EXH. CTM-4T
DOCKET UG-230968
WITNESS: CHRISTOPHER T. MICKELSON

BEFORE THE
WASHINGTON UTILITIES AND TRANSPORTATION COMMISSION

WASHINGTON UTILITIES AND TRANSPORTATION COMMISSION, **Complainant,** **v.** **PUGET SOUND ENERGY,** **Respondent.**	**Docket UG-230968**

PREFILED REBUTTAL TESTIMONY (NONCONFIDENTIAL) OF

CHRISTOPHER T. MICKELSON

ON BEHALF OF PUGET SOUND ENERGY

SEPTEMBER 12, 2024

PUGET SOUND ENERGY

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I. INTRODUCTION

Q. Are you the same Christopher T. Mickelson who submitted prefiled direct testimony on April 25, 2024, on behalf of Puget Sound Energy in this proceeding?

A. Yes, I am.

II. SCOPE AND SUMMARY OF TESTIMONY

Q. What is the purpose of your rebuttal testimony?

A. My rebuttal testimony responds to the positions of the Washington Utilities and Transportation Commission Staff ("Staff") and Joint Environmental Advocates ("JEA"), collectively the "Non-company Parties", regarding the earnings test in their alternative proposals for risk-sharing mechanisms ("RSM").

Q. Please summarize your rebuttal testimony.

A. My rebuttal testimony maintains that Puget Sound Energy ("PSE" or the "Company") proposal more fairly balances the issues without causing financial instability compared to the proposals put forth by the Non-company Parties in this case. Specifically, my rebuttal testimony demonstrates that the Non-company Parties' earnings sharing tests are indecipherable and unworkable.

III. THE COMMISSION SHOULD REJECT THE NON-COMPANY PARTIES' EARNINGS SHARING TESTS

A. PSE's Approach

Q. PSE presented an RSM and financial earnings test in its direct testimony in this proceeding. Does PSE now support Commission approval of an RSM?

A. No. PSE's position remains as PSE witness Matt Steuerwalt describes it in his direct and rebuttal testimonies – an RSM is not necessary nor required by the Climate Commitment Act ("CCA"). If the Commission decides to require an RSM of PSE, the Commission should reject JEA's proposal and instead approve an RSM based on PSE's proposal. PSE's proposal is largely approved by Staff, as explained in the rebuttal testimony of Jason Kuzma, Exh. JK-3T, but it includes a more reasonable and measured financial earnings test than Staff's. As explained below, Staff's and JEA's financial earnings test is inappropriate and should be rejected.

Q. Can you explain PSE's current approach to the financial earnings test and how it compares to Staff's and JEA's proposals?

A. Yes; PSE's current approach to the financial earnings test is a simple mechanism designed to balance cost recovery with maintaining financially viability. It includes a single-side RSM, where PSE shares risk only if costs exceed expectations and the Company is in a financially viable situation, while all resulting benefits are passed on to the customer. This approach accounts for normal business fluctuations and complexities of financial performance over the compliance period, both of which PSE is in the best position to quantify and anticipate. In contrast, the Non-company Parties' proposals introduce more rigid caps and stringent earnings tests, which could exacerbate under-earning situations and create financial instability. The implications of multiple tests or caps across different mechanisms, such as decoupling, must be analyzed to avoid unintended consequences and ensure regulatory fairness and efficiency.

Q. How does the current decoupling mechanism illustrate the challenges of implementing multiple tests or caps?

A. The current decoupling mechanism already has caps on deferral that introduce delays in recovery, increasing regulatory lag. Implementing multiple tests or caps on all trackers, as proposed by the Non-company Parties, would compound these challenges, leading to higher administrative burdens and potential conflicts between different regulatory requirements. This complexity could divert resources from essential operational activities and hinder PSE's ability to maintain reliable service and attract investment.

B. The Non-company Parties' Approaches

Q. What are the potential operational impacts of the Non-company Parties' sharing cap and earnings test proposals on PSE?

A. Operationally, the rigid caps and stringent earnings tests in both Staff's and JEA's proposals could lead to higher compliance costs and inefficiencies, without fully accounting for how these caps and tests would operate in tandem with the RSM.

Another reason to reject the Non-company Parties' proposals is because they are not completely thought out.

Q. What do you mean the Non-company Parties' proposals are not completely thought out?

A. Staff's proposal introduce caps as an alternative approach to PSE's earnings test but does not explain its application to RSM. Staff's response testimony suggests a 10-basis points ("bps") cap placed upon the Company's annual return on equity ("ROE")[1] but does not clarify what the 10-bps is applied to (*e.g.,* rate base, net operating income, *etc*.) or even which party the cap impacts (*i.e.,* PSE or the customer) if a compliance amount is above such cap. In addition, it does not appear that Staff has thought through how the cap would be applied given the four-year compliance periods associated with the CCA.

