

BEFORE THE WASHINGTON UTILITIES AND TRANSPORTATION COMMISSION

WASHINGTON UTILITIES AND)	
TRANSPORTATION COMMISSION,)	
)	
Complainant,)	Dockets UE-121697 and UG-121705
)	<i>(Consolidated)</i>
v.)	
)	Dockets UE-130137 and UG-130138
PUGET SOUND ENERGY, INC.,)	<i>(Consolidated)</i>
)	
Respondent.)	
_____)	

EXHIBIT NO. ___ (MCD-3)

Excerpt of Transcript of Deborah J. Reynolds

April 26, 2013

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1 Q. -- rate projections, you'll know what we're referring
2 to?

3 A. Yes.

4 Q. Okay. Thank you.

5 Is it correct that as part of the global settlement,
6 Staff is accepting the amended petition for decoupling
7 mechanisms without change?

8 A. Again, I didn't see Mr. Schooley's final testimony on
9 the global settlement, so I'm not sure. But I personally am
10 endorsing this particular decoupling mechanism that's in front
11 of you.

12 Q. So you're endorsing the amended petition for
13 decoupling mechanisms without change, correct?

14 A. Yes. I don't think they need to be changed.

15 Q. The amended decoupling petition contains what's
16 called a "K-Factor."

17 Can you define "K-Factor" for me?

18 A. (Witness reviews document.)

19 (Pause in the proceedings.)

20 THE WITNESS: My testimony on page 4 defined the
21 K-Factor as the fixed-percentage increase applied only to
22 non-power costs.

23 BY MS. DAVISON:

24 Q. So is that your understanding of what a K-Factor is?

25 A. Well, clearly there are hundreds of different

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1 versions of K-Factor out there.

2 When Puget first filed their petition for decoupling,
3 it included an entirely different version of a K-Factor that
4 incorporated changes in conservation, and so a K-Factor is a
5 term of art that can be used in lots of different ways.

6 But this is a fairly standard version of a K-Factor.
7 I would call this the "plain vanilla K-Factor" that just applies
8 a percentage increase to some proportion of cost or some -- or
9 sometimes to overall costs going forward over time.

10 Q. Would you consider it to be synonymous with an
11 attrition adjustment?

12 A. It's not synonymous with an attrition adjustment, but
13 it can effectively act as an attrition adjustment.

14 An attrition adjustment is typically applied during
15 the development of a revenue requirement in a general rate case,
16 and so it will assume some -- some relationship between costs
17 and revenues and load at a particular point in time.

18 And a K-Factor will typically say take that -- take a
19 historic look at how those relationships have changed and be
20 applied in a going-forward kind of a way, so it's similar but
21 not the same.

22 Q. Do you know what the "K" stands for in the K-Factor?

23 A. I do not.

24 Q. The K-Factor that is contained in the amended
25 decoupling petition, is that similar to the K-Factor defined in

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1 the Regulatory Assistance Project guide dated June 2011?

2 A. Did you ask -- could you repeat the question?

3 Q. Sure. Is the K-Factor that is contained in the
4 amended decoupling petition the same K-Factor that is defined in
5 the Regulatory Assistance Project guide dated June 2011?

6 A. I would have to check. I don't have that definition
7 memorized.

8 Q. Thank you.

9 (Exhibit No. 1 marked.)

10 BY MS. DAVISON:

11 Q. I am handing you what the court reporter has marked
12 as Exhibit No. 1, which is your response to ICNU Data Request
13 3.4.

14 Do you recognize this document?

15 A. (Witness reviews document.)

16 So for whatever reason, I show that I submitted a
17 supplemental revised response, which I honestly don't think is
18 actually different, but I just thought I would point it out.

19 Q. I did see that.

20 A. Do you explicitly want me to use -- I mean, did you
21 want --

22 Q. I want you to use the exhibit. I did compare them --

23 A. Okay.

24 Q. -- and I did not see a difference, so I was a little
25 confused by that, so I used your --

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1 A. Okay.

2 Q. -- original submission.

3 A. The only thing I found was that Commission is
4 capitalized, and that makes me feel better.

5 Q. So you recognize --

6 A. Yes, I do.

7 Q. -- what's been marked as Exhibit 1 as your original
8 response to ICNU Data Request 3.4?

9 A. Yes, I do.

10 Q. In response to this data request marked as Exhibit 1,
11 you cite to the requirement that a decoupling mechanism provides
12 a two-way true-up mechanism increase or decrease.

13 Does the decoupling proposal contained in the revised
14 petition contain a mechanism that allows rates to both increase
15 and decrease?

16 A. It does for the two classes of customers included in
17 the mechanism, which are residential and nonresidential. And,
18 of course, Schedule 449 is in the rate plan group, which is
19 Group 3.

20 Q. And if you layer on top of that the K-Factor
21 mechanism, would customers see an overall annual rate decrease?

22 A. I can't answer that question, because I don't know
23 what load is going to do.

24 Q. So if load goes up, how would that impact your
25 answer?

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1 A. Under our decoupling mechanism, when load goes up in
2 a particular year, in the following year, rates will be lower or
3 bills will be lower, and it is possible that it could -- that
4 the change in load could exceed the 3 percent increase and
5 possibly could offset it.

6 Q. And the 3 percent increase, are you referring to the
7 K-Factor increase?

8 A. I am.

9 Q. Thank you. Do you recall attending a workshop in the
10 summer of 2012 with PSE in which John Story said that with the
11 K-Factor in place, it was highly unlikely that customers would
12 see a rate decrease under that mechanism?

13 A. If I recall correctly, that was the original K-Factor
14 that would have been under discussion in that situation.

15 And that is absolutely true, but that's because that
16 was a one-way decoupling mechanism.

17 Q. So --

18 A. It's not the same.

19 Q. As what's before us today?

20 A. Correct.

21 Q. Thank you. And if you refer to Ms. Barnard's
22 testimony, page 2, lines 21 through 22?

23 A. I don't have that.

24 Q. I'll just tell you.

25 A. Okay.

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1 Q. I can pull it out if you want to see it, but
2 generally she says that the K-Factor is set at a constant level
3 that is similar to a rate plan.

4 Is that your understanding of the K-Factor that is
5 being proposed in the global settlement?

6 A. It's my understanding that the K-Factor is set at a
7 specific level, and that it's being referred to as a rate
8 plan -- or I'm not sure I understand the question.

9 Q. Ms. Barnard --

10 A. Do you want me to confirm that she said that or...

11 Q. Well, let me try the question again.

12 Ms. Barnard refers to the K-Factor being set at a
13 constant level; is that your understanding?

14 A. Yes.

15 Q. And in light of that, customers are likely to see
16 rate increases each year under the K-Factor; is that correct?

17 A. Again, they may see rate increases, and they may not.
18 It will depend on load.

19 Q. And does Staff have an analysis of what level of load
20 would need to materialize for rate increases not to occur?

21 A. I have multiple models of that from previous -- in
22 the preparation of the Bench request for -- in the previous
23 general rate case, so...

24 Q. Would those analyses apply to the proposal that's
25 before us today?

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1 A. I have not applied those models to this -- to this
2 proposal. I had Chris Mickelson work on some of that material,
3 though.

4 Q. And does he have analyses that show what level of
5 load would need to materialize in order for there not to be a
6 rate increase under the K-Factor?

7 A. Well, because it's a model, you could determine that.
8 But I think it's not different from the work papers provided by
9 Mr. Piliaris in terms of looking at, you know, how it works and
10 what will happen.

11 Q. Is it more probable than not that customers would see
12 annual rate increases under the K-Factor?

13 A. It really depends on the weather. And the weather
14 has been less and less predictable, so I really can't say. At
15 some point it should balance.

16 Q. The revised decoupling mechanism, does it have -- is
17 it weather normalized?

18 A. I don't recall.

19 Q. What conservation opportunities are being foregone by
20 PSE due to a lack of a decoupling mechanism?

21 A. I don't -- I don't think that's the right question.

22 With all due respect, this mechanism is not a
23 conservation impact mechanism, and so it's not intended to
24 address only the effective conservation on load.

25 Q. What's it intended to address?

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1 A. It addresses all change in load from the economy --

2 MS. BROWN: Can you speak up?

3 THE WITNESS: -- from weather.

4 All changes in load from the economy. From weather.

5 All of them.

6 BY MS. DAVISON:

7 Q. So it captures all those components?

8 A. It's supposed to. We'll know better after two years
9 have gone by.

10 Q. So I will go back to my question, which is: Are
11 there any conservation opportunities that are being foregone by
12 PSE due to a lack of any type of decoupling mechanism?

13 A. So in the attachment to my supplemental revised
14 response, 3.2, I provided the table of the Commission basis
15 reports. And it shows that in -- since 2005, the Company has
16 never managed to earn their authorized rate of return, and part
17 of that impact is the effect of conservation.

18 And so, again, the Company is required to do
19 conservation by the Energy Independence Act, and they have to do
20 all conservation. And so they had better be doing all
21 conservation, but I believe that that increases our duty to make
22 sure that the rates are compensatory.

23 Q. So is it your view that there are no conservation
24 opportunities being foregone by PSE at this time?

25 A. I think I said there had better not be, but I don't

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1 know that there aren't any.

2 Q. So this is not an area in which Staff has done any
3 analysis on?

4 A. We have done -- conservation programs are -- we are
5 investigating them annually --

6 Q. But my question goes --

7 A. -- all the time, so -- I mean, we are attempting to
8 ensure that the Company is -- is pursuing all the conservation
9 they're supposed to achieve.

10 But can I ever make a flat statement, everything is
11 perfect, no.

12 Q. And my question is whether you're aware of any
13 conservation opportunities that are being foregone by PSE.

14 A. No, I'm not.

15 Q. Thank you. Is it your testimony that customers will
16 be better off under this decoupling mechanism than without it?

17 (Pause in the proceedings.)

18 THE WITNESS: I don't think it's a question of
19 ratepayers being better off or worse off. I think it's a
20 question of finding the balance point between the interest of
21 ratepayers and the interest of shareholders, and I think that
22 this mechanism does that.

23 BY MS. DAVISON:

24 Q. Right. I understand that's what Staff was trying to
25 achieve, but my question is: Will ratepayers be better off

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1 then it is a reasonable jumping-off point for a decoupling
2 mechanism.

3 And, no, I -- well, my testimony addresses whether or
4 not it's consistent with the policy statement. I don't know
5 that the global settlement does.

6 THE WITNESS: Could you read my answer back; is that
7 okay?

8 MS. BROWN: Yes.

9 MS. DAVISON: Sure.

10 THE WITNESS: Thank you.

11 (Answer was read back.)

12 BY MS. DAVISON:

13 Q. I would like to hand you what the court reporter will
14 mark as Exhibit 2, and it is your response to ICNU Data Request
15 No. 3.5.

16 (Exhibit No. 2 marked.)

17 BY MS. DAVISON:

18 Q. Do you recognize this document?

19 A. (Witness reviews document.)

20 Yes.

21 Q. Is it true that Staff's global settlement proposal
22 does not recognize the Commission's policy statement requirement
23 that a decoupling proposal include a mechanism for accounting
24 for off-system sales and other avoided costs?

25 A. (Witness reviews document.)

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1 So I did not testify about the global settlement.
2 The decoupling mechanism...

3 Can you phrase your question in terms of the
4 decoupling mechanism?

5 Q. Sure. I think as it relates to my question, it's one
6 and the same, but is it true that Staff's support of the
7 settlement proposal, which contains the revised decoupling
8 proposal, does not recognize the Commission's policy statement's
9 requirement that the decoupling proposal include a mechanism for
10 accounting for off-system sales and other avoided costs?

11 A. (Witness reviews document.)

12 (Pause in the proceedings.)

13 THE WITNESS: We need to make two points about the
14 Commission's policy statement on decoupling.

15 First --

16 BY MS. DAVISON:

17 Q. Could you first answer "yes" or "no," and then
18 explain?

19 MS. BROWN: If it's susceptible to a "yes" or "no"
20 answer.

21 THE WITNESS: I forget.

22 Is it does it include it or does it exclude it?

23 BY MS. DAVISON:

24 Q. Is it true that Staff's support of the global
25 settlement proposal does not recognize the policy statement's

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1 requirement that a decoupling proposal include a mechanism for
2 accounting for off-system sales and other avoided costs?

3 A. Yes, because the Commission's Order 08 in Puget's
4 most recent general rate case states that the decoupling
5 mechanism that was discussed in that general rate case was
6 consistent in intent and general design with the Commission's
7 decoupling policy statement, and I refer to that in my testimony
8 on page 16, lines 7 through 10.

9 Q. So --

10 A. And in order --

11 Q. I'm sorry. Go ahead.

12 A. In order to avoid a situation where the Commission's
13 policy statement creates a situation that has no resolution, in
14 order to move forward, you -- as I state in this, Exhibit 2, the
15 Commission has elected to refrain from applying its decoupling
16 policy on wholesale sales and given that guidance, I believe it
17 is appropriate to maintain the current PCA and approve the
18 revised petition and amend the PCA, which is the power cost
19 adjustment, within a power cost only rate case or in a general
20 rate case that comes in two years.

21 Q. So it's your testimony that you believe that the
22 Commission has backed off on the requirement that a full
23 decoupling mechanism include an ability to account for
24 off-system sales and other avoided costs?

