with Cebulko's proposal. First, PSE has a legal obligation
14 to serve gas customer growth, and it has to incur project spending to meet this
15 customer demand. Accordingly, to suggest that PSE somehow has the ability to
16 deploy its funding to other projects that have a higher ROE and avoid its legal
17 obligation to serve gas customer growth is logically flawed. Second, there is
18 nothing to incentivize; when PSE's customers request gas service, PSE must
19 provide it. Stated alternatively, there is no need for performance-based ratemaking
20 incentives where legal obligations to serve exist.

21 **Q. You testified that JEA witness Cebulko's recommendation is, in reality, an**
22 **unnecessary and inappropriate return on equity penalty. How do you reach**
23 **this conclusion?**

24 A. As stated above, PSE has a legal obligation to serve gas customer growth.
25 Contrary to Cebulko's testimony, PSE does not have the ability to deploy project

⁴⁷ Cebulko, Exh. BTC-1T at 100:19-22 and 101:1-2.

1 spending away from serving gas customer growth investments to earn a higher
2 return on equity. Accordingly, under Cebulko's recommendation, PSE would be
3 penalized in its return on equity, in the amount of 75 basis points, for attending to
4 customer requests for gas service, which PSE has a legal obligation to provide.
5 For all the reasons stated above, PSE strongly recommends that the Commission
6 reject this proposal.

7 **III. PSE CONTINUES TO UNDEREARN AND THE PROPOSALS OF**
8 **INTERVENING PARTIES WILL ONLY EXACERBATE THE UNDEREARNING**

9 **Q. Do the proposals in the various response testimony address PSE's**
10 **underearning?**

11 A. No. As discussed throughout my testimony, many of the proposals are likely to
12 exacerbate PSE's prolonged and significant underearning discussed by PSE
13 witness Doyle, in his prefiled direct testimony. Moreover, as I have previously
14 discussed, the MYRP, in and of itself, does not fix PSE's credit metrics and has
15 not corrected PSE's underearning situation.

16 **Q. Earlier you testified that PSE forecasts that it will under earn in 2024. Can**
17 **you elaborate on the reason for this underearning?**

18 A. Yes, see Table 4 below. The following factors are contributing to PSE's under
19 earning in 2024:

20 First, in the final order in the 2019 general rate case, the Commission required
21 PSE to defer the return on its AMI investments until all the AMI equipment was

1 fully installed and the Commission could evaluate the use cases for the
2 equipment. Because of this requirement imposed by the Commission, PSE
3 continued to defer its return on equity on its AMI investments in the settlement in
4 its 2022 general rate case. In addition, PSE continued to defer a return on its
5 investment in Tacoma LNG Project as part of that same negotiated settlement.
6 Under generally accepted accounting principles, PSE cannot record, in its income
7 statement and results of operations, any equity returns that are not included in
8 rates. As a result, PSE's allowed rate of return under earned by a combined after-
9 tax total of \$18 million or 33 basis points.

10 Second, in January 2024, PSE's electric and gas operating systems set record
11 peaks during an extended winter cold streak. On the electric side of the business,
12 even though PSE served every kilowatt hour of demand, PSE incurred a \$36
13 million pretax loss to the net income and results of operations in these
14 extraordinary conditions due to the continuing impacts of the PCA sharing bands.
15 On a forecasted basis, all else equal, PSE expects to incur an after-tax \$28 million
16 reduction to net income and a 51 basis point reduction to its otherwise allowed
17 return on equity.

18 Third, during the second quarter of 2024, the Commission ruled on PSE's final
19 prudence and inclusion of the Tacoma LNG investment into rates. In doing so the
20 Commission disallowed \$15 million of PSE's deferred equity returns,⁴⁸ which it

⁴⁸ *WUTC v. PSE*, Docket UG-230393 Order 07 ¶ 153 (April 24, 2024) (allowing deferred O&M expenses and depreciation, but not a return on the investment for the period up to January 11, 2023).

could not heretofore include in earnings due to the restrictions of generally accepted accounting principles as described above. This resulted in a \$12 million after-tax reduction to PSE's net income and a 22 basis point reduction to its otherwise allowed return on equity.

Fourth, PSE's AFUDC returns on equity and debt on CWIP and other items on the balance sheet are insufficient to reflect, in its income statement and results of operations. ~~In essence,~~ PSE's deploys capital at a higher cost than the AFUDC calculation allows PSE to record. This creates a regulatory drag of \$[REDACTED] million reduction to PSE's net income or a [REDACTED] basis point reduction to its otherwise allowed return on equity. These amounts include the effects of unrecovered book interest expense in excess of interest expense allowed in rates.

Fifth, PSE will incur below the line expenses, which have been historically denied inclusion in rates, in the after-tax amount of \$[REDACTED] million or [REDACTED] basis points of under-earned return on equity. The vast majority of these expenses relate to PSE's long-term incentive compensation plan, governmental affairs and lobbying, and a \$10 million investment in Energy Northwest's efforts to develop small modular reactor that could generate up to 960 MW of electricity. PSE's investment secures an option and a priority claim on future developed capacity for the benefit of customers should the technology prove viable and cost-effective. These expenses are not included in rates based on long standing commission policy and state law. PSE raises them here because they represent legitimate and necessary costs of

doing business and because they are not included in rates, they represent an annual regulatory policy drag on PSE's ability to earn its allowed equity return.

Sixth, PSE incurred unrecoverable regulatory interest expense on refundable PGA regulatory liabilities. This reduced net income and results of operations by \$ million after tax and basis points of under earned return on equity.

Seventh, PSE expects that it will incur O&M expenditures, over and above what it has embedded in its current revenue requirement, by \$ million pre-tax or \$ million after tax, which equates to basis points under earned return on equity.

PSE has no choice but to incur these expenses to operate its business. The additional O&M expense was used to fund necessary work in the business including customer outage response and wildfire prevention. As I discuss in more detail later in my testimony, further cuts to O&M expense in the rate years are not sustainable. Table 4 below breaks out these causes of under earning.

Table 4 – 2024 Under Earning Analysis

2024 ROE Under Earning Analysis (After Tax)		
1	Deferred Return on Equity-AMI and LNG	\$18
2	PCA PSE Share	28
3	LNG Deferred Equity Return Disallowance	12
4	CWIP & Other Balance Sheet Regulatory Drag	
5	Below-the-line expenses	
6	Unrecoverable Regulatory Interest Expense	
7	Excess O&M spending vs. Rate Recovery	
8	Total	
9		
10	Regulated AMA Equity	\$
11		
12	Allowed Return on Equity %	9.40
13	Total Forecasted Lag and Drag-ROE Lost %	
14	Net, Forecasted Earned Return on Equity %	

1 **Q. What are your conclusions in this regard?**

2 A. Various intervening witnesses including McGuire, Parcell, and Woolridge⁴⁹ have
3 presented testimony extolling the virtues and risk reducing aspects of MYRPs.
4 The above analyses demonstrate that intervenors' testimonies do not place a keen
5 eye on the totality of the Washington regulatory environment. PSE demonstrates
6 in the analyses above that the vestiges of historical ratemaking and Commission
7 policymaking (e.g., PSE's share of PCA, Commission policy determinations
8 related to earning cash returns on AMI and LNG, Commission mandated
9 disallowances related to deferred returns on equity related to LNG, unrecoverable
10 below the line expenses, and unrecoverable regulatory interest expense) can and
11 do have, collectively and independently, very negative impacts that undermine
12 PSE's ability to earn its allowed return on equity. Thus, it is incorrect to view
13 legislation authorizing MYRPs as a risk reducing, cash flow enhancing remedy
14 without considering the significant and material variables that exist in
15 Washington. The intervening parties ignore this important context, and their
16 recommendations in this regard only serve to incrementally and negatively chip-
17 away at PSE's ability to earn its allowed return on equity. While MYRPs, in and
18 of themselves, are a regulatory step forward from the state of Washington's
19 traditional historical ratemaking, implementing this tool effectively is a critical
20 action and one that remains in its early stages. The mere existence of MYRPs
21 should not be credibly used to refute and deny the proposals PSE has made in this

⁴⁹ See generally McGuire, Exh. CRM-1Tr; Parcell, Exh. DCP-1T; Woolridge, Exh. JRW-1T.