Q. Why is the compliance period an issue?

A As Staff correctly points out, the CCA compliance period is four years long. Staff's 10-bps proposal is an annual calendar amount.[2] Over a four-year compliance period, Staff's proposal would total 40-bps. In addition to being drastic, the proposed cap is arbitrary. Staff has provided no support for its selection of 40-bps and has provided no financial analysis to demonstrate the potential impact of such a cumulative hit on PSE's earnings. Staff simply appears

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[1] McConnell, Exh. KM-1T at 7:13-16.

[2] McConnell, Exh. KM-1T at 7:15-16: "10 basis points of 2023 ROE + 10 basis points of 2024 ROE + 10 basis points of 2025 ROE + 10 basis points of 2026 ROE = Total 4-year compliance period cost."

to have pulled 10-bps out of the air with no attempt to show how the annual or cumulative earnings impact will affect PSE or its investors.

Q. What are the potential operational challenges posed by multiple earnings tests proposed by Staff?

A. The multiple earnings tests proposed by Staff could pose significant operational challenges for PSE, including increased administrative burden, higher compliance costs, more complexity filings, and potential conflicts between different regulatory requirements and mechanisms. Implementing multiple tests without a coordinated approach can lead to inefficiencies and make it difficult for PSE to manage its financial performance effectively. This complexity could divert resources away from essential operational and investment activities or increase overall costs to meet these new regulatory requirements.

Q. You have articulated serious concerns with Staff's earnings test, but what about JEAs?

JEA's earnings sharing proposal contains other similar flaws to Staff's. First, it is extreme. Staff's proposal would reduce PSE's earnings 40 bps over four years, but JEA's proposal is even more drastic. While Staff is 40-bps over four years, JEA could reduce PSE's ROE 400-bps (four percent) over four years.

Further, as with Staff's 10-bps cut, JEA's 50-bps trigger is wholly arbitrary, simply "picked,"[3] and based on no data, empirical evidence, or analysis. Also,

[3] Gehrke, Exh. WG-1T at 28:12.

like Staff, it is unclear how JEA's alternative earnings test will function within a four-year compliance period, given that the RSM is conducted annually. This misalignment with the intended operation of compliance instruments creates additional complications. JEA's proposal suggests that each emission has a cost based on its corresponding allowance, applying the cost again to the RSM bands at the time purchase. This approach does not acknowledge PSE's ability to purchase offsetting allowances at any time during the four-year compliance period, nor does JEA's proposed earnings test consider this flexibility.

C. Lack of Support and Detail

Q. Was there enough information on the record to implement the Non-company Parties' proposals?

A. No. The Parities' proposals lacked sufficient details on how their alternative test or caps would be applied. To address this, PSE submitted multiple data requests to the Non-company Parties to clarify the record. See Exh. CTM-5 for copies of data requests and Staff's responses thereto and see Exh. CTM-6 for copies of data requests and JEA's responses thereto. Without these data requests, neither PSE nor the Commission would have had the necessary information to fully understand how to implement the Non-company Parties' proposals. Still, despite these efforts, neither Staff nor JEA provided sufficient detail or explanation, and further analysis is still needed to fully understand the implications and be comfortable with these proposals.

The complexity and depth of the proposed mechanisms necessitate thorough examination, which the given timeframe and forum did not adequately accommodate. Consequently, while some aspects were clarified through responses to PSE's data requests, significant uncertainty remains regarding the feasibility and impact of the Non-company Parties' proposals. This uncertainty could lead to unintended consequences if the mechanisms are implemented without a complete understanding of their operational and financial implications. Additionally, there is a risk that the proposals could misalign customer and Company interests, potentially incentivizing investments in costly decarbonization measures as allowance price increases, since such measures would not subject to the RSM could be seen as less risky investments.

Q. What questions remain unanswered by the Non-company Parties regarding their proposals?

A. In addition to the lack of clarity regarding the mechanics of the Non-company Parties' proposals discussed previously in my testimony, several broader questions remain unanswered by the Non-company Parties regarding their proposals, such as:

1. How will the proposed mechanisms account for market volatility and operational realities?
2. How will multiple earnings tests be coordinated to avoid regulatory inefficiencies and increased complexities?
3. What provisions are in place to ensure ongoing investment in critical infrastructure?

4. What comprehensive assessments have been conducted to evaluate the potential impacts of these earnings tests on PSE's financial stability and ability to attract investment?
5. How will the proposed mechanisms ensure fair and consistent returns for investors while protecting customer interests?

If the Commission is intent on ordering an RSM using an earnings test similar to those proposed by Staff or JEA, it would need a further record in this, or another proceeding, to develop answers to these questions. Without this information, the proposals of the non-company parties are not well understood at this time and may be unworkable due to their inherent complexity. Therefore, PSE submits the Commission does not have a fully developed record before it at this time.

IV. CONCLUSION

Q. Does that conclude your rebuttal testimony?

A. Yes, it does.