25 MS. BROWN: Objection. Leading.

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1 BY MS. DAVISON:

2 Q. So your answer is "yes"?

3 A. Obviously, yes.

4 Q. Thank you.

5 A. It is dated November 18, 2010, which is clearly prior
6 to the Commission's most recent general rate case order, which
7 is the driver for my testimony dated May of 2012.

8 Q. So if you refer to these comments on the second page,
9 it states that -- and these are Staff's comments, that "The
10 Policy Statement also requires that a utility's request for a
11 limited decoupling mechanism" -- and "must" is emphasized -- "be
12 made in its direct testimony in the rate case filing and
13 include, at a minimum, a true-up mechanism, impact on rate of
14 return, a proposed earnings test, offsets or found margin,
15 impact on customer rates, and a weather adjustment mechanism."

16 Do you agree with that statement?

17 A. No.

18 Q. Thank you.

19 A. The Commission -- it's Order 08 in Docket
20 UE-111048 -- found that the Coalition's previous decoupling
21 mechanism, the decoupling mechanism in that general rate case,
22 was consistent in intent and general design with the
23 Commission's decoupling policy statement.

24 Q. Is it your testimony that the Commission has backed
25 away from its policy statement requirement --

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1 A. How many times are you going to me this question?

2 Q. -- that it must include a true-up mechanism and
3 impact on rate of return, a proposed earnings test, offsets or
4 found margin, impact on customer rates, and a weather adjustment
5 mechanism?

6 A. It is my testimony that the Commission's order dated
7 May 2012 found that the Coalition's decoupling mechanism
8 proposal was consistent in intent and general design with its
9 decoupling policy statement.

10 If that differs from that language, then that
11 language is not correct any longer. But you are reading from a
12 document dated 2010.

13 Can we please move on?

14 Q. So is it your view that the Commission's decision or
15 order in PSE's last general rate case was intended to be a
16 revision of the Commission's decoupling policy statement?

17 A. I have 20 pages of testimony about why it's
18 different.

19 Q. No. My question is: Is it your view that the
20 Commission's order in PSE's last general rate case was intended
21 to be a revision to the Commission's decoupling policy
22 statement?

23 A. I have explained my reconciliation of the
24 Commission's order with my previous testimony in the 20 pages of
25 testimony that are filed here.

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1 Q. So was that --

2 A. Do you have a more specific question to ask me?

3 Please ask it.

4 Q. So is that a "yes," then?

5 A. It took me 19 pages to say it, and I'm not going to
6 say it any differently.

7 Q. Well, I'm trying to --

8 A. There's a lot of detail here, and it's important
9 detail, or I would have just filed a page that said "yes," and I
10 couldn't.

11 Q. Well, I guess I'm not clear on -- I understand your
12 testimony and your attempt to reconcile your current position
13 with the policy statement, but you've relied very heavily upon
14 the Commission's decision in the last PSE general rate case
15 order.

16 And do you believe that the Commission intended to
17 revise its policy statement through that order?

18 A. I do not know what the Commission intended to do.

19 Q. Thank you.

20 MS. BROWN: And also it assumes facts not in
21 evidence.

22 We call that "an objection."

23 MS. DAVISON: We're -- I'm -- all right. I won't
24 even go down that path...

25 (Exhibit No. 5 marked.)

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1 BY MS. DAVISON:

2 Q. The court reporter is handing you a document that's
3 been marked as Exhibit 5, which is your response to ICNU Data
4 Request 3.2.

5 Do you recognize this document?

6 A. (Witness reviews document.)

7 No. The supplemental response is attached to the
8 nonsupplemental cover attachment.

9 Q. Okay. We'll try to find you the original.

10 A. But it said the -- you have the original, but then
11 you have the supplemental attachment but not the supplemental
12 response, which does have more words on it.

13 (Pause in the proceedings.)

14 BY MS. DAVISON:

15 Q. All right. So I think what we need to do is maybe at
16 the next break, we can make copies. I see that you do have an
17 additional paragraph on your supplemental response to 3.2.

18 A. Mm-hm.

19 Q. And you obviously have that in front of you, but we
20 will correct that exhibit during the break.

21 So if you look at your response to 3.2, you state
22 that (as read): "Staff strongly believes that adjustments to
23 return on equity or capital structure are only appropriate
24 within a general rate case...."

25 A. Yes.

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1 Q. And why is that? Why could we not look at that in
2 this proceeding?

3 A. Because you can't see all the offsetting factors.
4 You can't do it on a partial company view.

5 Q. And what offsetting factors would you be referring
6 to?

7 A. All of the offsetting factors in a general rate case.

8 Q. Well, can you give some examples of what you're
9 concerned about that wouldn't be captured in doing a
10 cost-to-capital analysis in the context of this proceeding?

11 A. I'm not a cost-to-capital witness, and I can't name
12 them off the top of my head.

13 You could give me data request later, and I will try
14 to respond.

15 Q. So you don't consider yourself to be an expert on
16 cost to capital, rate of return, those sorts of issues?

17 A. No, just decoupling.

18 Q. And in evaluating this issue in preparing your
19 response to Data Request 3.2, did you consult with anyone on
20 Staff that is a cost-to-capital expert?

21 A. Yes.

22 Q. And who would that be?

23 A. Ken Elgin.

24 Q. And did Mr. Elgin give you any opinion regarding the
25 impact on PSE's cost to capital if the global settlement is

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1 adopted?

2 A. I didn't ask him that question because I was only
3 looking at decoupling. I asked him for assistance with the
4 paragraph on page 9 of my testimony.

5 Q. And which lines are you referring to that Mr. Elgin
6 gave you assistance with?

7 A. (Witness reviews document.)

8 (Pause in the proceedings.)

9 THE WITNESS: Page 8, line 23, through page 9, line
10 2, which is a -- pretty much a direct quote from the Bench
11 request response prepared in Docket UE-111048.

12 (Reporter interruption for clarification.)

13 THE WITNESS: So this is from a significant time ago.
14 And then I generally discussed the remaining ideas,
15 but I did not get assistance with -- he didn't give me red line
16 edits, but we generally discussed the ideas, and I would not say
17 that he necessarily agreed with everything that I had written.

18 BY MS. DAVISON:

19 Q. Do you recall what he disagreed with?

20 MS. BROWN: Melinda, I'm going to object.

21 THE WITNESS: I don't exactly recall what we
22 disagreed with, which is probably why I didn't change it so that
23 he could agree with it, because I couldn't figure out exactly
24 what it was he disagreed with. It was a conversation in
25 passing, and so that's all I remember.

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1 BY MS. DAVISON:

2 Q. Okay.

3 (Exhibit No. 6 marked.)

4 BY MS. DAVISON:

5 Q. I'm going to hand you what is being marked as Exhibit
6 6.

7 And this document is entitled (as read): "RESPONSE
8 TESTIMONY OF Deborah Reynolds," regarding the decoupling
9 proposal with NW Energy Coalition dated February 24, 2012.

10 A. Yes.

11 Q. Do you recognize this testimony?

12 A. I do.

13 Can we just note right at the very beginning that...

14 Q. There's no question pending. I just asked you if you
15 recognized it. I'll ask you some questions, and you'll have an
16 opportunity to explain your testimony.

17 On page 12, lines 1 through 3, do you see that you
18 recommend that the Commission should reject the decoupling
19 mechanism proposed by NWECA for Avista on the basis that it did
20 not provide customers with the benefits of revenue risk
21 reduction associated with decoupling?

22 A. Sorry. Which page?

23 Q. Page 12, starting at line 1.

24 A. (Witness reviews document.)

25 (Pause in the proceedings.)

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1 BY MS. DAVISON:

2 Q. Do you want me to repeat the question?

3 A. No, thank you.

4 (Witness reviews document.)

5 (Pause in the proceedings.)

6 THE WITNESS: I'm glad that you -- thank you for
7 bringing this explicitly to my attention.

8 In this testimony you've referred to from Dockets
9 UE-1110 -- 11 -- I'm sorry. Docket UE-110876, page 12, line 1,
10 which is my decoupling testimony concerning the Energy
11 Coalition's decoupling proposal and its interaction with the
12 appropriate cost of equity.

13 In my current testimony, page 9 --

14 BY MS. DAVISON:

15 Q. Excuse me.

16 A. -- I said --

17 Q. I'm not asking you about your current testimony.
18 My question was --

19 A. Yep.

20 Q. -- did you recommend that the Commission reject
21 NWECC's decoupling proposal because you state customers should
22 receive the benefits of their revenue risk reduction resulting
23 from decoupling?

24 A. Yes. And the Commission's order May '12, 2012 -- not
25 May 12, 2012; May 2012 -- said that the Coalition's decoupling

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1 proposal was consistent in intent and general design with the
2 Commission's decoupling policy statement.

3 Q. I understand that's your testimony now. I'm just
4 asking you about your testimony --

5 A. Oh, I'm sorry. That's what the order says now.

6 Q. No, I understand that's -- that's your position, and
7 I just wanted to ask you about your testimony in the Avista
8 case.

9 A. It's not relevant. It's from before the Commission's
10 order.

11 Q. My question is: Does the current NWECS-PSE proposal
12 provide customers with the benefits of the revenue risk
13 reduction associated with decoupling?

14 A. That question is not relevant because the Commission
15 has found that that proposal is consistent in intent and general
16 design with their decoupling policy statement.

17 Q. My question is relevant, and my question is: Does
18 the current NWECS-PSE proposal provide customers with the
19 benefits of revenue risk reduction associated with decoupling?
20 It is a "yes" or "no" answer.

21 A. I -- I cannot reconcile that statement with the
22 Commission's finding that it is consistent in intent and general
23 design.

24 Q. And my question isn't asking you to. My question is
25 a simple one.

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1 In the current decoupling proposal that is being
2 proposed by PSE and NWECC and supported by Staff, does it provide
3 customers with the benefits of revenue risk reduction associated
4 with decoupling; yes or no?

5 A. It's not a "yes" or "no" question. I'm sorry. It's
6 not a "yes" or "no" answer. It takes Ken Elgin a hundred pages
7 to write cost-to-capital testimony. It's not a "yes" or "no"
8 answer.

9 Q. And you don't know whether or not their customers
10 will see the benefits of revenue risk reduction associated with
11 decoupling in the current proposal?

12 A. I said it is not a "yes" or "no" answer.

13 Q. Well, explain. Feel free to explain your answer. It
14 seems like it's very black and white to me. Either customers
15 are going to see the benefits of the revenue risk reduction in
16 the current proposal or they are not.

17 A. I can't answer the question. I'm sorry.

18 Q. You don't know?

19 A. I did not say that. I said I can't answer the
20 question.

21 Q. And why can't you answer the question?

22 A. Because it is a "yes" or "no" question.

23 Q. Well, feel free to expand on it.

24 (Pause in the proceedings.)

25 THE WITNESS: Well, the Commission found that the

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1 Coalition's proposal in that previous case was consistent in
2 intent and general design with its decoupling policy statement,
3 and the decoupling policy statement requires that you
4 appropriately recognize the benefits of revenue risk reduction
5 resulting from decoupling. So, apparently, the Commission has
6 determined that somehow the Coalition's proposal does recognize
7 those benefits. I don't know how. I didn't write the order. I
8 don't know how they got there, but they did.

9 BY MS. DAVISON:

10 Q. And didn't the Commission also say that the
11 Commission remains open to proposals for full decoupling
12 mechanisms, even to one that may vary somewhat from what is
13 described in our policy statement?

14 A. Absolutely. I have it quoted right here on lines 13
15 to 15 of my testimony on page 9.

16 Q. So does the Commission explicitly say in Order 08
17 that NWECC's mechanism provides customers with the benefits of
18 revenue risk reduction associated with decoupling?

19 A. No, they did not.

20 Q. But it's your testimony that you believe the
21 Commission believes that the NWECC proposal did contain a
22 mechanism to provide customers with the benefits of the revenue
23 risk reduction associated with decoupling?

24 A. That is not what I said.

25 THE WITNESS: Could you read back my answer?

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1 BY MS. DAVISON:

2 Q. Well, this is a different question, so you can feel
3 free to correct what is wrong with the assumptions in my
4 question. I'm just trying to understand your testimony and your
5 position on revenue risk reduction associated with decoupling in
6 providing customers with the benefits of it. I'm not trying to
7 trick you. I'm not trying to trip you up. I am simply trying
8 to understand your position. That's all.

9 A. And I did not write the Commission order, and the
10 Commission order says that the Coalition's proposal is
11 consistent in intent and general design with the Commission's
12 policy statement. And I have answered you repeatedly. I have
13 no way of knowing how the Commission reconciles those two
14 things. I do not know. I have provided 19 pages of testimony
15 that explains what I do know. I do not know what happened to
16 the benefits of revenue risk reduction.

17 Q. Has Staff conducted any studies that quantify the
18 amount of risk that -- risk reduction that will be associated
19 with this decoupling mechanism if it is approved?

20 A. No. We rely on the general rate case, which is where
21 we established the rate of return.

22 Q. So in evaluating the revised decoupling proposal and
23 reaching the conclusion that you would support it, did you
24 factor the risk shifted to customers through decoupling in your
25 analysis of whether or not to support it?

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1 A. Could you repeat the question?

2 Q. When Staff decided to support the revised decoupling
3 petition, did you factor into your analysis the risk that it
4 shifted to customers through decoupling, and did you evaluate
5 the cost in -- or I'm sorry. Let me try this again. I was
6 trying to simplify the question, and I made it worse.