1 proceeding to improve its overall credit profile, increase its cash flows, enhance
2 its ability to attract and compete for capital at reasonable prices, and to fulfill its
3 responsibilities under the dual mandate.

4 **IV. COMMISSION STAFF'S TRACKER STANDARDS SHOULD BE**
5 **REJECTED**

6 **Q. Please summarize the primary recommendations of Commission Staff**
7 **witness McGuire regarding PSE's proposals for a Clean Generation**
8 **Resource Tracker, a Wildfire Prevention Plan Rate Adjustment, and a**
9 **Decarbonization Rate Adjustment.**

10 A. McGuire opposes the Clean Generation Resources Tracker and the
11 Decarbonization Rate Adjustment.⁵⁰ He possibly supports the Wildfire
12 Prevention Plan Adjustment Rider with a risk sharing mechanism.⁵¹ In general,
13 his position is to include the costs in base rates rather than in a tracker or rate
14 adjustment mechanism.

15 **Q. How do you respond generally to his position regarding these mechanisms?**

16 A. I am concerned that McGuire does not understand the role these mechanisms play
17 in allowing PSE to recover its costs for important policy objectives—clean
18 energy, decarbonization, and wildfire prevention. In her rebuttal testimony, PSE
19 witness Susan E. Free discusses why the tracker and rate adjustment mechanisms

⁵⁰ McGuire, Exh. CRM-1Tr at 55:1-9; 66:8-17.

⁵¹ McGuire, Exh. CRM-1Tr at 63:5-64:2.

1 are important from a rate recovery standpoint for these important initiatives.⁵²
2 PSE witness Matt Steuerwalt also responds to this proposal in his rebuttal
3 testimony, discussing that this general rate case is not the appropriate venue for
4 setting broad policies on trackers that affect numerous regulated entities and
5 interested parties beyond this case.⁵³ In addition, PSE witness Shipman rebuts
6 McGuire's contention that tracker mechanisms "shift risk" from shareholders to
7 rate payers and elaborates on the potential negative credit rating impacts of
8 McGuire's recommendations.

9 **Q. Are there other statements in Mr. McGuire's testimony that you find to be**
10 **inaccurate?**

11 A. Yes. He incorrectly states that PSE is being compensated through its ROE to
12 assume the variance risk related to the various trackers currently in operation in
13 PSE's tariffs.⁵⁴ McGuire errs materially in this regard. As Todd Shipman
14 testifies in his rebuttal testimony, the use of tracker mechanisms has expanded
15 significantly since the energy crisis in the late 1970s and every state commission
16 in the United States employs the use of trackers in various forms.⁵⁵ In general,
17 most commissions, including the Washington Commission, capture the potential
18 risk-reducing impacts of trackers when setting ROEs. PSE is aware that the
19 Commission does just that in PSE's GRCs.

⁵² Free, Exh. SEF-28T.

⁵³ Steuerwalt, Exh. MS-4T.

⁵⁴ McGuire, Exh. CRM-1Tr at 33:18-22.

⁵⁵ Shipman, Exh. TAS-5T.

1 **Q. What authoritative support can you provide that the Commission considers**
2 **the potential risk reducing impacts of trackers when setting ROE?**

3 A. In Dockets UE-121697 and UG-121705, in which the Commission approved
4 PSE's electric and natural gas decoupling mechanisms, the Commission
5 considered whether the risk reducing nature of decoupling required an adjustment
6 to PSE's ROE. The Commission stated in its remand order:

7 The Commission has never tried to account separately in its
8 ROE determinations for specific risks or risk mitigating
9 factors [associated with tracker mechanisms], nor should it.
10 Circumstances in the industry today and modern regulatory
11 practice that have led to a proliferation of risk reducing
12 mechanisms being in place for utilities throughout the
13 United States make it particularly inappropriate and
14 unnecessary to consider such an undertaking. The effects of
15 these risk mitigating factors was by 2013, and is today,
16 built into the data experts draw from the samples of
17 companies they select as proxies.⁵⁶

18 In short, the Commission determined that the cost of capital and peer group
19 studies it considers when setting ROEs implicitly capture the risk reducing
20 impacts of tracker mechanisms. This conclusively demonstrates that PSE is not
21 being over-compensated in its ROE as McGuire suggests, and the foundational
22 premise of his proposal is entirely flawed. Clearly, for costs being recovered in
23 trackers (except for the PCA due to its sharing bands) there is no variance risk
24 assumed by PSE and neither is PSE improperly compensated in its ROE for risk

⁵⁶ *WUTC v. Puget Sound Energy*, Dockets UE-121697 and UG-121705, Order 15, ¶ 155 (June 29, 2015).

1 that does not exist. Stated more simply, tracker variance risk and ROE
2 compensation are largely in balance.

3 **Q. Should the Commission evaluate the effects of PSE's proposed tracker and**
4 **rate adjustment mechanism in setting its allowed return on equity?**

5 A. No. As stated in its order in Dockets UE-121697 and UG-121705, "The
6 Commission has never tried to account separately in its ROE determinations for
7 specific risks or risk mitigating factors [associated with tracker mechanisms], nor
8 should it."⁵⁷ The Commission looks to cost of capital and peer group studies to
9 implicitly capture the effects of trackers when setting the ROE in GRCs.

10 **Q. Will such an approach result in PSE's return on equity being set higher than**
11 **it should be?**

12 A. No. The Commission did not examine the risk increasing aspects of growing
13 wildfires, decarbonization requirements, and CETA, in setting PSE's return on
14 equity over the last several years. In fact, PSE's return on equity has decreased
15 over the past decade, despite the introduction of these additional risks. The
16 existence of trackers and rate adjustment mechanisms will be subsumed in the
17 determination of ROE in this case.

⁵⁷ *Id.*

1 **Q. Commission Staff witness McGuire testifies that the Commission should**
2 **require a risk sharing mechanism when it authorizes all such trackers and**
3 **cost recovery mechanism.⁵⁸ Do you have concerns with his proposal?**

4 A. I do. As the Commission noted in PSE's decoupling dockets referenced above,
5 tracker and other risk reducing mechanisms are widely employed across the
6 United States; however, risk sharing mechanisms are not widely deployed across
7 the United States. Accordingly, were the Commission to require, at some point in
8 the future, risk sharing mechanisms in all of PSE's existing tracker mechanisms,
9 PSE's cost recovery would become more volatile as would PSE's cash flows,
10 earnings, and returns on equity, relative to its peers across the United States. In
11 short, PSE would become more risky than its peers across the United States This
12 would create a serious and potentially material disconnect when the Commission
13 considers cost of capital studies and peer group analyses when setting PSE's ROE
14 in the future. Those studies and analyses would no longer implicitly consider the
15 risk increasing aspects of risk sharing mechanism, because risk sharing
16 mechanisms are not widely deployed in the United States and would not be
17 reflected in the peer group analysis or the ultimate cost of capital study
18 recommendations the Commission would use to set PSE's ROE.⁵⁹ This is
19 discussed in the Prefiled Rebuttal Testimony of Cara G. Peterman, Exh. CGP-
20 11CT, in which she cites a recent S&P report that says the additions of risk-
21 sharing tools in tracker mechanisms will be seen as a reversal of recent credit

⁵⁸ McGuire, Exh. CRM-1Tr at 52:4-5.