7 So did Staff factor the risk associated -- or the
8 risk shifted to customers through the decoupling proposal in
9 your analysis of the cost benefits of the settlement?

10 (Pause in the proceedings.)

11 THE WITNESS: No, because we relied on the analysis
12 that occurred in the general rate case.

13 BY MS. DAVISON:

14 Q. Thank you.

15 (Exhibit No. 7 marked.)

16 BY MS. DAVISON:

17 Q. The court reporter is handing you a document that is
18 marked as Exhibit 7, and this document is entitled (as read):
19 "CROSS-ANSWERING TESTIMONY OF Deborah Reynolds," dated January
20 17, 2012. And it's in the PSE docket responding to the
21 decoupling proposal of the NW Energy Coalition, and it contains
22 one page of your testimony.

23 Do you recognize this document?

24 A. (Witness reviews document.)

25 (Pause in the proceedings.)

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1 THE WITNESS: Do you have any more of it?

2 (Pause in the proceedings.)

3 (Mr. ffitch left the proceedings.)

4 BY MS. DAVISON:

5 Q. There we go. There's the entire testimony.

6 A. Thank you.

7 (Witness reviews document.)

8 (Pause in the proceedings.)

9 BY MS. DAVISON:

10 Q. My question is whether you recognize this testimony.

11 A. Yes. And I just was trying to get into my head which
12 section of the testimony this was in and get the context, so,
13 yes, I do recognize it.

14 Q. Okay.

15 A. Thank you for the time.

16 Q. Okay. And I would refer you to lines 18 through 20
17 on page 8 of your testimony --

18 A. Mm-hm.

19 Q. -- that's marked as Exhibit 7, the statement that
20 says with regard to (as read): "...the financial impact of full
21 decoupling on the utility's revenues is immediate. The utility
22 should capitalize itself properly due to this important change
23 to its operations. Waiting only causes ratepayers to pay for
24 risk twice: first, by having those risks shifted to ratepayers
25 from investors, and again, by keeping the capital structure the

Deborah J. Reynolds - 4/2/2013

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1 same as if the utilities" -- "the utility was subject to those
2 risks."

3 A. Mm-hm.

4 (Mr. ffitch joined the proceedings.)

5 BY MS. DAVISON:

6 Q. Do you agree with that statement?

7 A. The whole -- the paragraph, or one particular piece?

8 Q. What I read to you.

9 A. So lines 16 through 20?

10 Q. Yes.

11 A. (Witness reviews document.)

12 (Pause in the proceedings.)

13 THE WITNESS: Mostly.

14 BY MS. DAVISON:

15 Q. What part of that paragraph do you no longer agree
16 with?

17 A. (Witness reviews document.)

18 The word "important" on line 17 I would strike.

19 Q. And other than that, you --

20 A. I'm not convinced that the magnitude of the change is
21 as big as I was at that point, even though that was only
22 January, a year ago and a half almost. A year and a third.

23 Q. Okay. All right. So if the decoupling mechanism
24 before us in this proceeding were adopted, how would ratepayers
25 be compensated for the heightened risk they would bear between

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1 BY MS. DAVISON:

2 Q. Sure. Go ahead and list what you can remember.

3 A. So the power cost only rate case. The conservation
4 writers. The -- there are a number of other writers that the
5 Company uses, one for taxes, and I believe the renewable energy
6 credits. Purchased gas adjustments. There may be others that I
7 don't recall.

8 Q. So has Staff done any type of analysis regarding the
9 rate impacts of the items that are exempt from this rate plan?

10 A. I know that analysis occurred, but I -- it was not
11 prepared by me, and I haven't seen the results of it. There was
12 some discussion between Tom Schooley and some other Staff
13 person, and I have not seen the results.

14 Q. All right. So we should ask a data request to Tom
15 Schooley for the analysis of the rate impacts of the items
16 excluded from the rate plan?

17 A. Yes.

18 Q. Okay. So this afternoon, you've referred a great
19 deal to PSE's last general rate case, and on an average basis,
20 is it correct that PSE saw about a 3 percent rate increase?

21 A. I believe that's correct, but I don't recall the
22 exact percentage.

23 Q. So in evaluating the settlement proposal, did Staff
24 go back and evaluate what portion of the GRC rate increase was
25 related to non-power cost items?

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1 A. I don't know. I didn't.

2 Q. Have you heard of anyone looking at these issues?

3 MS. BROWN: Asked and answered.

4 (Reporter interruption for clarification.)

5 THE WITNESS: I don't know. I don't recall.

6 BY MS. DAVISON:

7 Q. So I'm trying to understand. Under this decoupling
8 proposal, will the evaluation process, and all that sort of
9 thing, be recovered through general rates and not the
10 conservation tariff, or how will that be handled?

11 A. I believe that that is correct. It will be recovered
12 through general rates.

13 Q. Okay. In Staff's evaluation of whether or not to
14 support the K-Factor, did PSE present any current attrition
15 studies?

16 A. I don't know if Mr. Schooley received anything like
17 that.

18 Q. Did you hear any discussion about that during your
19 evaluation of this proposal?

20 A. I don't recall. I -- there were a number of data
21 requests from other Staff to PSE looking at both the expedited
22 rate filing and the decoupling filing, and I did not review all
23 those data requests. And a number of them asked for studies, so
24 I'm sorry, I just don't recall.

25 Q. So --

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1 A. But I think you have copies of all the data requests.

2 Q. Were these informal data requests?

3 A. I don't know. That's a process question.

4 Q. Okay. Do you know if Staff conducted any independent
5 analysis of PSE's capital improvement program for the next five
6 years?

7 A. I don't know. I -- I don't know.

8 Q. Did you submit data requests in the decoupling
9 docket? So from the time period of, say, January 2013, to the
10 current time period, to PSE?

11 A. So I supervised Staff who submit data requests on
12 this issue, and I don't know if they submitted the data requests
13 before or after January.

14 Q. Well, my question is from January 2013 forward, did
15 Staff submit data requests to PSE on decoupling?

16 A. I don't know the dates. They're in the -- I'm sorry.
17 I don't know the dates.

18 Q. So you're not aware of whether from January 2013
19 forward there have been any recent data requests on the revised
20 decoupling?

21 A. I did not check the dates on the -- I did not check
22 the dates of the last data request. I don't know when they
23 stopped.

24 Q. Okay. So do you know if Staff conducted any scenario
25 analysis regarding the potential rate impacts of the global

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1 settlement?

2 A. I believe you're going to send me a data request
3 about that, aren't you?

4 Q. Well, this is a slightly different question, the
5 scenario analysis.

6 A. Well, would you define what you mean by "scenario
7 analysis"? You asked me about load and how load would change
8 right before the break.

9 Q. So --

10 A. That is scenario analysis.

11 Q. So my question is whether Staff conducted any
12 scenario analyses of potential outcomes of what the rate impacts
13 would be under the global settlement if approved.

14 A. What do you mean by "scenario analysis"?

15 Q. Well, assuming certain outcomes with regard to load,
16 weather --

17 A. Yes. That is the question that I answered before the
18 break, and you're going to send me a data request about it.

19 Q. So you're not aware, sitting here today, of any
20 analyses were done on that?

21 A. No. I said that there were analyses done on that,
22 and that Tom Schooley did them. And that there was a model that
23 Chris Mickelson had worked on --

24 Q. Okay.

25 A. -- and that you were going to send me a data request,

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1 and we were going to provide that.

2 Q. Okay.

3 A. Okay.

4 Q. So just on a real global level, have you heard Public
5 Counsel say that they did an analysis of the rate impacts of the
6 global settlement and that that could potentially result in a
7 \$200 million revenue requirement increase?

8 A. Yes.

9 Q. And do you disagree with that number?

10 A. That is not the number that I would have expected. I
11 think the number I have seen is closer to 160 million, but
12 that's over the whole four years --

13 Q. So --

14 A. -- that entire period. And I -- honestly, that's in
15 that. It would be better to look at that analysis.

16 Q. So we'll see that number --

17 A. Mm-hm.

18 Q. -- when we get the response to the data request that
19 we asked on the analyses of the global settlement?

20 A. You will.

21 Q. Okay. Thank you. Is there anyone on Staff who is
22 considered an attrition expert?

23 A. I don't know. I -- we have all done a lot of work
24 getting comfortable with attrition, but I don't know who would
25 be considered the attrition expert.

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1 Q. Did Staff bring on any outside attrition expert to
2 evaluate any of these proposals?

3 A. No. We rarely have money for that kind of thing.

4 Q. So shifting gears and moving on to the PCORC, what is
5 the purpose of the requirement that PSE file a general rate case
6 within three months of any rate increase caused by PCORC?

7 A. I don't know.

8 Q. Do you know what the basis is for waiving this
9 requirement in the global settlement?

10 A. That we need a general rate case at the end of -- let
11 me back up. That we have chosen the appropriate point for a
12 general rate case as related to a decoupling mechanism.

13 Q. But Staff didn't find it appropriate to put any
14 limitations on rate increases associated with PCORC?

15 A. No.

16 Q. Would you have any reason to disagree if I told you
17 that one reason for having a general rate case three months
18 after any rate increase associated with PCORC is to see if there
19 are any offsetting factors?

20 A. I would not be surprised.

21 Q. Are you aware of any analyses that Staff has
22 performed to evaluate the impact of waiving the requirement of a
23 general rate case following any increase associated with PCORC?

24 (Pause in the proceedings.)

25 THE WITNESS: Could you repeat the question?

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1 BY MS. DAVISON:

2 Q. Sure. Has Staff performed any analyses of the risk
3 or the cost associated with waiving the general rate case
4 requirement if there is an increase in rates associated with
5 PCORC?

6 A. I don't know, but I would expect that Mr. Schooley
7 might.

8 Q. Okay.

9 MS. BROWN: I would like to take a ten-minute break
10 if that's okay.

11 MS. DAVISON: You know, I am so close to being done.

12 MS. BROWN: Are you closed to being finished?

13 MS. DAVISON: I'm just down to a couple questions, so
14 you may --

15 MS. BROWN: Okay. Talk fast. My bladder is full.

16 MS. DAVISON: Okay. All right. But if you need to
17 go to the rest room --

18 MS. BROWN: No, no. That's all right. Go ahead.

19 MS. DAVISON: Okay. I'm really, really honing in on
20 this. I promise. I'm down to my last two pages.

21 BY MS. DAVISON:

22 Q. So do you know how Staff intends to treat the gains
23 from the sale of PSE's service territory to Jefferson Public
24 Utility District?

25 A. I don't recall.

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1 Q. Do you know if Staff was treating the gains
2 associated with the sale of territory to Jefferson PUD as a
3 known and measurable event?

4 A. I don't recall.

5 Q. Does the global settlement ensure that PSE makes a
6 filing to provide customers with the benefits of the sale of the
7 service territory to Jefferson PUD?

8 A. I don't recall. This is the area I didn't testify
9 about.

10 MS. DAVISON: I'm done. Okay.

11 THE WITNESS: Okay.

12 MS. DAVISON: Thank you.

13 THE WITNESS: Thank you.

14

15 (Deposition concluded at 4:34 p.m.)

16

17 (By agreement between counsel
18 and the witness, signature was
19 reserved.)

20

21 -o0o-

22

23

24

25

WASHINGTON UTILITIES AND TRANSPORTATION COMMISSION
STAFF RESPONSE TO ICNU DATA REQUESTS

DATE PREPARED: March 21, 2013
DOCKETS: UE-121697/UG-121705
REQUESTER: ICNU

WITNESS: Deborah Reynolds
RESPONDER: Deborah Reynolds
TELEPHONE: 360-664-1255

REQUEST NO. 3.4: Regarding the Testimony of Deborah Reynolds, page 15, lines 32, 33, please explain how the revised decoupling proposal is consistent with the Commission's Policy Statement at paragraph 28, which called for a true up of "of revenue attributed to each affected class of customer." Please provide all documents that refer or relate to a true up of revenue by customer class.

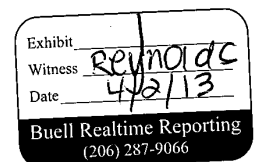
RESPONSE:

First, my testimony at page 15, lines 32-33, refers to off-system sales as described in Element 4 of paragraph 28 of the Decoupling Policy Statement.

The quote in the data request above is from Element 1 of paragraph 28. This is the full quote:

True-up Mechanism. Where, between general rate cases, customer use by class deviates either higher or lower from that determined by the Commission when setting rates, a utility can seek an annual true-up of revenue attributed to each affected class of customer.

The commission does not mention specific tariff schedules in its Decoupling Policy Statement. In my opinion, the decoupling mechanisms appropriately identify two classes of customers included in the mechanisms: residential and non-residential. Further differentiation of customers by rate schedule would contribute unnecessary complexity.



WASHINGTON UTILITIES AND TRANSPORTATION COMMISSION
STAFF RESPONSE TO ICNU DATA REQUESTS

DATE PREPARED: March 21, 2013
DOCKETS: UE-121697/UG-121705
REQUESTER: ICNU

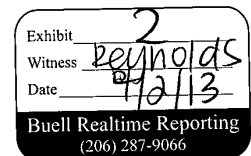
WITNESS: Deborah Reynolds
RESPONDER: Deborah Reynolds
TELEPHONE: 360-664-1255

REQUEST NO. 3.5: Regarding the Testimony of Deborah Reynolds, page 16-17, please verify whether the amended decoupling proposal complies with the Commission's requirement that a decoupling proposal determine the financial benefits associated with off-system sales or avoided costs attributable to the utilities conservation efforts, and net these benefits against the true-up mechanism, as stated in the Report and Policy Statement at paragraph 28. Please provide all related documents.