⁵⁹ See Bulkley, Exh. AEB-19T.

1 supportive actions and detrimental to utility financial security. This is not an
2 immaterial matter given that PSE recovers over 50 percent of its revenue
3 requirement through various tracker mechanisms, PCA, PGA, CCA and
4 conservation being the most significant. Thus, requiring risk sharing mechanisms
5 as a matter of tracker mechanism regulatory policy would require an adjustment
6 to the Commission's current approach for setting ROEs to reflect the impact such
7 a proposal would have on cash flow and earnings volatility.

8 **Q. Are you concerned about any other aspects of McGuire's proposal?**

9 A. Yes. McGuire presents his proposal with little or no financial analysis and
10 suggests that his policy proposal should be imposed incrementally in the
11 Washington state regulatory environment without analyzing its contextual impact
12 on that very environment. Stated alternatively, McGuire asks the Commission to
13 approve his tracker policy proposal without any analysis of how that policy
14 proposal will interact with other cost recovery mechanisms and regulatory
15 policies. As I state above, there are a myriad of regulatory policy and ratemaking
16 practices that collectively present an accurate context for assessing the
17 incremental impact of McGuire's recommendations on the totality of the
18 regulatory environment in the state of Washington. PSE does not believe the
19 Commission should entertain McGuire's proposal until that analysis can be
20 presented and explored in an all-inclusive proceeding.

1 **Q. What are your conclusions?**

2 A. The root of McGuire's proposal is that, except in limited circumstances,
3 ratepayers should not be burdened with what he calls "variance risk" because
4 ratepayers are compensating for that risk in the form of higher returns on equity.
5 PSE has already rebutted McGuire's contention that ratepayers are paying for
6 variance risk in the context of PSE's allowed rate of return those same points
7 apply here. However, as I have shown elsewhere in my testimony, PSE is already
8 significantly underearning its authorized return on equity by ■ basis points, or
9 more than ■ percent, much of which is due to regulatory policies. Despite this
10 underearning, McGuire asks this Commission to increase the volatility of PSE's
11 cash flow, earnings, and return on equity above and beyond what PSE expects to
12 experience in 2024. The data above clearly illustrate that a confluence of existing
13 ratemaking practices and regulatory policies already undermine PSE's ability to
14 earn its allowed rate of return. The Commission should resist any attempt to
15 incrementally add, delete or materially restructure ratemaking tools and practices
16 in a manner that increases volatility and risk regarding cash flow, earnings, and
17 returns on equity.

1 **V. FURTHER CUTS TO O&M AS PROPOSED BY COMMISSION STAFF**
2 **AND INTERVENING PARTIES WILL UNDERMINE PSE’S ABILITY TO**
3 **TRANSITION TO CLEAN ENERGY WHILE PROVIDING SAFE AND**
4 **RELIABLE SERVICE**

5 **Q. Do parties propose cuts to PSE’s operations and maintenance budget in the**
6 **multiyear rate plan?**

7 A. Yes. Commission Staff witness McGuire proposes to decrease PSE’s O&M
8 budget by \$24 million reduction in 2025 and 2026.⁶⁰ Additionally, Public
9 Counsel witness Meyer proposes to decrease PSE’s O&M spending by \$62
10 million in 2025 and \$64 million in 2026.⁶¹

11 **Q. How do you respond to these proposals?**

12 A. I respond at a high level, while PSE witness Theresa Huizi and PSE witness
13 Susan E. Free respond to the details of these proposed cuts in their respective
14 rebuttal testimony.⁶²

15 **Q. What are your high-level concerns?**

16 A. The proposed cuts seem likely to hurt customers by compromising PSE’s ability
17 to perform its dual mandate. I do not believe PSE can continue to safely and
18 reliably provide electric and gas service to its customers while moving toward
19 decarbonization and a clean energy transition, if PSE’s O&M expenditures are cut
20 as proposed by Commission Staff and Public Counsel. As discussed in the

⁶⁰ McGuire, Exh. CRM-1Tr at 121:12-16.

⁶¹ Meyer, Exh. GRM-1CT at 31:8–32:8.

⁶² Huizi, Exh. TRH-1T; Free, Exh. SEF-28T.

1 Prefiled Direct Testimony of Daniel A. Doyle, Exh. DAD-1CT, PSE already has
2 made significant cuts to its O&M budget in 2023 and these savings were
3 incorporated into the development of its 2024 budget as well as the rate years in
4 this case in order to make headroom in rates for the substantial increase in capital
5 investments required to implement the dual mandate.⁶³ Moreover, if there was
6 any “fat” to cut, PSE would have done so in order to remediate its underearning
7 discussed above. It did not do so because PSE views this O&M expense to be
8 critical to operate the business. Additional cuts are not sustainable. PSE has
9 proposed a reasonable amount of O&M expense in its rate years.

10 It is also important to recognize that PSE’s O&M expenditures are low as
11 compared to other utilities. As described in more detail by PSE witness Huizi in
12 her rebuttal testimony, PSE’s O&M per customer is in the first quartile of peer
13 utilities, and PSE has historically kept its O&M costs reasonable.

14 **Q. What would the impact of adopting parties’ positions on O&M expense be on**
15 **PSE’s operations?**

16 A. As described in the prior section and elaborated on in PSE witness Huizi’s
17 rebuttal testimony, PSE’s O&M costs are reasonable, aligned with important
18 categories of work including electric and gas system maintenance for safety and
19 reliability, emergency response, and the clean energy transition. PSE has
20 exercised significant control over its costs for many years and as a result, does not

⁶³ Doyle, Exh. DAD-1CT at 25:1-19.

1 have room to further reduce its costs without eroding the customer experience and
2 impacting the ability to meet customers' future needs. If parties' positions are
3 adopted, PSE will make difficult decisions on what work it will no longer perform
4 and customers will experience different outcomes. As a first area of focus for
5 reductions, PSE will significantly scale back its work associated with the Clean
6 Energy Implementation Program, including customer education programs, CETA
7 administration, targeted electrification and distribution energy resource
8 planning. If further reductions are necessary to align spend with the GRC
9 outcome, other areas of PSE's service quality will be impacted, including non-
10 emergency customer response times, inability to deliver on growing need for
11 outreach in support of named communities, electric reliability, as well as the work
12 to coordinate PSE's long term transmission and distribution investments with
13 local governments. For context, the Commission has established a series of
14 service quality indices, many of which represent O&M costs. Indices that would
15 be impacted by further reductions to PSE's O&M expense budget include longer
16 times to reach a live representative for non-emergencies, longer wait times for
17 customer appointments, and worsening reliability performance.

1 **VI. THE COMMISSION HAS AUTHORITY TO AUTHORIZE AND SHOULD**
2 **AUTHORIZE PSE TO EARN A RETURN ON PPAS**

3 **Q. Did any of the intervening parties address PSE's request to earn a rate of**
4 **return on certain of its PPAs for which it is requesting rate recovery in this**
5 **proceeding?**

6 A. Yes. Despite the fact that RCW 80.28.410 allows the Commission to authorize a
7 return on certain PPAs, several parties oppose PSE's proposal to earn a return on
8 its AutoGrid, Oracle, and EnelX demand response PPAs.