RESPONSE:

It does not. As I stated in my testimony at page 17, lines 7-12:

In making a determination to either change the PCA as Staff had advocated, or refrain from applying the Commission's decoupling policy on wholesale sales, the Commission has elected the latter. Given this guidance, it is appropriate to maintain the current PCA and approve the revised petition. If the PCA needs to be modified, it should be done separately within a power cost only rate case, or in a general rate case.



WASHINGTON UTILITIES AND TRANSPORTATION COMMISSION
STAFF RESPONSE TO ICNU DATA REQUESTS

DATE PREPARED: March 21, 2013
DOCKETS: UE-121697/UG-121705
REQUESTER: ICNU

WITNESS: Deborah Reynolds
RESPONDER: Deborah Reynolds
TELEPHONE: 360-664-1255

REQUEST NO. 3.2: Regarding the Testimony of Deborah Reynolds, page 8, has Staff evaluated the impact of this decoupling proposal on PSE's return on equity? Please produce all such calculations.

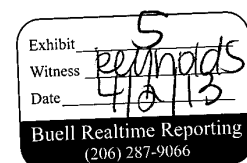
SUPPLEMENTAL REVISED RESPONSE:

No. As my testimony states at page 9, lines 6-8, 18-20, and page 10, lines 1-2:

Staff strongly believes that adjustments to return on equity or to capital structure are only appropriate within a general rate case, where the commission can look at all offsetting factors.

[W]hen combined with the Commission's discussion of the previous decoupling proposal and its discussion of expedited rate filings, which urged parties to come forward with proposals that would reduce the frequency of general rate cases, [this] seems to support acceptance of an allowed rate of return over multiple years.

In any event, Staff did consider the Company's recent rate-of-return performance from the Commission-basis reports for the last six years. This information is attached. Gas operations have been 106 to 215 basis points below the authorized rate of return. Electric operations, since 2008, have been 152 to 214 basis points below the authorized rate of return. I reiterate that the authorized rate of return is only an opportunity to earn, not a guarantee. The Company will still need to control its costs to achieve its authorized rate of return. Staff will continue to use the Commission-basis report to monitor the Company's earnings each year.



ATTACHMENT TO SUPPLEMENTAL REVISED RESPONSE 3.2

PSE Commission Basis Results

For Year of	Docket	ELECTRIC					GRC			ELECTRIC Deviation from Authorized Equity	
		Overall		Equity			Increases			Overall	Equity
		Normalized	Authorized	Normalized	Authorized	Authorized	Date	Percent			
2011	UE-120608	6.62%	8.14%	6.98%	10.10%	10.10%	4/2/2010	3.70%	-1.52%	-3.12%	
2010	UE-110764	6.07%	8.10%	5.57%	10.10%	10.10%			-2.03%	-4.53%	
2009	UE-100719	6.11%	8.25%	5.63%	10.15%	10.15%			-2.14%	-4.52%	
2008	UE-090674	6.39%	8.25%	5.94%	10.15%	10.15%	11/1/2008	7.10%	-1.86%	-4.21%	
2007	UE-080850	8.13%	8.40%	9.89%	10.40%	10.40%	8/2/2007	3.70%	-0.27%	-0.51%	
							1/5/2007	-1.30%			
2006	UE-070825	8.78%	8.40%	10.30%	10.40%	10.40%	7/6/2006	6.00%	0.38%	-0.10%	
2005							3/1/2005	3.90%	-1.24%	-2.83%	
							average>				

For Year of	Docket	GAS					GRC			GAS Deviation from Authorized Equity	
		Overall		Equity			Increases			Overall	Equity
		Normalized	Authorized	Normalized	Authorized	Authorized	Date	Percent			
2011	UG-120609	6.78%	8.14%	7.30%	10.10%	10.10%			-1.36%	-2.80%	
2010	UG-110765	6.24%	8.10%	5.57%	10.10%	10.10%	4/2/2010	0.80%	-1.86%	-4.53%	
2009	UG-100720	6.10%	8.25%	5.63%	10.15%	10.15%			-2.15%	-4.52%	
2008	UG-090675	6.52%	8.25%	5.94%	10.15%	10.15%	11/1/2008	4.60%	-1.73%	-4.21%	
2007	UG-080851	7.34%	8.40%	9.89%	10.40%	10.40%	1/5/2007	3.10%	-1.06%	-0.51%	
2006	UG-070826	7.21%	8.40%	10.30%	10.40%	10.40%	3/1/2005	3.20%	-1.19%	-0.10%	
2005							average>		-1.56%	-2.78%	

Exhibit No. ___ (DJR-1T)
Docket UE-110876/UG-110877
Witness: Deborah J. Reynolds

BEFORE THE WASHINGTON UTILITIES AND TRANSPORTATION COMMISSION

**WASHINGTON UTILITIES AND
TRANSPORTATION COMMISSION,**

Complainant,

v.

**AVISTA CORPORATION d/b/a AVISTA
UTILITIES,**

Respondent.

**DOCKET UE-110876
DOCKET UG-110877**

(Consolidated)

RESPONSE TESTIMONY OF

Deborah J. Reynolds

**STAFF OF
WASHINGTON UTILITIES AND
TRANSPORTATION COMMISSION**

Re: The Decoupling Proposal of the NW Energy Coalition

February 24, 2012

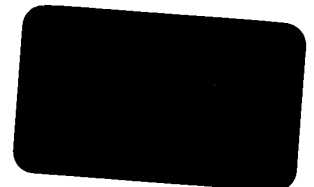
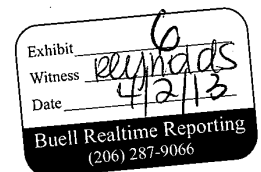


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 C. NWEC’s Proposal Excludes the Impact of Decoupling on the
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 D. NWEC’s Proposal Does Not Condition Recovery on Conservation
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 E. NWEC’s Proposal Does Not Identify Comparable Conservation
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 F. NWEC’s Proposal Does Not Describe Incremental Conservation 16

 G. NWEC’s Proposal Does Not Account for the Net Benefits of
 Off-System Sales and Costs Avoided Due to the Utility’s
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IV. CONCLUSION..... 20

LIST OF EXHIBITS

- Exhibit No. ___ (DJR-2): UTC Staff’s Response to Bench Request in Dockets UE-111048 and UG-111049
- Exhibit No. ___ (DJR-3): NWEC Cover Letter and Data Requests 2-4 Dated September 1, 2011
- Exhibit No. ___ (DJR-4): Excerpt from “Revenue Regulation and Decoupling: A Guide to Theory and Application” (The Regulatory Assistance Project, June 2011) (Cover page and pages 4, 5, 36-39)

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I. INTRODUCTION

Q. Please state your name and business address.

A. My name is Deborah J. Reynolds. My business address is the Richard Hemstad Building, 1300 S. Evergreen Park Dr. SW, Olympia, Washington 98504.

Q. By whom are you employed and in what capacity?

A. I am employed by the Washington Utilities and Transportation Commission (“Commission”) as the Assistant Director of the Conservation and Energy Planning Section of the Regulatory Services Division. My employment at the Commission began in 1999.

Q. Please describe your education and your professional qualifications.

A. I have a Bachelor of Science degree in General Studies emphasizing ecology and statistics and a Master of Regional Planning degree, both from Washington State University. I attended the National Association of Regulatory Utility Commissioners’ Annual Regulatory Studies Program in August 2004, the New Mexico State University’s rate case basics workshop in May 2008, Electric Utility Consultants, Inc.’s cost of service and rate design workshops in August 2008, the International Energy Program Evaluation Conference and training in August 2009, as well as a number of other utility related seminars, conferences, and training opportunities.

1 I am responsible primarily for Staff who review and evaluate conservation
2 programs, conservation resource planning, cost of service, rate spread and rate
3 design, decoupling, reliability, service quality, low-income issues, and other analyses
4 in general rate cases and other tariff filings of Commission-regulated electric and
5 natural gas utilities. I also provide technical assistance to companies on energy
6 regulatory matters.

7 I have participated in the development of Commission rules and examined
8 utility reports for compliance with Commission regulations. I have also presented
9 Staff recommendations at numerous open public meetings. I have filed testimony on
10 decoupling in Avista's consolidated general rate case, Dockets UE-090134, UE-
11 090135 and UG-060518, Staff comments on conservation target filings in Dockets
12 UE-100170, UE-100176, and UE-100177, and testimony on decoupling in Puget
13 Sound Energy, Inc.'s (PSE) consolidated general rate case, Dockets UE-111048 and
14 UG-111049.

15

16

II. PURPOSE AND SUMMARY

17

18 **Q. What is the purpose of your testimony in this proceeding?**

19 A. My testimony responds to the full electric decoupling proposal of the NW Energy
20 Coalition, presented by Mr. Ralph Cavanagh.

21

1 **Q. Have you responded to a decoupling proposal by NVEC in another**
2 **Commission docket?**

3 A. Yes. I filed and defended testimony on this issue in consolidated PSE Dockets UE-
4 111048 and UG-111049.

5

6 **Q. In those PSE dockets, did Staff file a response to a Bench Request regarding**
7 **decoupling?**

8 A. Yes. In those PSE dockets, the Commission issued the same (or substantially the
9 same) decoupling-related Bench Request that the Commission issued in this general
10 rate case. Although the Commission relieved Staff from filing a response in these
11 Avista dockets, I am including a copy of the Bench Request response Staff filed in
12 the PSE dockets so the Commission will have that information available here.
13 Staff's response is my Exhibit No. ___ (DJR-2).

14

15 **Q. Please summarize Staff's response to NVEC's decoupling proposal.**

16 A. In its direct testimony in this case, Avista alleged that it is experiencing growth in
17 costs that are not reflected in rates. A decoupling mechanism will not address that
18 phenomenon. Staff recommends an attrition adjustment as the best way to deal with
19 this issue, including any lost revenues due to conservation.

20 The Commission should reject Mr. Cavanagh's decoupling proposal because
21 it does not comply with the Commission's Decoupling Policy Statement.¹ In their

¹ Report and Policy Statement on Regulatory Mechanisms, Including Decoupling, to Encourage Utilities to Meet or Exceed their Conservation Targets, Docket U-100522 (November 4, 2010) ("Decoupling Policy Statement").

1 joint testimony supporting settlement, the Settling Parties, including Staff,
2 recommend that, in the event that the Commission orders further consideration
3 (beyond this Docket No. UE-110876) or adoption of electric decoupling or any other
4 similar mechanism, this should not occur until the Company's next general rate
5 case.² The Settling Parties reserved the right to advocate any position or to offer
6 recommendations regarding the rejection, adoption or implementation of electric
7 decoupling or other similar mechanisms in Avista's next general rate case or in any
8 future proceeding.³

9

10 **III. DISCUSSION OF NVEC'S DECOUPLING PROPOSAL**

11

12 **Q. Please generally describe NVEC's decoupling proposal.**

13 A. NVEC proposes a full decoupling mechanism for Avista's electric operations.
14 Avista's revenues would be based upon a revenue-per-customer ("RPC") value for
15 all electric customers, except the 22 customers Avista serves under Schedule 25,
16 Extra Large General Service.⁴

17 The NVEC proposal would guarantee Avista would recover that RPC
18 through a deferred accounting and true-up process. The true-ups of actual revenue to
19 the RPC level would occur annually, subject to a three percent rate increase cap.

² The Stipulation states that consideration of any ROE adjustment related to decoupling would be at issue with any decoupling proposal. See fn. 3 of Exhibit No. 1, Settlement Stipulation.

³ Exhibit No. 2, Joint Testimony at 16:13-19.

⁴ Schedules 1 (Residential), 11/12 (General), 21/22 (Large General), 31/32 (Pumping), 41-49 (Street and Area Lighting).

1 Avista would defer any amount above the cap and recover it in later annual rate
2 changes.

3 NWEC proposes that the mechanism run for at least five years, subject to a
4 future evaluation by an independent contractor. Finally, the proposed mechanism
5 requires annual reports by Avista describing its progress toward conservation
6 targets.⁵

7

8 **Q. Does Staff have any general concerns about implementing NWEC's decoupling**
9 **proposal for Avista?**

10 A. Yes, Staff has two general concerns. First, Avista alleges it is experiencing growth
11 in costs that are not reflected in rates.⁶ It is Staff's view that an attrition adjustment
12 is the best way to deal with this issue, including any lost revenues due to
13 conservation.⁷ Decoupling does not address attrition, as Mr. Cavanagh has conceded
14 in testimony he filed in the PSE rate case currently pending before this Commission.⁸

15 Second, the NWEC proposal fails to comply with the most significant
16 elements of the Decoupling Policy Statement, namely:

- 17
- 18 • It does not appropriately analyze the impact of conservation on Avista;
 - 19 • it is not appropriately applied to all customer classes;
 - 20 • it makes no reduction to cost of capital;
 - 21 • it fails to condition RPC recovery on achieving conservation targets;

⁵ The Commission requires Avista to file similar reports per Docket UE-100176;

⁶ Exhibit No. ___ (MTT-1T) at 9:12-15.

⁷ PSE Dockets UE-111048 & UG-111049, Elgin, Exhibit No. ___ (KLE-1T) at 80:5-9.