9 Commission Staff witness McGuire presents testimony in support of PSE's
10 request to earn a rate of return on certain of its PPAs, but McGuire adjusts PSE's
11 proposal to earn on the subject PPAs at PSE's overall rate of return and in its
12 place recommends that the return be based on PSE's embedded cost of debt.⁶⁴

13 Public Counsel witness Gorman presents testimony requesting that the
14 Commission deny PSE's request to earn a return on certain of its PPAs.⁶⁵ Gorman
15 does state in his testimony, however, that if the Commission is inclined to allow a
16 return on certain of PSE's PPAs as proposed in this proceeding, it should do so at
17 PSE's embedded cost of debt.⁶⁶ This latter point aligns with McGuire's
18 recommendation.

⁶⁴ McGuire, Exh. CRM-1Tr at 80:1-4.

⁶⁵ Gorman, Exh. MPG-1CT at 25:20-26:13.

⁶⁶ Gorman, Exh. MPG-1CT at 26:6-13.

1 AWEC witness Mullins correctly notes that not only is the Commission
2 authorized by law to allow a return on PPAs, but in addition the settlement
3 agreement in PSE's 2022 multiyear rate plan stated that demand response PPAs
4 would be eligible for potential earning on the PPAs. Even so, he opposes PSE's
5 proposal.⁶⁷

6 JEA witness McCloy agrees that the demand response PPAs are prudent but
7 argues against PSE earning a return on them, preferring instead a PIM.⁶⁸

8 The Energy Project witness Stokes testifies that the Commission is not required to
9 provide PSE a rate of return for PPAs and it should not do so.⁶⁹ In essence,
10 Stokes's argument seems to be that the Commission should never allow a return
11 on a PPA, despite the legislature authorizing such a return.

12 **Q. Do you wish to comment further?**

13 A. Yes. RCW 80.28.410(2)(b) allows the Commission to approve a return on certain
14 PPAs within the range of PSE's authorized rate of return at the high-end and its
15 approved embedded cost of debt on the low-end. In its initial testimony, PSE
16 requested that the Commission consider authorizing a return on certain of PSE's
17 PPAs at the higher end of the range, more specifically at its approved rate of
18 return. PSE requested a return on PPAs for two reasons in this proceeding. First,
19 earning returns on PPAs, on the margin, makes PSE more indifferent to whether it

⁶⁷ Mullins, Exh. BGM-1T at 29:10–30:18.

⁶⁸ McCloy, Exh. LCM-1T at 15:20–16:4.

⁶⁹ Stokes, Exh. SNS-1T at 56:1–58:7.

1 purchases energy and capacity versus building and owning facilities that are
2 included in rate base and earn a full rate of return. Second, in its attempt to
3 continually manage credit metrics and its overall credit profile, PSE believes that
4 earning a return on PPAs has significant policy benefits to manage credit metric
5 pressures in discussions with the rating agencies. While it is true that PSE witness
6 Doyle testified that PSE would accept a return at its authorized cost of debt
7 because it would still achieve the policy benefits of allowing PSE to earn a return
8 on qualifying PPAs,⁷⁰ it is also true that the customer scale distributed energy
9 resources and demand response PPAs for which PSE seeks to earn a return are the
10 type of PPAs that should earn a return at the higher end of the spectrum. These
11 PPAs have a much higher administrative burden, and most likely have a higher
12 equity value per MW, than contracting for utility scale resources to meet resource
13 needs. For this reason, the demand response PPAs for which PSE seeks a return
14 are deserving of something closer to the higher end of the range of earnings. It is
15 reasonable to assume that the legislature included a range of allowable returns
16 based on the assumption that some resources are more deserving of the higher end
17 of the range than others. For the reasons discussed, it is appropriate for PSE to
18 earn a return at the higher end of the range for these customer-scale PPAs.

⁷⁰ See Doyle, Exh. DAD-1CT at 76-77.

1 **Q. How do you respond to Public Counsel witness Gorman's testimony**
2 **regarding PSE's request for earning a return on certain PPAs?**

3 A. On page 24 of his testimony, Gorman states, "In order to produce a ratemaking
4 capital structure that balances the amount of debt leverage with the utilities cost of
5 service, utilities often increase their ratemaking common equity ratio to offset its
6 total leverage risk including on balance sheet and off-balance-sheet equivalents.
7 Increasing the common equity ratio of the ratemaking capital structure increases
8 the utilities revenue requirement to recognize the existence of PPAs and their
9 debt-like characteristics."⁷¹ While PSE cannot comment on whether other
10 utilities make the adjustments that Gorman describes, PSE does not make such
11 adjustments and did not make them in this case. Gorman's inference that PSE
12 made such adjustments is incorrect.

13 Further, Gorman states, "the combination of increasing ratemaking common
14 equity ratio and providing a full return on PPAs imposes double cost impact on
15 customers for the existence of PPAs."⁷² In short, Gorman explicitly opines that
16 PSE increased its equity ratio in its cost of capital to cover the off-balance-sheet
17 aspects of imputed debt on PPAs by rating agencies and then double dips to the
18 customers' detriment by requesting returns on PPAs. First, as previously stated,
19 PSE makes no adjustments to its capital structure to consider any form of off-
20 balance-sheet financing, including imputed debt related to PPAs. Second, PSE has

⁷¹ Gorman, Exh. MPG-1CT at 24:6-12.

⁷² Gorman, Exh. MPG-1CT at 24:18-20.

1 requested an increase in its equity ratio in this proceeding because its current
2 equity ratio ranks at or near the fourth quartile of its peers.⁷³ Contrary to
3 Gorman's assertion, PSE requests that its equity ratio be increased in this
4 proceeding in order to increase cash flows, improve its credit metrics, and better
5 position PSE to compete for and attract both debt and equity capital to fund the
6 capital expenditure program that PSE must undertake to meet the requirements of
7 the dual mandate. Gorman is inaccurate in his assertion on this point.

8 Third, Gorman incorrectly states that PSE's imputed debt is lower than S&P's
9 actual calculations and he inaccurately suggests that PSE's imputed debt is being
10 amortized toward zero.⁷⁴ PSE witness Peterman rebuts this argument. PSE's
11 forecasted imputed debt is expected to rise significantly under CETA and thus,
12 this matter is important to PSE.

13 Lastly, as discussed above, there are two primary reasons why PSE has requested
14 to earn a return on certain PPAs in this proceeding: (1) to make PSE more
15 indifferent to whether it purchases energy and capacity versus building and
16 owning facilities that are included in rate base and earn a full rate of return, and
17 (2) to manage credit metrics and PSE's overall credit profile. PSE's requests (i) to
18 earn returns on PPAs and (ii) to increase its equity ratio are separate and distinct
19 from one another, as is the underlying rationale that supports those requests.

⁷³ Doyle, Exh. DAD-1CT at 14:10-18.

⁷⁴ Gorman, Exh. MPG-1CT at 25:1-7, n. 23.

1 Contrary to Gorman's assertion, there is no connection between these requests by
2 PSE, and as such, there is no double dip.