⁸ PSE Dockets UE-111048 & UG-111049, Cavanagh, Exhibit No. ___ (RCC-1T) at 10:14.

- 1 • it does not identify comparable conservation benefits for low income customers;
2 • it does not describe the incremental conservation the Company should pursue;
3 and
4 • it fails to net increased wholesale sales due to conservation in the true-up.

5 I explain each of these deficiencies in the following sections of my testimony.

6

7 **A. Response to Mr. Cavanagh’s “Fixed Cost Recovery” Analysis**

8

9 **Q. What is the main premise supporting Mr. Cavanagh’s decoupling testimony?**

10 **A.** Mr. Cavanagh’s main supporting premise is: “If Avista helped its customers save just
11 one percent of system-wide electricity use per year every year for the next five years,
12 it would automatically lose almost \$38 million in authorized fixed-cost recovery.”⁹

13

14 **Q. Is that testimony accurate?**

15 **A.** No. Mr. Cavanagh uses an extremely broad definition of “fixed costs” that includes
16 costs that are not “fixed”. As a result, Mr. Cavanagh’s \$38 million over five years is
17 a gross overstatement.

18 Mr. Cavanagh believes his definition of “fixed cost” is consistent with how
19 that term is used in a recent publication regarding decoupling by the Regulatory
20 Assistance Project (RAP), entitled *Revenue Regulation and Decoupling*

⁹ Cavanagh, Exhibit No. ___ (RCC-1T) at 2:12-15 and at 5:20 to 6:20.

1 (June 2011).¹⁰ In fact, that RAP publication did not define “fixed costs”. RAP was
2 addressing decoupling in the context of utilities with fuel adjustment mechanisms
3 that allow for full recovery of production costs. Therefore, RAP needed to
4 distinguish between costs that were covered by “fully reconciled” fuel adjustment
5 mechanisms and costs that were not. RAP uses the terms “production” and “non-
6 production” costs to make that distinction. This is demonstrated in RAP’s discussion
7 on pages 4-5 of its publication, which are in my Exhibit No. ___ (DJR-4).

8 In short, RAP was not trying to distinguish between “fixed” and “variable”
9 costs, as Mr. Cavanagh tries to do in his testimony.¹¹

10 In addition, and perhaps more important, Mr. Cavanagh’s proposed
11 decoupling mechanism includes in the RPC all of Avista’s investment-related costs
12 associated with power supply, including investment in generating facilities and
13 transmission. If full decoupling were in effect, and Avista experienced lower retail
14 sales due to conservation, Avista would be able to sell the unused power in the
15 wholesale market, thus recovering much or all of this cost twice: once through the
16 decoupling mechanism, and once from wholesale customers. Though Mr. Cavanagh

¹⁰ According to his testimony Exhibit No. ___ (RCC-1T) at 5:21 to 6:5, Mr. Cavanagh relies on the Company’s response to NWECC Data Request 2. In NWECC Data Request 2, which I have included as my Exhibit No. ___ (DJR-3), NWECC instructed Avista to use the following definition of “fixed costs”:

please define “fixed costs” as the company’s revenue requirement excluding production costs, which “are those that vary more or less directly with energy consumption in the short run”, including “fuel, purchased power”, and “transmission by others”.

According to those same NWECC data request instructions, these definitions are from: “Regulatory Assistance Project, *Revenue Regulation and Decoupling* (June 2011, p. 4).”

¹¹ The accounting definition of a “fixed cost” is a cost that remains unchanged despite changes in volume or other units of production.

1 correctly excluded these costs in his PSE decoupling proposal, he fails to do so in his
2 Avista proposal.¹²

3

4 **Q. Is Avista's fuel adjustment clause "fully reconciled," as RAP uses that term?**

5 A. No. Avista's Energy Recovery Mechanism (ERM) has a dead band and sharing
6 bands, which means, by definition, Avista does not fully recover all production costs
7 within the mechanism. This not only proves Mr. Cavanagh improperly has taken the
8 RAP publication out of context, but it also presents significant issues for full
9 decoupling. As I discuss in more detail later, NWECC's proposal fails to address
10 those issues.

11

12 **B. NWECC's Proposal is Not Applied to All Customer Classes**

13

14 **Q. How does the Decoupling Policy Statement address the application of full
15 decoupling to customer classes?**

16 A. The Commission states that a full decoupling mechanism should include all customer
17 classes, unless it would be lawful or consistent with "the public interest" to do
18 otherwise:

19 *Application to Customer Classes.* Generally, a full decoupling proposal
20 should cover all customer classes. However, where in the public interest and
21 not unlawfully discriminatory or preferential, the Commission will consider a
22 proposal that would apply to fewer than all customer classes.¹³
23

¹² In the current low natural gas price environment, Avista would probably not recover all of its power supply costs through wholesale sales.

¹³ Decoupling Policy Statement at 18, Criterion 1, ¶ 28.

1 **Q. Is the Commission's policy appropriate?**

2 A. Yes. The discrimination and preference statutes are part of the Commission's overall
3 regulation of utilities; although there may be circumstances where excluding a
4 customer class would satisfy those statutes and also be in the "public interest".
5

6 **Q. Does NWEC's proposed decoupling mechanism include all customers?**

7 A. No. NWEC's proposal exempts all 22 customers Avista serves under Schedule 25,
8 Extra Large General Service.¹⁴ Typically, these customers are very large industrial
9 customers.
10

11 **Q. What specific reasons does Mr. Cavanagh give for excluding customers served
12 under Schedule 25 from decoupling?**

13 A. Mr. Cavanagh exempts Schedule 25 customers on the basis that this schedule "has so
14 few members (22) and accounts for a relatively small fraction of the fixed cost
15 revenue requirement that Avista recovers through its energy sales (about 10%,
16 although the class accounts for almost 20% of retail electricity sales)."¹⁵
17

18 **Q. Are these specific reasons sufficient to exempt these customers from
19 decoupling?**

20 A. No, although I do not offer a legal opinion regarding the discrimination or undue
21 preference statutes. The number of customers in a rate schedule or their relative
22 portion of electricity sales are facts, not reasons. Schedule 25 customers participate

¹⁴ Cavanagh, Exhibit No. ___ (RCC-1T) at 10:3.

¹⁵ Cavanagh, Exhibit No. ___ (RCC-1T) at 10:3-6.

1 in Avista's conservation programs. The sample decoupling mechanism found in my
2 Exhibit No. ___ (DJR-2) included all customers.¹⁶

3 In sum, the Commission needs and deserves much more justification than
4 NWECA has supplied before exempting Schedule 25 customers.

5

6 **C. NWECA's Proposal Excludes the Impact of Decoupling on the Rate of Return**

7

8 **Q. What does the Decoupling Policy Statement say with respect to the impact of**
9 **full decoupling on a utility's cost of capital?**

10 **A.** The Commission contemplates full decoupling will reduce the utility's cost of
11 capital:

12 By reducing the risk of volatility of revenue based on customer usage, both
13 up and down, such a mechanism can serve to reduce risk to the company, and
14 therefore to investors, which in turn should benefit customers by reducing a
15 company's debt and equity costs. This reduction in costs would flow through
16 to ratepayers in the form of rates that would be lower than they otherwise
17 would be, as the rates would be set to reflect the assumption of more risk by
18 ratepayers.¹⁷

19
20 The Commission specifically requires a full decoupling mechanism proposal
21 to evaluate its impact on the return on equity:

22 *Impact on Rate of Return.* Evidence evaluating the impact of the proposal on
23 risk to investors and ratepayers and its effect on the utility's ROE.¹⁸

24

¹⁶ See Exhibit No. ___ (DJR-2), at 8 and 9, and Appendix 1 Workpapers, Electric, at 1c.

¹⁷ Decoupling Policy Statement at 16-17, ¶ 27.

¹⁸ Id. at 17, Element 2, ¶ 28.

1 **Q. Is this policy appropriate?**

2 A. Yes. Full decoupling changes the utility's revenue risk by guaranteeing a specific
3 amount of revenue per customer regardless of typical causes of fluctuation in
4 revenue related to weather, economic conditions, or any other condition. Reduced
5 revenue volatility should translate into lower capital costs, either as a lower required
6 return on equity or the need for less equity in the utility's capital structure.

7
8 **Q. Does NWECC recognize any change to Avista's cost of capital due to full
9 decoupling?**

10 A. No. Apparently, Mr. Cavanagh believes full decoupling could actually *increase*
11 Avista's cost of equity, based on a study by the Brattle Group that found the cost of
12 equity to be higher for the decoupled gas utilities studied.¹⁹

13 In any event, Mr. Cavanagh concludes that the only possible cost of capital
14 benefit will be through a potential reduction in the utility's equity ratio, but, even
15 then, he proposes this capital structure benefit flow to ratepayers if and only if, and
16 only after, the utility actually decreases its equity ratio. He claims the Ratepayer
17 Assistance Project ("RAP") agrees with him on this timing issue.²⁰

18
19 **Q. Should the Commission wait to recognize any cost of capital benefit from
20 decoupling?**

¹⁹ Cavanagh, Exhibit No. ___ (RCC-1T) at 16:13-19.

²⁰ Id. at 17:1-3.

1 A. No. The Commission should reject Mr. Cavanagh's proposal as inconsistent with an
2 important element of the Decoupling Policy Statement: customers should receive the
3 benefits of the revenue risk reduction resulting from decoupling.

4 The Brattle Group study upon which Mr. Cavanagh relies did not attempt to
5 exclude any other variables that may have contributed to the higher cost of equity for
6 the studied utilities, such as market perceptions about the consistency of the
7 regulatory agencies that implement decoupling.²¹ Consequently, its conclusion about
8 higher cost of equity for decoupled gas utilities is suspect, and insufficient as
9 evidence on the appropriate cost of capital for Avista under a decoupling mechanism.

10

11 **Q. Did RAP agree, as Mr. Cavanagh states, that any capital structure benefits**
12 **should be passed through to customers, if and only if, and only when, the utility**
13 **actually achieves those improvements?**

14 A. No. Nowhere in its publication does RAP recommend regulators wait until actual
15 capital structure benefits materialize. In fact, RAP considers it appropriate to
16 recognize cost of capital improvements at the time full decoupling is put into place.

17 In particular, RAP estimates the equity ratio could be lower by three
18 percentage points due to risk-mitigation benefits of decoupling.²² RAP also
19 recognizes cost of capital benefits of full decoupling when it is implemented.²³

²¹ See Exhibit No. ___ (DJR-4) Regulatory Assistance Project, *Revenue Regulation and Decoupling: A Guide to Theory and Application* (June 2011), at 38, section 10.2. "If the risk mitigation measure is put in place only for a limited period, or the regulatory commission has a record of changing its regulatory principles frequently, the ratings agency may not recognize the measure."

²² Id. at 38, first paragraph.

²³ Id. at 39, first paragraph.

1 Though RAP suggests against lowering the cost of equity at the time a
2 decoupling mechanism is implemented, RAP also suggests that regulators may want
3 to lower the utility's equity ratio "when regulators consider how to flow through the
4 risk-mitigation benefits of decoupling to consumers when a mechanism is put into
5 place."²⁴ In other words, RAP agrees with the Decoupling Policy Statement that cost
6 of capital-related reductions may appropriately coincide with the adoption of a
7 decoupling mechanism.

8

9 **Q. Have other commissions lowered a utility's cost of capital when implementing a**
10 **decoupling mechanism?**

11 A. Yes, the Public Service Commission of Maryland, in its approval of a decoupling
12 mechanism for each of its three investor-owned utilities, reduced the return on equity
13 by 50 basis points. The District of Columbia Public Service Commission did the
14 same.²⁵

15

16 **Q. If the Commission approves a decoupling mechanism, how could the**
17 **Commission implement its cost of capital reduction policy?**

18 A. The Commission could reduce the overall rate of return by adopting a return on
19 equity in the lower end of a reasonable range, or by reducing the amount of equity in
20 the company's ratemaking capital structure, or both. However, while the Settlement
21 Stipulation the Commission approved in this docket identifies an agreed overall rate
22 of return, it does not identify a specific capital structure or specific cost rates.

²⁴ Id. at 39, last paragraph.

²⁵ Decoupling Policy Statement, Appendix 6, at 3.

1 Consequently, absent a fuller record on rate of return, the Commission will not be
2 able to apply its cost of capital reduction policy, should it decide to implement full
3 decoupling at this point in this case.

4

5 **D. NWEC's Proposal Does Not Condition Recovery on Conservation Achievement**

6

7 **Q. What is the Commission's policy regarding meeting conservation targets and**
8 **revenue per customer recovery by a utility under a decoupling mechanism?**

9 A. It is essential that the decoupled utility meet its conservation targets: "Revenue
10 recovery by the company under the mechanism will be conditioned upon a utility's
11 level of achievement with respect to its conservation target."²⁶ Later in the
12 Decoupling Policy Statement, in the discussion about direct conservation incentives,
13 the Commission explains further:

14 However, the EIA, in RCW 19.285.060(4), provides us with the express
15 authority to provide such incentives: "The commission ... may consider
16 providing positive incentives for an investor-owned utility to exceed the
17 targets established in RCW 19.285.040." We do not read this provision to
18 permit us to provide incentives to acquire conservation that is not cost-
19 effective. Rather, we read this to suggest that, between the biennial
20 conservation targets designed to determine what cost-effective conservation
21 can be required, the electric utility may be able to acquire additional
22 conservation as technology is improved, federal or other matching funds
23 become available, or for other reasons that were not known at the time of the
24 setting of the target.²⁷
25

²⁶ Id. at 17, Description of Mechanism, ¶ 28.