3 PSE witnesses Matt Steuerwalt and Susan Free provide further rebuttal testimony
4 addressing the appropriateness of PSE's request to earn a return on demand
5 response PPAs in their prefiled rebuttal testimony.⁷⁵

6 **VII. CWIP IN RATE BASE**

7 **Q. How did the intervening parties respond to PSE's request to include Beaver**
8 **Creek CWIP in rate base?**

9 A. While several intervening parties encourage the Commission to reject and deny
10 PSE's request for CWIP in rate base, none of the parties took a position that
11 relevant state law precludes the Commission from approving PSE's request.
12 Importantly, in his testimony, Commission Staff witness McGuire concludes
13 affirmatively that current state law allows the Commission to include CWIP in
14 rate base if it determines that doing so is in the public interest.⁷⁶ PSE agrees.
15 This is discussed in more detail in the Prefiled Rebuttal Testimony of Matt
16 Steuerwalt, Exh. MS-4T.

⁷⁵ Steuerwalt, Exh. MS-4T; Free, Exh. SEF-28T.

⁷⁶ McGuire, Exh. CRM-1Tr at 88:13-20.

1 **Q. Does PSE wish to comment on the intervening parties' testimonies as it**
2 **relates to their recommendations to reject and deny PSE's request for CWIP**
3 **in rate base?**

4 A. Yes. The following witnesses provided testimony regarding PSE's request for
5 CWIP in rate base:

- 6 1. Public Counsel witness Gorman;
- 7 2. AWEC witness Mullins;
- 8 3. Commission Staff witness McGuire;
- 9 4. JEA witness Gehrke.
- 10 5. TEP witness Stokes

11 I will address 1-4 above. PSE witness Susan Free will address TEP witness
12 Stokes's testimony.

13 **A. PSE's Response to Public Counsel Testimony on CWIP in Rate Base**

14 **Q. On page 19 of his testimony, Public Counsel witness Gorman states that PSE**
15 **did not outline the costs and benefits to customers based on PSE's CWIP in**
16 **rate base proposal.⁷⁷ Does PSE agree?**

17 A. No. PSE witness Doyle's prefiled direct testimony is replete with cost-benefit
18 analysis including:

⁷⁷ Gorman, Exh. MPG-1CT at 19:14-21.

- 1 1. Pages of testimony that illustrate that CWIP in rate base is less expensive to
2 customers than traditional AFUDC practices.⁷⁸
- 3 2. Consideration of the fact that CWIP in rate base is more risk reducing and credit
4 supportive than traditional AFUDC practices, which if applied on a broad basis
5 (versus the single project treatment of CWIP in rate base) could have positive
6 impacts on the long-term cost of financing PSE's capital expenditure program
7 over time.⁷⁹
- 8 3. Consideration of the fact that CWIP in rate base reduces external financing
9 pressure on the margin because CWIP is a cash producing ratemaking tool,
10 supporting PSE's efforts to implement the clean energy transition.⁸⁰
- 11 4. Consideration that the CWIP in rate base methodology reduces and mitigates
12 rate impacts to customers compared to when a project goes into service having
13 been treated under the traditional AFUDC practice.⁸¹

14 **Q. Public Counsel witness Gorman cites intergenerational equity challenges that**
15 **attend to PSE's CWIP in rate base proposal.⁸² Do you wish to comment?**

16 A. Yes. If the Commission approves PSE's CWIP in rate base proposal, customers
17 would only fund that treatment for a period of less than one year in the case of
18 PSE's Beaver Creek project. As such, Gorman's contention that PSE's request
19 should be denied based on intergenerational equity concerns is not accurate.

⁷⁸ Doyle, Exh. DAD-1CT at 64:10–70:20; 78:5–89:3.

⁷⁹ Doyle, Exh. DAD-1CT at 66:15–68:5.

⁸⁰ Doyle, Exh. DAD-1CT at 66:1–14.

⁸¹ Doyle, Exh. DAD-1CT at 68:6–19.

⁸² Gorman, Exh. MPG-1CT at 20:1–21:13.

1 There is no intergenerational equity issue. Further, Gorman overlooks the fact that
2 rate impacts will be mitigated to customers when the Beaver Creek project is
3 placed in service. No ratemaking practice is perfect, and there are positive and
4 negative aspects to customers for both CWIP in rate base and traditional AFUDC
5 practices. In the case of PSE's Beaver Creek project, any intergenerational equity
6 concern is offset by the positive impacts of rate mitigation. As PSE witness Doyle
7 stated in his prefiled direct testimony, PSE's Beaver Creek project is an
8 appropriate test case for the Commission to evaluate the usefulness and
9 appropriateness of CWIP in rate base treatment as the state of Washington
10 embarks on its journey to comply with the decarbonization mandates included in
11 CETA and CCA.⁸³

12 **Q. On page 21 of his testimony, Public Counsel witness Gorman suggests that**
13 **PSE witness Doyle presents a completely backward analysis of the cash flow**
14 **impacts of CWIP in rate base versus the traditional AFUDC practice.⁸⁴ Does**
15 **PSE wish to comment?**

16 A. Yes. On page 21 of his testimony, Gorman states that PSE witness Doyle
17 commented that "allowing for a current return on CWIP would increase the non-
18 cash levels of AFUDC earnings, which would be perceived as an increase in PSE
19 investment risk and would require a higher rate of return by investors."⁸⁵ What
20 PSE witness Doyle actually stated in his prefiled direct testimony is the following:

⁸³ Doyle, Exh. DAD-1CT at 62:8–63:7.

⁸⁴ Gorman, Exh. MPG-1CT at 21:14-23.

⁸⁵ Gorman, Exh. MPG-1CT at 21:14-17.

1 “The greater risk associated with higher levels of non-cash earnings, such as
2 AFUDC would ultimately be reflected in higher rates of return required by
3 investors.”⁸⁶ It is Gorman who has the issue backwards.

4 **Q. On page 22 of his testimony, Public Counsel witness Gorman asserts that the**
5 **combination of the existence of MYRPs and PSE’s current stable credit**
6 **outlooks provide ample evidence and rationale for the Commission to deny**
7 **PSE’s request for CWIP in rate base.⁸⁷ How does PSE respond?**

8 A. As PSE has already addressed in this rebuttal testimony, Gorman’s contention that
9 MYRPs are a risk reducing and financial stabilizing solution that can be
10 exclusively relied upon as a basis for rejecting PSE’s CWIP in rate base request is
11 inappropriate and incorrect. Likewise, stable ratings and outlooks and existing
12 regulatory mechanisms in the state of Washington have little if any bearing on
13 whether the Commission should approve or deny PSE’s CWIP in rate base
14 proposal. PSE requests that the Commission place its focus in determining
15 whether or not to approve PSE’s CWIP in rate base proposal based on the pros
16 and cons of such proposal in comparison to the pros and cons of the traditional
17 AFUDC practice to support the clean energy transition required by state law, as
18 they are outlined previously in this rebuttal testimony.

⁸⁶ Doyle, Exh. DAD-1CT at 65:13-15.

⁸⁷ Gorman, Exh. MPG-1CT at 22:6-22.

1 **B. PSE's Response to AWEC's Testimony on CWIP in Rate Base**

2 **Q. AWEC witness Mullins states that recovering CWIP through rate base**
3 **reduces utilities' incentives to efficiently manage construction.⁸⁸ Do you**
4 **agree?**

5 A. No, such an assertion is neither fair nor appropriate. To believe that CWIP in rate
6 base reduces utilities incentives to efficiently manage construction, one would
7 also have to believe that traditional AFUDC practices provide incremental
8 incentive for utilities to efficiently manage the same portfolio of construction
9 projects. This is not accurate. Neither CWIP in rate base nor traditional AFUDC
10 practices impact a utility's motivation or incentive to efficiently manage its
11 construction portfolio because, absent a prudence disallowance, a utility recovers
12 the cost of its construction projects through rates under either ratemaking
13 methodology. Furthermore, PSE's construction project managers are motivated
14 by, and held accountable to, the time-tested and best in class project management
15 principles of:

- 16 1. Schedule: complete the project as quickly and safely as possible.
17 2. Cost: complete the project within budget.
18 3. Scope: complete the project in scope, to deliver anticipated customer benefits.

⁸⁸ Mullins, Exh. BGM-1T at 26:5-16.

1 PSE's construction project managers are not motivated or incentivized by
2 ratemaking or cost recovery alternatives; their jobs are to manage schedule, cost,
3 and scope relative to the projects to which they are assigned.

4 Moreover, PSE as a regulated company has an interest in keeping costs as low as
5 possible for customers because it is the prudent and appropriate thing to do, and
6 keeping costs in line with budgets builds trust with the Commission and
7 intervenors and demonstrates that PSE is a prudent manager of investments made
8 on behalf of customers. Notably, Mullins provides no examples or other
9 supporting evidence to back up his testimony that allowing CWIP in rate base
10 reduces PSE's incentive to operate efficiently.

11 **Q. AWEC witness Mullins suggests that the Commission's ability to determine**
12 **that the cost of equipment is prudent prior to a resource being placed in**
13 **service should somehow have an impact on the Commission's consideration**
14 **of PSE's CWIP in rate base proposal.⁸⁹ How do you respond?**

15 A. It is challenging to decipher Mullins' exact points. I presume that Mullins
16 believes there is a prudence consideration required with respect to PSE's CWIP in
17 rate base request. Prudence is not relevant to the Commission's consideration of
18 PSE's CWIP in rate base request, because the Commission's evaluation of the
19 prudence of a project is unaffected by whether the project was included in rate
20 base during construction or whether it accrues AFUDC during construction. In

⁸⁹ Mullins, Exh. BGM-1T at 26:12-16.

1 either case, the project goes into service on a provisional basis and the
2 Commission will consider the prudence of the project after it is placed in
3 service.⁹⁰ Accordingly, Mullins presents a distinction without a difference.

4 **Q. AWEC witness Mullins states that the cost difference to customers between**
5 **PSE's CWIP in rate base proposal and traditional AFUDC practices are "not**
6 **necessarily a systematic benefit to ratepayers."**⁹¹ **Do you wish to comment?**

7 A. Yes. As stated earlier in this rebuttal testimony, PSE provided pages of testimony
8 and mathematical calculations that support the contention that CWIP in rate base
9 is systematically beneficial to customers compared to the traditional AFUDC
10 practice.⁹² Mullins does not provide support or analysis for his contention to the
11 contrary.

12 **Q. AWEC witness Mullins raises generational equity concerns similar to those**
13 **raised by Public Counsel witness Gorman.**⁹³ **Do you have anything further to**
14 **add to address AWEC witness Mullins' intergenerational equity concerns?**

15 A. No. My rebuttal testimony responding to Gorman's concerns about
16 intergenerational equity also address the intergenerational equity concerns raised
17 by Mullins and the same points apply here.

⁹⁰ See *In re Commission Inquiry into the Valuation of Public Service Company Property that Becomes Used and Useful after Rate Effective Date*, Docket U-190531, Policy Statement on Property that becomes Used and Useful after Rate Effective Date, ¶27 (Jan. 31, 2020) (Used and Useful Policy Statement).

⁹¹ Mullins, Exh. BGM-1T at 27:5-7.

⁹² Doyle, Exh. DAD-1CT at 64:10-70:20; 78:5-89:3.

⁹³ Mullins, Exh. BGM-1T at 25:16-26:4.

1 **C. PSE's Response to Commission Staff's Testimony on CWIP in Rate Base**

2 **Q. Commission Staff witness McGuire cites RCW 80.04.250 to state, "[i]n**
3 **determining what property is used and useful for providing electric, gas or**
4 **water service, the commission may include the reasonable costs of**
5 **construction work in progress to the extent that the commission finds that**
6 **the inclusion is in the public interest."**⁹⁴ **Do you agree?**

7 A. Yes. I agree with McGuire in his reading of state law that the Commission has full
8 authority to approve CWIP in rate base when it believes such inclusion is in the
9 public interest.

10 **Q. Commission Staff witness McGuire questions whether PSE's CWIP in rate**
11 **base proposal will have a near-term or immediate impact on PSE's overall**
12 **cost of capital."**⁹⁵ **How do you respond?**

13 A. PSE does not state anywhere in its testimony that implementation of its CWIP in
14 rate base request will have immediate or near-term impacts on its cost of capital.
15 PSE's proposal to include CWIP in rate base for the Beaver Creek project is an
16 appropriate test case for the Commission to evaluate the usefulness and
17 appropriateness of CWIP in rate base treatment as the state of Washington
18 embarks on its journey to comply with the decarbonization mandates included in
19 CETA and CCA. That said, approving PSE's CWIP in rate base request will
20 signal to the rating agencies that the Commission is utilizing the available tools to

⁹⁴ McGuire, Exh. CRM-1Tr at 86:12-15.

⁹⁵ McGuire, Exh. CRM-1Tr at 89:7-90:15.

1 provide credit supportive regulatory outcomes to strengthen their assessments of
2 the quality of regulation in the state of Washington. This impact will be more
3 immediate and will serve to help maintain PSE's current issuer ratings.

4 **Q. Does Commission Staff witness McGuire raise any intergenerational equity**
5 **concerns?**

6 A. Not directly. In his testimony on page 90, McGuire states, "Staff cannot support
7 the notion that ratepayers paying an extra \$23.9 million over the next two years in
8 exchange for the uncertain prospect of a lower cost of capital at some point in the
9 future supports a finding that the CWIP in rate base is in the public interest."⁹⁶
10 PSE has already addressed in this rebuttal testimony the issue that McGuire raises
11 related to the uncertain prospect of lower cost of capital at some point in the
12 future and will not readdress it here. What remains is an intergenerational equity
13 concern in disguise. PSE agrees that there is an upfront \$23.9 million impact to
14 rates from its CWIP in rate base request during its proposed MYRP, but this rate
15 impact is offset by the mitigation of rate impacts that would otherwise be forced
16 on customers under traditional AFUDC practices. This treatment mitigates rate
17 shock and results in lower costs to customers.⁹⁷ McGuire neglects to mention
18 these benefits in his analysis.

⁹⁶ McGuire, Exh. CRM-1Tr at 90:12-15.

⁹⁷ See Doyle, Exh. DAD-1CT at 68:6 – 70:5.

1 **Q. Does Commission Staff witness McGuire raise equity concerns in his**
2 **evaluation of PSE's CWIP in rate base proposal?**

3 A. Yes. McGuire analyzes the discount rates utilized in PSE's analysis of the cost
4 differential to customers between its CWIP in rate base proposal and the
5 traditional AFUDC practice.⁹⁸ In doing so, he questions whether PSE's analysis
6 properly includes the impact of PSE's CWIP in rate base request from the
7 perspective of PSE's lower-income customers. Ultimately, he claims that PSE's
8 lower-income customers who tend to have a higher opportunity cost of capital
9 than the average person would be made worse off if CWIP were included in rate
10 base consistent with PSE's request.⁹⁹ McGuire views the issue narrowly and
11 incompletely. McGuire fails to recognize in his analysis that equity considerations
12 cannot be viewed in a vacuum without analyzing the complete impacts—costs
13 and benefits—of a proposal or project on PSE's customer base, including lower-
14 income customers. Equity in and of itself is not a gating hurdle; it is component
15 part of a broader cost-benefit review. For example, PSE's Beaver Creek project
16 benefits its entire customer base by making significant and necessary progress to
17 implement the requirements of CETA. In addition, PSE's CWIP in rate base
18 request mitigates the rate impacts to all customers as compared to when a major
19 project is placed in service under the traditional AFUDC practice.¹⁰⁰ Further, PSE
20 has significantly expanded its low-income assistance programs. If PSE's CWIP in

⁹⁸ McGuire, Exh. CRM-1Tr at 89:1–94:18.