²⁷ Id. at 20, ¶ 31, 32.

1 **Q. Can this policy be practically applied?**

2 A. Yes. On page 14 of my Exhibit No. ___ (DJR-2), Staff's response to the
3 Commission's Bench Request in Docket UE-111048 and UG-111049, Staff
4 identified a Conservation Test that would implement this policy. That test could
5 apply to Avista as well.

6

7 **Q. Does NWECC's proposal condition Avista's revenue recovery under decoupling
8 with achieving the Company's conservation targets?**

9 A. No.

10

11 **E. NWECC's Proposal Does Not Identify Comparable Conservation Benefits to
12 Low-Income Customers**

13

14 **Q. What is the Commission's policy on conservation for low income customers in
15 the context of full decoupling?**

16 A. The Commission's policy is:

17 *Low-income.* A utility proposing a full decoupling mechanism must
18 demonstrate whether or not its conservation programs provide benefits to
19 low-income ratepayers that are roughly comparable to other ratepayers and, if
20 not, it must provide low-income ratepayers targeted programs aimed at
21 achieving a level of conservation comparable to that achieved by other
22 ratepayers, so long as such programs are feasible within cost-effectiveness
23 standards.²⁸

24

25

²⁸ Id. at 19, Criterion 4, ¶ 28.

1 **Q. Does NWEC's proposal satisfy this Commission policy?**

2 A. No. In response to Staff Data Request 12, NWEC states that "Mr. Cavanagh has not
3 conducted such an analysis."
4

5 **Q. Did Staff independently determine whether Avista's conservation programs
6 provide benefits to low-income ratepayers that are roughly comparable to other
7 ratepayers?**

8 A. No. Staff does not have the information available to conduct such analysis.
9

10 **F. NWEC's Proposal Does Not Describe Incremental Conservation**
11

12 **Q. What is the Commission's policy regarding a utility's acquisition of more
13 conservation than it would have acquired absent decoupling?**

14 A. The Commission requires a decoupling proposal to contain: "Evidence describing
15 any incremental conservation the company intends to pursue in conjunction with the
16 mechanism".²⁹
17

18 **Q. Does Mr. Cavanagh address this policy?**

19 A. No. The only specific levels of conservation Mr. Cavanagh refers to are
20 conservation targets that are in place for Avista today, absent decoupling.³⁰
21

²⁹ Id. at 19, Criterion 3, ¶ 28.

³⁰ Cavanagh, Exhibit No. ___ (RCC-1T) at 7:1-13.

1 **G. NWEC's Proposal Does Not Account for the Net Benefits of Off-System Sales**
2 **and Costs Avoided Due to the Utility's Conservation Efforts**
3

4 **Q. What is the Commission's policy on increased wholesale sales as a result of**
5 **decoupling?**

6 A. The Commission requires a full decoupling mechanism to account for certain off-
7 system sales and avoided costs, and to net the benefits as part of the true-up:

8 *Accounting for Off-System Sales and Avoided Costs.* A description of the
9 method the company intends to use to determine the financial benefits
10 associated with off-system sales or avoided costs attributable to the utility's
11 conservation efforts and then to net these benefits against the true-up
12 provided in this mechanism.³¹
13

14 In the related footnote, the Commission explains:

15
16 In principle, for every megawatt hour saved through the operation of the
17 utility's conservation program, it has the opportunity to either sell the same in
18 the appropriate market (off-system sales), or avoid having to purchase or
19 produce electricity to meet its load requirements. The accounting of this
20 form of found revenue differs between electric utilities with power cost
21 adjustment mechanisms and those without. After rates have been set for an
22 electric utility that does not have a power cost adjustment mechanism, the
23 marginal avoided cost of producing or buying electricity, or the marginal
24 revenue (net of marginal cost) from the sale of electricity made surplus by
25 conservation not incorporated into the calculation of the power costs, is a
26 direct benefit to the utility shareholders. For utilities with a power cost
27 adjustment mechanism, loads are projected in a future test year, with
28 reductions in the load for the expected conservation levels. Consequently, for
29 the effective rate year following the setting of rates, only conservation above
30 the expected level of conservation would result in an opportunity to reduce
31 power costs or realize additional revenues from incremental sales. In the
32 years after the projected rate year, the marginal avoided cost of producing or
33 buying electricity, or the marginal revenue (net of marginal cost) from a sale
34 of electricity made surplus by conservation, is a direct benefit.³²
35

³¹ Decoupling Policy Statement at 17, Element 4, ¶ 28.

³² Id. at n. 45.

1 **Q. Is this Commission policy appropriate?**

2 A. Yes. When customers conserve energy, the utility should market the electricity the
3 utility would have sold to its own retail customers. Moreover, the utility incurs
4 lower costs due to the wholesale sales, such as reduced line losses, reduced
5 uncollectible expense, and avoidance of the Public Utility Tax, which effectively
6 applies only to retail sales.

7 Under full decoupling, ratepayers guarantee the utility's recovery of a
8 specified level of revenues per customer. It is appropriate for the decoupling
9 mechanism to recognize the benefits of enhanced wholesale sales that may result
10 from decoupling.

11

12 **Q. Can this policy be practically applied?**

13 A. Yes, but not within the decoupling mechanism itself. Rather, this policy could be
14 implemented by revising the ERM. One possible revision could be to eliminate the
15 dead band from the ERM.³³ However, doing that would also eliminate a key feature
16 of the ERM: to provide rate stability to consumers except under extreme
17 circumstances, while giving the Company a very strong incentive to manage power
18 supply costs to avoid such extreme circumstances. Needless to say, addressing this
19 policy will require more detailed analysis than has been presented thus far.

20

³³ In the absence of an energy cost adjustment clause, this part of the decoupling policy would be very difficult and administratively burdensome to apply.

1 **Q. Does NWECA's proposal apply this Commission policy?**

2 A. No. Mr. Cavanagh suggests the Commission ignore this policy on the basis of his
3 belief that Avista's ERM "already responds to this concern" regarding enhanced
4 wholesale sales.³⁴ In short, Mr. Cavanagh chooses to not apply the Commission's
5 decoupling policy on wholesale sales, without adequately supporting that choice.

6

7 **Q. Is Mr. Cavanagh's characterization of Avista's ERM correct?**

8 A. No. Because Avista's ERM has a "dead band" and "sharing bands", the practical
9 result under full decoupling is that ratepayers would not receive the full benefit of
10 incremental wholesale sales occasioned by any reductions in retail sales. This is
11 because any revenues from such wholesale sales likely would fall within the dead
12 band and, therefore, Avista would retain the benefits.³⁵

13

14 **Q. Is it consistent with the Decoupling Policy Statement to allow decoupling while
15 also maintaining Avista's current ERM?**

16 A. No. The current structure of the ERM and the Commission's decoupling policy on
17 enhanced wholesale sales are not compatible. If the Commission wishes to
18 implement full decoupling for Avista, there are two choices: change the ERM, or do
19 not apply the Commission's decoupling policy on wholesale sales.

20

³⁴ Cavanagh, Exhibit No. ___ (RCC-1T) at 12:7-13.

³⁵ Exhibit No. ___ (DJR-2), at 18.

1 **Q. What choice should the Commission make and why?**

2 A. Should the Commission choose to implement full decoupling for Avista, it should
3 maintain its policy regarding wholesale sales. However, Staff believes the
4 Commission does not have a sufficient record in this docket to both address full
5 decoupling and appropriately revise the ERM. Therefore, any decision to adopt full
6 decoupling should await full examination of any required revisions to the ERM.

7

8

IV. CONCLUSION

9

10 **Q. Please summarize your position on the full decoupling proposal offered by**
11 **NWEC.**

12 A. The Commission should reject in its entirety NWEC's full decoupling proposal as
13 inconsistent with the several elements I have identified from the Commission's
14 Decoupling Policy Statement.

15

16 **Q. Should the Commission nevertheless decide to implement full decoupling at this**
17 **time, what issues should be addressed prior to implementation?**

18 A. The Commission should:

- 19 • Require additional evidence quantifying the change in the overall rate of return
20 occasioned by the specific decoupling mechanism adopted by the Commission,
21 or the amount of equity in the ratemaking capital structure the Commission
22 deems appropriate, or both.

- 1 • Adopt the Earnings Test as outlined in Exhibit No. ___ (DJR-2), modifying the
2 Earnings Test dead band as appropriate.³⁶
- 3 • Adopt the Conservation Test as outlined in Exhibit No. ___ (DJR-2).³⁷
- 4 • Require third party evaluation of conservation achievement, which will also
5 identify any incremental conservation.
- 6 • Require third party evaluation of comparable benefits for low-income customers.
- 7 • Require revision of the ERM.

8

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

10 **A. Yes.**

11

12

³⁶ Exhibit No. ___ (DJR-2) includes an earnings test for discussion purposes that was essentially the same as that addressed by Mr. Cavanagh. It is also very similar to the earnings test in Avista's gas decoupling mechanism, although Avista's gas mechanism does not contemplate the 25 basis point dead band. I would clarify, however, that whatever dead band is chosen by the Commission, it should be based on a rate of return set in the general rate case that implements decoupling. In addition, the dead band should be carefully crafted to provide upside earnings only if the Company can demonstrate a connection between achieved efficiencies beyond those required by statute and its earnings at the high end of any range determined to be fair.

³⁷ Exhibit No. ___ (DJR-2), at 13-14, and Appendix 1 Workpapers, Electric, at 1b.

Exhibit No. ___ (DJR-3T)
Docket UE-111048/UG-111049
Witness: Deborah J. Reynolds

BEFORE THE WASHINGTON UTILITIES AND TRANSPORTATION COMMISSION

**WASHINGTON UTILITIES AND
TRANSPORTATION COMMISSION,**

Complainant,

v.

PUGET SOUND ENERGY, Inc.

Respondent.

**DOCKET UE-111048
DOCKET UG-111049**

(Consolidated)

CROSS-ANSWERING TESTIMONY OF

Deborah J. Reynolds

**STAFF OF
WASHINGTON UTILITIES AND
TRANSPORTATION COMMISSION**

Responding to the Decoupling Proposal of the NW Energy Coalition

January 17, 2012



1 only after, the utility actually decreases its equity ratio. He claims the Ratepayer
2 Assistance Project (“RAP”) agrees with him on this timing issue.¹⁶

3
4 **Q. Should the Commission agree that PSE’s cost of equity likely will be higher**
5 **under full decoupling and that it should wait for any capital structure benefits**
6 **to actually occur, before recognizing any cost of capital benefit from**
7 **decoupling?**

8 A. No. The Commission should reject Mr. Cavanagh’s proposal as inconsistent with an
9 important element of the Decoupling Policy Statement: customers should receive the
10 benefits of the risk reduction resulting from decoupling.

11 Moreover, the Brattle Group study upon which Mr. Cavanagh relies did not
12 attempt to exclude any other variables that may have contributed to the higher cost of
13 equity for the studied utilities, such as market perceptions about the consistency of
14 the regulatory agencies that implement decoupling.¹⁷ Consequently, its conclusion
15 about higher cost of equity for decoupled gas utilities is suspect.

16 In addition, the financial impact of full decoupling on the utility’s revenues is
17 immediate, and the utility should capitalize itself properly due to this important
18 change to its operations. Waiting only causes ratepayers to pay for risks twice: first,
19 by having those risks shifted to ratepayers from investors, and again, by keeping the
20 capital structure the same as if the utility was subject to those risks.

¹⁶ Id. at 20:12-17.

¹⁷ See Regulatory Assistance Project, Revenue Regulation and Decoupling: A Guide to Theory and Application (June 2011), at 38, section 10.2. “If the risk mitigation measure is put in place only for a limited period, or the regulatory commission has a record of changing its regulatory principles frequently, the ratings agency may not recognize the measure.”

WASHINGTON UTILITIES AND TRANSPORTATION COMMISSION
STAFF RESPONSE TO ICNU DATA REQUESTS

DATE PREPARED: March 21, 2013
DOCKETS: UE-121697/UG-121705
REQUESTER: ICNU

WITNESS: Deborah Reynolds
RESPONDER: Deborah Reynolds
TELEPHONE: 360-664-1255

REQUEST NO. 3.4: Regarding the Testimony of Deborah Reynolds, page 15, lines 32, 33, please explain how the revised decoupling proposal is consistent with the Commission's Policy Statement at paragraph 28, which called for a true up of "of revenue attributed to each affected class of customer." Please provide all documents that refer or relate to a true up of revenue by customer class.

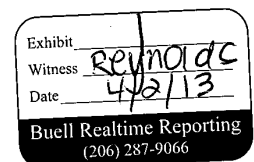
RESPONSE:

First, my testimony at page 15, lines 32-33, refers to off-system sales as described in Element 4 of paragraph 28 of the Decoupling Policy Statement.

The quote in the data request above is from Element 1 of paragraph 28. This is the full quote:

True-up Mechanism. Where, between general rate cases, customer use by class deviates either higher or lower from that determined by the Commission when setting rates, a utility can seek an annual true-up of revenue attributed to each affected class of customer.

The commission does not mention specific tariff schedules in its Decoupling Policy Statement. In my opinion, the decoupling mechanisms appropriately identify two classes of customers included in the mechanisms: residential and non-residential. Further differentiation of customers by rate schedule would contribute unnecessary complexity.



WASHINGTON UTILITIES AND TRANSPORTATION COMMISSION
STAFF RESPONSE TO ICNU DATA REQUESTS

DATE PREPARED: March 21, 2013
DOCKETS: UE-121697/UG-121705
REQUESTER: ICNU

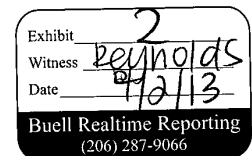
WITNESS: Deborah Reynolds
RESPONDER: Deborah Reynolds
TELEPHONE: 360-664-1255

REQUEST NO. 3.5: Regarding the Testimony of Deborah Reynolds, page 16-17, please verify whether the amended decoupling proposal complies with the Commission's requirement that a decoupling proposal determine the financial benefits associated with off-system sales or avoided costs attributable to the utilities conservation efforts, and net these benefits against the true-up mechanism, as stated in the Report and Policy Statement at paragraph 28. Please provide all related documents.

RESPONSE:

It does not. As I stated in my testimony at page 17, lines 7-12:

In making a determination to either change the PCA as Staff had advocated, or refrain from applying the Commission's decoupling policy on wholesale sales, the Commission has elected the latter. Given this guidance, it is appropriate to maintain the current PCA and approve the revised petition. If the PCA needs to be modified, it should be done separately within a power cost only rate case, or in a general rate case.



WASHINGTON UTILITIES AND TRANSPORTATION COMMISSION
STAFF RESPONSE TO ICNU DATA REQUESTS

DATE PREPARED: March 21, 2013
DOCKETS: UE-121697/UG-121705
REQUESTER: ICNU

WITNESS: Deborah Reynolds
RESPONDER: Deborah Reynolds
TELEPHONE: 360-664-1255

REQUEST NO. 3.2: Regarding the Testimony of Deborah Reynolds, page 8, has Staff evaluated the impact of this decoupling proposal on PSE's return on equity? Please produce all such calculations.

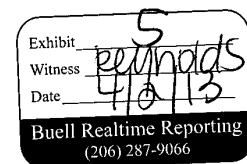
SUPPLEMENTAL REVISED RESPONSE:

No. As my testimony states at page 9, lines 6-8, 18-20, and page 10, lines 1-2:

Staff strongly believes that adjustments to return on equity or to capital structure are only appropriate within a general rate case, where the commission can look at all offsetting factors.

[W]hen combined with the Commission's discussion of the previous decoupling proposal and its discussion of expedited rate filings, which urged parties to come forward with proposals that would reduce the frequency of general rate cases, [this] seems to support acceptance of an allowed rate of return over multiple years.

In any event, Staff did consider the Company's recent rate-of-return performance from the Commission-basis reports for the last six years. This information is attached. Gas operations have been 106 to 215 basis points below the authorized rate of return. Electric operations, since 2008, have been 152 to 214 basis points below the authorized rate of return. I reiterate that the authorized rate of return is only an opportunity to earn, not a guarantee. The Company will still need to control its costs to achieve its authorized rate of return. Staff will continue to use the Commission-basis report to monitor the Company's earnings each year.



ATTACHMENT TO SUPPLEMENTAL REVISED RESPONSE 3.2

PSE Commission Basis Results

For Year of	Docket	ELECTRIC				GRC			ELECTRIC Deviation from Authorized Equity					
		Overall		Equity		Increases			Overall	Equity				
		Normalized	Authorized	Normalized	Authorized	Date	Percent							
2011	UE-120608	6.62%	8.14%	6.98%	10.10%									
2010	UE-110764	6.07%	8.10%	5.57%	10.10%	4/2/2010	3.70%							
2009	UE-100719	6.11%	8.25%	5.63%	10.15%									
2008	UE-090674	6.39%	8.25%	5.94%	10.15%	11/1/2008	7.10%							
2007	UE-080850	8.13%	8.40%	9.89%	10.40%	8/2/2007	3.70%							
						1/5/2007	-1.30%							
2006	UE-070825	8.78%	8.40%	10.30%	10.40%	7/6/2006	6.00%							
2005						3/1/2005	3.90%							
							average>							

For Year of	Docket	GAS				GRC			GAS Deviation from Authorized Equity					
		Overall		Equity		Increases			Overall	Equity				
		Normalized	Authorized	Normalized	Authorized	Date	Percent							
2011	UG-120609	6.78%	8.14%	7.30%	10.10%									
2010	UG-110765	6.24%	8.10%	5.57%	10.10%	4/2/2010	0.80%							
2009	UG-100720	6.10%	8.25%	5.63%	10.15%									
2008	UG-090675	6.52%	8.25%	5.94%	10.15%	11/1/2008	4.60%							
2007	UG-080851	7.34%	8.40%	9.89%	10.40%	1/5/2007	3.10%							
2006	UG-070826	7.21%	8.40%	10.30%	10.40%	3/1/2005	3.20%							
2005							average>							

Exhibit No. ___ (DJR-1T)
Docket UE-110876/UG-110877
Witness: Deborah J. Reynolds

BEFORE THE WASHINGTON UTILITIES AND TRANSPORTATION COMMISSION

**WASHINGTON UTILITIES AND
TRANSPORTATION COMMISSION,**

Complainant,

v.

**AVISTA CORPORATION d/b/a AVISTA
UTILITIES,**

Respondent.

**DOCKET UE-110876
DOCKET UG-110877**

(Consolidated)

RESPONSE TESTIMONY OF

Deborah J. Reynolds

**STAFF OF
WASHINGTON UTILITIES AND
TRANSPORTATION COMMISSION**

Re: The Decoupling Proposal of the NW Energy Coalition

February 24, 2012

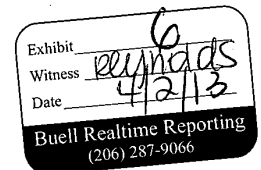


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IV. CONCLUSION..... 20

LIST OF EXHIBITS

- Exhibit No. ___ (DJR-2): UTC Staff’s Response to Bench Request in Dockets UE-111048 and UG-111049
- Exhibit No. ___ (DJR-3): NWECS Cover Letter and Data Requests 2-4 Dated September 1, 2011
- Exhibit No. ___ (DJR-4): Excerpt from “Revenue Regulation and Decoupling: A Guide to Theory and Application” (The Regulatory Assistance Project, June 2011) (Cover page and pages 4, 5, 36-39)

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I. INTRODUCTION

Q. Please state your name and business address.

A. My name is Deborah J. Reynolds. My business address is the Richard Hemstad Building, 1300 S. Evergreen Park Dr. SW, Olympia, Washington 98504.

Q. By whom are you employed and in what capacity?

A. I am employed by the Washington Utilities and Transportation Commission (“Commission”) as the Assistant Director of the Conservation and Energy Planning Section of the Regulatory Services Division. My employment at the Commission began in 1999.

Q. Please describe your education and your professional qualifications.

A. I have a Bachelor of Science degree in General Studies emphasizing ecology and statistics and a Master of Regional Planning degree, both from Washington State University. I attended the National Association of Regulatory Utility Commissioners’ Annual Regulatory Studies Program in August 2004, the New Mexico State University’s rate case basics workshop in May 2008, Electric Utility Consultants, Inc.’s cost of service and rate design workshops in August 2008, the International Energy Program Evaluation Conference and training in August 2009, as well as a number of other utility related seminars, conferences, and training opportunities.

1 I am responsible primarily for Staff who review and evaluate conservation
2 programs, conservation resource planning, cost of service, rate spread and rate
3 design, decoupling, reliability, service quality, low-income issues, and other analyses
4 in general rate cases and other tariff filings of Commission-regulated electric and
5 natural gas utilities. I also provide technical assistance to companies on energy
6 regulatory matters.

7 I have participated in the development of Commission rules and examined
8 utility reports for compliance with Commission regulations. I have also presented
9 Staff recommendations at numerous open public meetings. I have filed testimony on
10 decoupling in Avista's consolidated general rate case, Dockets UE-090134, UE-
11 090135 and UG-060518, Staff comments on conservation target filings in Dockets
12 UE-100170, UE-100176, and UE-100177, and testimony on decoupling in Puget
13 Sound Energy, Inc.'s (PSE) consolidated general rate case, Dockets UE-111048 and
14 UG-111049.

15

16

II. PURPOSE AND SUMMARY

17

18 **Q. What is the purpose of your testimony in this proceeding?**

19 A. My testimony responds to the full electric decoupling proposal of the NW Energy
20 Coalition, presented by Mr. Ralph Cavanagh.

21

1 **Q. Have you responded to a decoupling proposal by NVEC in another**
2 **Commission docket?**

3 A. Yes. I filed and defended testimony on this issue in consolidated PSE Dockets UE-
4 111048 and UG-111049.

5

6 **Q. In those PSE dockets, did Staff file a response to a Bench Request regarding**
7 **decoupling?**

8 A. Yes. In those PSE dockets, the Commission issued the same (or substantially the
9 same) decoupling-related Bench Request that the Commission issued in this general
10 rate case. Although the Commission relieved Staff from filing a response in these
11 Avista dockets, I am including a copy of the Bench Request response Staff filed in
12 the PSE dockets so the Commission will have that information available here.
13 Staff's response is my Exhibit No. ___ (DJR-2).

14

15 **Q. Please summarize Staff's response to NVEC's decoupling proposal.**

16 A. In its direct testimony in this case, Avista alleged that it is experiencing growth in
17 costs that are not reflected in rates. A decoupling mechanism will not address that
18 phenomenon. Staff recommends an attrition adjustment as the best way to deal with
19 this issue, including any lost revenues due to conservation.

20 The Commission should reject Mr. Cavanagh's decoupling proposal because
21 it does not comply with the Commission's Decoupling Policy Statement.¹ In their

¹ Report and Policy Statement on Regulatory Mechanisms, Including Decoupling, to Encourage Utilities to Meet or Exceed their Conservation Targets, Docket U-100522 (November 4, 2010) ("Decoupling Policy Statement").

1 joint testimony supporting settlement, the Settling Parties, including Staff,
2 recommend that, in the event that the Commission orders further consideration
3 (beyond this Docket No. UE-110876) or adoption of electric decoupling or any other
4 similar mechanism, this should not occur until the Company's next general rate
5 case.² The Settling Parties reserved the right to advocate any position or to offer
6 recommendations regarding the rejection, adoption or implementation of electric
7 decoupling or other similar mechanisms in Avista's next general rate case or in any
8 future proceeding.³

9

10 **III. DISCUSSION OF NVEC'S DECOUPLING PROPOSAL**

11

12 **Q. Please generally describe NVEC's decoupling proposal.**

13 A. NVEC proposes a full decoupling mechanism for Avista's electric operations.
14 Avista's revenues would be based upon a revenue-per-customer ("RPC") value for
15 all electric customers, except the 22 customers Avista serves under Schedule 25,
16 Extra Large General Service.⁴

17 The NVEC proposal would guarantee Avista would recover that RPC
18 through a deferred accounting and true-up process. The true-ups of actual revenue to
19 the RPC level would occur annually, subject to a three percent rate increase cap.

² The Stipulation states that consideration of any ROE adjustment related to decoupling would be at issue with any decoupling proposal. See fn. 3 of Exhibit No. 1, Settlement Stipulation.

³ Exhibit No. 2, Joint Testimony at 16:13-19.

⁴ Schedules 1 (Residential), 11/12 (General), 21/22 (Large General), 31/32 (Pumping), 41-49 (Street and Area Lighting).

1 Avista would defer any amount above the cap and recover it in later annual rate
2 changes.

3 NWEC proposes that the mechanism run for at least five years, subject to a
4 future evaluation by an independent contractor. Finally, the proposed mechanism
5 requires annual reports by Avista describing its progress toward conservation
6 targets.⁵

7
8 **Q. Does Staff have any general concerns about implementing NWEC's decoupling
9 proposal for Avista?**

10 A. Yes, Staff has two general concerns. First, Avista alleges it is experiencing growth
11 in costs that are not reflected in rates.⁶ It is Staff's view that an attrition adjustment
12 is the best way to deal with this issue, including any lost revenues due to
13 conservation.⁷ Decoupling does not address attrition, as Mr. Cavanagh has conceded
14 in testimony he filed in the PSE rate case currently pending before this Commission.⁸

15 Second, the NWEC proposal fails to comply with the most significant
16 elements of the Decoupling Policy Statement, namely:

- 17
- 18 • It does not appropriately analyze the impact of conservation on Avista;
 - 19 • it is not appropriately applied to all customer classes;
 - 20 • it makes no reduction to cost of capital;
 - 21 • it fails to condition RPC recovery on achieving conservation targets;

⁵ The Commission requires Avista to file similar reports per Docket UE-100176;

⁶ Exhibit No. ___ (MTT-1T) at 9:12-15.

⁷ PSE Dockets UE-111048 & UG-111049, Elgin, Exhibit No. ___ (KLE-1T) at 80:5-9.

⁸ PSE Dockets UE-111048 & UG-111049, Cavanagh, Exhibit No. ___ (RCC-1T) at 10:14.

- 1 • it does not identify comparable conservation benefits for low income customers;
2 • it does not describe the incremental conservation the Company should pursue;
3 and
4 • it fails to net increased wholesale sales due to conservation in the true-up.