⁹⁹ McGuire, Exh. CRM-1Tr at 96:11–17.

¹⁰⁰ Doyle, Exh. DAD-1CT at 68:6–19.

1 rate base proposal is rejected by the Commission, customers will be denied the
2 cost benefits of PSE's CWIP in rate base proposal as a balancing consideration
3 for funding lower-income assistance programs.

4 **D. PSE's Response to JEA's Testimony on CWIP in Rate Base**

5 **Q. JEA witness Gehrke states that delays have occurred with generating**
6 **facilities that have led to issues with CWIP in rate base for customers.¹⁰¹**
7 **How do you respond?**

8 A. Construction delays should have no impact on the Commission's consideration of
9 the merits of PSE's CWIP in rate base proposal. Construction delays can happen
10 whether CWIP is in rate base or traditional AFUDC practices are followed. In
11 both cases, absent prudence disallowances, a utility will recover the cost of its
12 construction expenditures under either method. PSE requests that the Commission
13 place its focus on determining whether or not to approve PSE's CWIP in rate base
14 proposal based on the pros and cons of such proposal in comparison to the pros
15 and cons of the traditional AFUDC practice as they are outlined previously in
16 PSE's direct and rebuttal testimony. The difference is one of timing. In the case of
17 CWIP in rate base, the recovery will be higher during the construction period and
18 lower during the in-service period compared to the traditional AFUDC
19 methodology.

¹⁰¹ Gehrke, Exh. WAG-1T at 11:8-22.

1 **Q. JEA witness Gehrke states that it would be best for PSE to seek approval for**
2 **CWIP in rate base in the context of a certificate of necessity process.¹⁰² Do**
3 **you agree?**

4 A. No. The Commission has authority to approve CWIP in rate base separate and
5 apart from the certificate of necessity process. This is supported by the testimony
6 of Commission Staff witness McGuire.¹⁰³ Contrary to Gehrke's suggestion, the
7 issue of including CWIP in rate base is ripe for Commission consideration in this
8 proceeding.

9 **Q. JEA witness Gehrke presents an elaborate framework for the Commission to**
10 **consider as it evaluates whether or not to approve PSE's CWIP in rate base**
11 **proposal.¹⁰⁴ Do you agree with this approach?**

12 A. No. As PSE witness Doyle stated in his prefiled direct testimony, PSE's Beaver
13 Creek project is an appropriate test case for the Commission to evaluate the
14 usefulness and appropriateness of CWIP in rate base treatment as the state of
15 Washington embarks on its journey to comply with the decarbonization mandates
16 included in CETA and CCA.¹⁰⁵ In this context, Gehrke's recommendation to
17 implement an elaborate framework to evaluate PSE's CWIP in rate base proposal
18 is unnecessary at this time.

¹⁰² Gehrke, Exh. WAG-1T at 14:10-13.

¹⁰³ McGuire, Exh. CRM-1Tr at 88:13-16.

¹⁰⁴ Gehrke, Exh. WAG-1T at 14:14-16:12.

¹⁰⁵ Doyle, Exh. DAD-1CT at 62:8-63:7.

1 **Q. Do you have any specific concerns about Gehrke's framework for**
2 **considering CWIP in rate base?**

3 A. Yes I do. Under Gehrke's proposal, the Commission would approve CWIP in
4 rate base treatment on a project-by-project basis. Under such an approach, PSE
5 would not know whether CWIP in rate base was available to finance a project
6 until *after* deciding to proceed with the project. But in some cases, deciding to
7 proceed with the project might be rejected as an unviable alternative depending on
8 the cash flow constraints of the company at that time. Such an approach could
9 hinder PSE's ability to move forward opportunistically and aggressively to meet
10 the CETA 2030 and 2045 targets. As discussed in the rebuttal testimony of Matt
11 Steuerwalt and Susan Free, PSE is requesting the Commission authorize CWIP in
12 rate base treatment for rate recovery for *all* CETA-eligible owned resources going
13 forward.

14 **VIII. WILDFIRE TRACKER AND INSURANCE COSTS**

15 **Q. Do you agree with Public Counsel witness Gorman's recommendations to the**
16 **Commission regarding PSE's proposed wildfire prevention tracker?**

17 A. No, I do not.

18 **Q. What are his recommendations?**

19 A. Gorman states that "the proposed new tariff rate tracker for these costs [wildfire
20 prevention cost recovery] is not necessary in combination with the multi-year rate

1 setting process.”¹⁰⁶ He goes on to state that “[f]or the insurance premium costs
2 proposed to be recovered I recommend the company recover such costs based on
3 stated premiums from third-party insurance companies over the multiyear rate
4 plan period. This will protect the company from at least short-term unexpected
5 variation in insurance premium cost to the extent the company can secure bids
6 over various time periods within the multi-year planning period.”¹⁰⁷

7 **Q. Do you agree with Gorman’s recommendations regarding insurance**
8 **premium cost recovery?**

9 A. No. Gorman’s recommendation presumes that current wildfire insurance market
10 dynamics position insurers to provide stated premiums over the multiyear rate
11 plan period. That is simply not the case. In Exh. DAD-6, PSE presents a letter
12 from its wildfire insurance broker, Marsh, dated December 8, 2023. In that letter,
13 Marsh states that “[t]he insurance market for utilities operating in wildfire prone
14 areas has become more challenging. Insurers have become more cautious and
15 selective in underwriting policies, leading to reduced capacity and increased
16 premiums. The limited availability of coverage options and increased competition
17 among utilities for insurance, coverage have driven up premiums.”¹⁰⁸ Marsh
18 continues, “Market conditions are very unlikely to improve in the near future,
19 absent a major change in the exposure, such as a change in public policy through
20 legislation. In fact, it is likely to continue to worsen. EIM [a utility industry

¹⁰⁶ Gorman, Exh. MPG-1CT at 33:21-22.

¹⁰⁷ Gorman, Exh. MPG-1CT at 34:1-7.

¹⁰⁸ Doyle, Exh. DAD-6 at 1.

1 mutual insurer] has told members they may stop offering wildfire capacity
2 completely as soon as 2025. This will likely result in greater demand for a limited
3 amount of capacity available in the commercial market, resulting in even greater
4 price increases.”¹⁰⁹

5 Given this market backdrop, which continues to present, the probability that PSE
6 could obtain reliable wildfire insurance premium bids is extremely remote.
7 Furthermore, even if PSE could obtain such bids, its ability to incorporate them
8 into this MYRP proceeding is limited. Based on these facts, Gorman’s
9 recommendations are not reasonable. Furthermore, Gorman overlooks the fact
10 that PSE’s wildfire insurance renewal in 2023 doubled as compared to the price of
11 the prior year’s premium, which prompted PSE to file a request for deferral. That
12 fact, coupled with the uncertainty regarding pricing and capacity in the wildfire
13 insurance market going forward, as cited in the quotes above from the Marsh,
14 establish the very reason why PSE’s request for a wildfire prevention rate tracker
15 is appropriate. Contrary to Gorman’s assertion, in this wildfire insurance market,
16 without a tracker, PSE will have little ability to protect itself from short,
17 unexpected variation in insurance premium costs.

¹⁰⁹ *Id.* at 2.

1 **Q. Does Gorman propose that the Commission consider other alternatives to**
2 **providing PSE damage cost protection from wildfire costs to the extent third-**
3 **party insurance becomes too expensive or unavailable?**

4 A. Yes.

5 **Q. How do you respond?**

6 A. Public Counsel witness Gorman does not have an accurate finger on the pulse of
7 the current wildfire insurance marketplace. His recommendation that PSE and the
8 Commission consider a self-insurance reserve is misplaced. This is exemplified in
9 a recent letter from Warren Buffett, provided as Exh. CGP-12, regarding the
10 implications of utilities becoming self-insured or stated another way becoming the
11 “insurer of last resort.”

12 Wildfire risk is a serious matter. The Commission should be assured that PSE has
13 an accurate finger on the pulse of alternatives to traditional wildfire liability
14 coverages. As viable, cost-effective alternatives to that coverage become
15 available, PSE will prudently consider them.

1 **IX. ACCELERATED GAS DEPRECIATION**

2 **A. Response to The Energy Project Witness Stokes**

3 **Q. Does PSE agree with TEP witness Stokes's contention that PSE's accelerated**
4 **gas depreciation proposal will "provide short-term financial windfall to**
5 **PSE's shareholders"?¹¹⁰**

6 A. No. PSE's accelerated gas depreciation proposal is, from a financial perspective, a
7 cash flow enhancing mechanism that does not provide a short-term financial
8 windfall to PSE's shareholders. To the contrary, the accelerated gas depreciation
9 proposal will, over PSE's two-year MYRP, decrease gas AMA rate base, which
10 will have a short-term financial detriment to PSE's shareholders. Stated
11 alternatively, the accelerated gas depreciation expense will increase accumulated
12 gas depreciation, which will decrease gas AMA rate base over the two-year
13 MYRP, all else equal. Reduced gas AMA rate base translates into reduced
14 returns, reduced net income, and reduced earned returns on equity across PSE's
15 two-year MYRP.

16 **Q. Do you agree with Stokes's contention that PSE's accelerated gas**
17 **depreciation proposal is "[...] [t]oo fast too soon"?¹¹¹**

18 A. No. PSE's accelerated gas depreciation proposal appropriately balances rate
19 impacts on today's customers versus the potential "stranded investment cost" that
20 would be imposed in the future on a materially smaller set of gas customers, as

¹¹⁰ Stokes, Exh. SNS-1T at 54:5-6.

¹¹¹ Stokes, Exh. SNS-1T at 54:12.

1 the state of Washington's gas decarbonization policy initiatives are implemented.
2 TEP witness Stokes overlooks this policy balance, focusing only on the present.
3 In this context, it is important to also bring into perspective the substantial
4 assistance PSE is providing to low-income and energy-burdened customers, and
5 the steps PSE is taking to make its energy assistance programs more accessible to
6 those in need. This is discussed in the Prefiled Direct Testimony of Carol L.
7 Wallace, Exh. CLW-1T.

8 **B. Response to JEA Witness Gehrke's Gas Depreciation Proposal**

9 **Q. JEA witness Gehrke proposes to adjust PSE gas accelerated depreciation**
10 **request. Does PSE wish to respond?**

11 A. Yes. JEA witness Gehrke proposes to shorten gas depreciation service lives by
12 five years versus PSE's request to shorten those service lives by ten years.¹¹² The
13 net effect of Gehrke's proposal is to reduce PSE's gas accelerated depreciation
14 request from \$76.9 million to \$33.1 million.¹¹³

15 **Q. Does PSE agree with this proposal?**

16 A. No. In this proceeding, PSE proposes a carefully balanced set of requests that will
17 bolster cash flows, improve credit metrics, and improve PSE's overall financial
18 integrity as PSE prepares to undertake an unprecedented level of capital
19 expenditures to provide safe, reliable, and efficient gas and electric utility services

¹¹² Gehrke, Exh. WAG-1T at 7:8-15.

¹¹³ *Id.*

1 and simultaneously meet its responsibilities under CETA. PSE proposed its gas
2 accelerated depreciation request as an important component of its balanced
3 approach to improve PSE's cash flows. Gehrke's proposal undermines the
4 balance of PSE's overall request (which includes CWIP in rate base, an enhanced
5 return on equity and equity ratio, in addition to its gas accelerated depreciation
6 request) and would result in a material \$43.8 million reduction in PSE's cash
7 flow, which would materially detract from PSE's ability to improve credit metric
8 performance and improve its overall financial integrity. The capital expenditure
9 and financing challenges PSE faces across its proposed MYRP require that PSE's
10 carefully balanced set of requests to bolster cash flow remain intact. As such, PSE
11 requests that the Commission reject Gehrke's proposal.

12 **Q. Do you have anything else to add?**

13 A. Yes. There are compelling financial reasons for rejecting Gehrke's proposal,
14 which I presented above, but there are compelling policy considerations as well.
15 PSE witness Steuerwalt, in his prefiled rebuttal testimony, provides an accurate
16 historical summary of challenges encountered with respect to the depreciable lives
17 of the Colstrip coal generating units. In brief, as part of a settlement in PSE's
18 2007 general rate case, the depreciable lives of the Colstrip units were increased
19 from 40 to 60 years. In PSE's subsequent 2017 general rate case, the parties
20 grappled with the 2022 closing date for Colstrip units 1 and 2 and the need to
21 address depreciation of the plant over a very tight timeframe. PSE witness
22 Steuerwalt concludes his review by stating, "The lesson learned from Colstrip is

1 that it is better to begin the accelerated depreciation of gas plant now, when there
2 is a more reasonable runway for depreciation, than to wait and deal with the
3 accelerated depreciation on a tightly compressed timeline with the specter of
4 substantial stranded costs, which places a greater burden on customers.”¹¹⁴ From
5 a policy perspective, I fully concur in PSE witness Steuerwalt’s conclusion and
6 submit, on this basis, that the Commission should reject Gehrke’s “kick the can
7 down the road” approach and proposal.

8 **Q. Does JEA witness Gehrke propose anything else?**

9 A. Yes. Gehrke recommends that the reduction he proposes to PSE’s gas accelerated
10 depreciation request be diverted to fund other gas decarbonization initiatives.¹¹⁵

11 There are two problems with this recommendation. First, Gehrke makes no
12 proposal to reallocate a portion of his recommended disallowance of gas
13 accelerated depreciation (\$43.8 million) to fund the incremental gas
14 decarbonization initiatives he references. If Gehrke’s proposal were to be
15 accepted, PSE would need to defund some other activity to implement his
16 recommendation due to the cash flow diversion that would result from his
17 proposal. This is inappropriate and unnecessary, in and of itself, but also in the
18 context of the following point. Second, Gehrke overlooks the fact that PSE has
19 requested a separate decarbonization tracker mechanism to recover the cost of the
20 very decarbonization initiatives that he references. Accordingly, his

¹¹⁴ Steuerwalt, Exh. MS-4T at 16:3-7.

¹¹⁵ Gehrke, Exh. WAG-1T at 7:16-8:9.

1 recommendation is duplicative to PSE's request, and the Commission can decline
2 his proposal.

3 **X. CONCLUSION**

4 **Q. Does that conclude your prefiled rebuttal testimony?**

5 **A. Yes.**