5 I explain each of these deficiencies in the following sections of my testimony.

6

7 **A. Response to Mr. Cavanagh’s “Fixed Cost Recovery” Analysis**

8

9 **Q. What is the main premise supporting Mr. Cavanagh’s decoupling testimony?**

10 **A.** Mr. Cavanagh’s main supporting premise is: “If Avista helped its customers save just
11 one percent of system-wide electricity use per year every year for the next five years,
12 it would automatically lose almost \$38 million in authorized fixed-cost recovery.”⁹

13

14 **Q. Is that testimony accurate?**

15 **A.** No. Mr. Cavanagh uses an extremely broad definition of “fixed costs” that includes
16 costs that are not “fixed”. As a result, Mr. Cavanagh’s \$38 million over five years is
17 a gross overstatement.

18 Mr. Cavanagh believes his definition of “fixed cost” is consistent with how
19 that term is used in a recent publication regarding decoupling by the Regulatory
20 Assistance Project (RAP), entitled *Revenue Regulation and Decoupling*

⁹ Cavanagh, Exhibit No. ___ (RCC-1T) at 2:12-15 and at 5:20 to 6:20.

1 (June 2011).¹⁰ In fact, that RAP publication did not define “fixed costs”. RAP was
2 addressing decoupling in the context of utilities with fuel adjustment mechanisms
3 that allow for full recovery of production costs. Therefore, RAP needed to
4 distinguish between costs that were covered by “fully reconciled” fuel adjustment
5 mechanisms and costs that were not. RAP uses the terms “production” and “non-
6 production” costs to make that distinction. This is demonstrated in RAP’s discussion
7 on pages 4-5 of its publication, which are in my Exhibit No. ___ (DJR-4).

8 In short, RAP was not trying to distinguish between “fixed” and “variable”
9 costs, as Mr. Cavanagh tries to do in his testimony.¹¹

10 In addition, and perhaps more important, Mr. Cavanagh’s proposed
11 decoupling mechanism includes in the RPC all of Avista’s investment-related costs
12 associated with power supply, including investment in generating facilities and
13 transmission. If full decoupling were in effect, and Avista experienced lower retail
14 sales due to conservation, Avista would be able to sell the unused power in the
15 wholesale market, thus recovering much or all of this cost twice: once through the
16 decoupling mechanism, and once from wholesale customers. Though Mr. Cavanagh

¹⁰ According to his testimony Exhibit No. ___ (RCC-1T) at 5:21 to 6:5, Mr. Cavanagh relies on the Company’s response to NWECC Data Request 2. In NWECC Data Request 2, which I have included as my Exhibit No. ___ (DJR-3), NWECC instructed Avista to use the following definition of “fixed costs”:

please define “fixed costs” as the company’s revenue requirement excluding production costs, which “are those that vary more or less directly with energy consumption in the short run”, including “fuel, purchased power”, and “transmission by others”.

According to those same NWECC data request instructions, these definitions are from: “Regulatory Assistance Project, *Revenue Regulation and Decoupling* (June 2011, p. 4).”

¹¹ The accounting definition of a “fixed cost” is a cost that remains unchanged despite changes in volume or other units of production.

1 correctly excluded these costs in his PSE decoupling proposal, he fails to do so in his
2 Avista proposal.¹²

3

4 **Q. Is Avista's fuel adjustment clause "fully reconciled," as RAP uses that term?**

5 A. No. Avista's Energy Recovery Mechanism (ERM) has a dead band and sharing
6 bands, which means, by definition, Avista does not fully recover all production costs
7 within the mechanism. This not only proves Mr. Cavanagh improperly has taken the
8 RAP publication out of context, but it also presents significant issues for full
9 decoupling. As I discuss in more detail later, NWECC's proposal fails to address
10 those issues.

11

12 **B. NWECC's Proposal is Not Applied to All Customer Classes**

13

14 **Q. How does the Decoupling Policy Statement address the application of full
15 decoupling to customer classes?**

16 A. The Commission states that a full decoupling mechanism should include all customer
17 classes, unless it would be lawful or consistent with "the public interest" to do
18 otherwise:

19 *Application to Customer Classes.* Generally, a full decoupling proposal
20 should cover all customer classes. However, where in the public interest and
21 not unlawfully discriminatory or preferential, the Commission will consider a
22 proposal that would apply to fewer than all customer classes.¹³
23

¹² In the current low natural gas price environment, Avista would probably not recover all of its power supply costs through wholesale sales.

¹³ Decoupling Policy Statement at 18, Criterion 1, ¶ 28.

1 **Q. Is the Commission's policy appropriate?**

2 A. Yes. The discrimination and preference statutes are part of the Commission's overall
3 regulation of utilities; although there may be circumstances where excluding a
4 customer class would satisfy those statutes and also be in the "public interest".
5

6 **Q. Does NWECC's proposed decoupling mechanism include all customers?**

7 A. No. NWECC's proposal exempts all 22 customers Avista serves under Schedule 25,
8 Extra Large General Service.¹⁴ Typically, these customers are very large industrial
9 customers.
10

11 **Q. What specific reasons does Mr. Cavanagh give for excluding customers served
12 under Schedule 25 from decoupling?**

13 A. Mr. Cavanagh exempts Schedule 25 customers on the basis that this schedule "has so
14 few members (22) and accounts for a relatively small fraction of the fixed cost
15 revenue requirement that Avista recovers through its energy sales (about 10%,
16 although the class accounts for almost 20% of retail electricity sales)."¹⁵
17

18 **Q. Are these specific reasons sufficient to exempt these customers from
19 decoupling?**

20 A. No, although I do not offer a legal opinion regarding the discrimination or undue
21 preference statutes. The number of customers in a rate schedule or their relative
22 portion of electricity sales are facts, not reasons. Schedule 25 customers participate

¹⁴ Cavanagh, Exhibit No. ___ (RCC-1T) at 10:3.

¹⁵ Cavanagh, Exhibit No. ___ (RCC-1T) at 10:3-6.

1 in Avista's conservation programs. The sample decoupling mechanism found in my
2 Exhibit No. ___ (DJR-2) included all customers.¹⁶

3 In sum, the Commission needs and deserves much more justification than
4 NWECA has supplied before exempting Schedule 25 customers.

5

6 **C. NWECA's Proposal Excludes the Impact of Decoupling on the Rate of Return**

7

8 **Q. What does the Decoupling Policy Statement say with respect to the impact of**
9 **full decoupling on a utility's cost of capital?**

10 **A.** The Commission contemplates full decoupling will reduce the utility's cost of
11 capital:

12 By reducing the risk of volatility of revenue based on customer usage, both
13 up and down, such a mechanism can serve to reduce risk to the company, and
14 therefore to investors, which in turn should benefit customers by reducing a
15 company's debt and equity costs. This reduction in costs would flow through
16 to ratepayers in the form of rates that would be lower than they otherwise
17 would be, as the rates would be set to reflect the assumption of more risk by
18 ratepayers.¹⁷

19

20 The Commission specifically requires a full decoupling mechanism proposal
21 to evaluate its impact on the return on equity:

22 *Impact on Rate of Return.* Evidence evaluating the impact of the proposal on
23 risk to investors and ratepayers and its effect on the utility's ROE.¹⁸

24

¹⁶ See Exhibit No. ___ (DJR-2), at 8 and 9, and Appendix 1 Workpapers, Electric, at 1c.

¹⁷ Decoupling Policy Statement at 16-17, ¶ 27.

¹⁸ Id. at 17, Element 2, ¶ 28.

1 **Q. Is this policy appropriate?**

2 A. Yes. Full decoupling changes the utility's revenue risk by guaranteeing a specific
3 amount of revenue per customer regardless of typical causes of fluctuation in
4 revenue related to weather, economic conditions, or any other condition. Reduced
5 revenue volatility should translate into lower capital costs, either as a lower required
6 return on equity or the need for less equity in the utility's capital structure.

7
8 **Q. Does NWEAC recognize any change to Avista's cost of capital due to full
9 decoupling?**

10 A. No. Apparently, Mr. Cavanagh believes full decoupling could actually *increase*
11 Avista's cost of equity, based on a study by the Brattle Group that found the cost of
12 equity to be higher for the decoupled gas utilities studied.¹⁹

13 In any event, Mr. Cavanagh concludes that the only possible cost of capital
14 benefit will be through a potential reduction in the utility's equity ratio, but, even
15 then, he proposes this capital structure benefit flow to ratepayers if and only if, and
16 only after, the utility actually decreases its equity ratio. He claims the Ratepayer
17 Assistance Project ("RAP") agrees with him on this timing issue.²⁰

18
19 **Q. Should the Commission wait to recognize any cost of capital benefit from
20 decoupling?**

¹⁹ Cavanagh, Exhibit No. ___ (RCC-1T) at 16:13-19.

²⁰ Id. at 17:1-3.

1 A. No. The Commission should reject Mr. Cavanagh's proposal as inconsistent with an
2 important element of the Decoupling Policy Statement: customers should receive the
3 benefits of the revenue risk reduction resulting from decoupling.

4 The Brattle Group study upon which Mr. Cavanagh relies did not attempt to
5 exclude any other variables that may have contributed to the higher cost of equity for
6 the studied utilities, such as market perceptions about the consistency of the
7 regulatory agencies that implement decoupling.²¹ Consequently, its conclusion about
8 higher cost of equity for decoupled gas utilities is suspect, and insufficient as
9 evidence on the appropriate cost of capital for Avista under a decoupling mechanism.

10

11 **Q. Did RAP agree, as Mr. Cavanagh states, that any capital structure benefits**
12 **should be passed through to customers, if and only if, and only when, the utility**
13 **actually achieves those improvements?**

14 A. No. Nowhere in its publication does RAP recommend regulators wait until actual
15 capital structure benefits materialize. In fact, RAP considers it appropriate to
16 recognize cost of capital improvements at the time full decoupling is put into place.

17 In particular, RAP estimates the equity ratio could be lower by three
18 percentage points due to risk-mitigation benefits of decoupling.²² RAP also
19 recognizes cost of capital benefits of full decoupling when it is implemented.²³

²¹ See Exhibit No. ___ (DJR-4) Regulatory Assistance Project, *Revenue Regulation and Decoupling: A Guide to Theory and Application* (June 2011), at 38, section 10.2. "If the risk mitigation measure is put in place only for a limited period, or the regulatory commission has a record of changing its regulatory principles frequently, the ratings agency may not recognize the measure."

²² Id. at 38, first paragraph.

²³ Id. at 39, first paragraph.

1 Though RAP suggests against lowering the cost of equity at the time a
2 decoupling mechanism is implemented, RAP also suggests that regulators may want
3 to lower the utility's equity ratio "when regulators consider how to flow through the
4 risk-mitigation benefits of decoupling to consumers when a mechanism is put into
5 place."²⁴ In other words, RAP agrees with the Decoupling Policy Statement that cost
6 of capital-related reductions may appropriately coincide with the adoption of a
7 decoupling mechanism.

8

9 **Q. Have other commissions lowered a utility's cost of capital when implementing a**
10 **decoupling mechanism?**

11 A. Yes, the Public Service Commission of Maryland, in its approval of a decoupling
12 mechanism for each of its three investor-owned utilities, reduced the return on equity
13 by 50 basis points. The District of Columbia Public Service Commission did the
14 same.²⁵

15

16 **Q. If the Commission approves a decoupling mechanism, how could the**
17 **Commission implement its cost of capital reduction policy?**

18 A. The Commission could reduce the overall rate of return by adopting a return on
19 equity in the lower end of a reasonable range, or by reducing the amount of equity in
20 the company's ratemaking capital structure, or both. However, while the Settlement
21 Stipulation the Commission approved in this docket identifies an agreed overall rate
22 of return, it does not identify a specific capital structure or specific cost rates.

²⁴ Id. at 39, last paragraph.

²⁵ Decoupling Policy Statement, Appendix 6, at 3.

1 Consequently, absent a fuller record on rate of return, the Commission will not be
2 able to apply its cost of capital reduction policy, should it decide to implement full
3 decoupling at this point in this case.

4

5 **D. NWEC's Proposal Does Not Condition Recovery on Conservation Achievement**

6

7 **Q. What is the Commission's policy regarding meeting conservation targets and**
8 **revenue per customer recovery by a utility under a decoupling mechanism?**

9 A. It is essential that the decoupled utility meet its conservation targets: "Revenue
10 recovery by the company under the mechanism will be conditioned upon a utility's
11 level of achievement with respect to its conservation target."²⁶ Later in the
12 Decoupling Policy Statement, in the discussion about direct conservation incentives,
13 the Commission explains further:

14 However, the EIA, in RCW 19.285.060(4), provides us with the express
15 authority to provide such incentives: "The commission ... may consider
16 providing positive incentives for an investor-owned utility to exceed the
17 targets established in RCW 19.285.040." We do not read this provision to
18 permit us to provide incentives to acquire conservation that is not cost-
19 effective. Rather, we read this to suggest that, between the biennial
20 conservation targets designed to determine what cost-effective conservation
21 can be required, the electric utility may be able to acquire additional
22 conservation as technology is improved, federal or other matching funds
23 become available, or for other reasons that were not known at the time of the
24 setting of the target.²⁷
25

²⁶ Id. at 17, Description of Mechanism, ¶ 28.

²⁷ Id. at 20, ¶ 31, 32.

1 **Q. Can this policy be practically applied?**

2 A. Yes. On page 14 of my Exhibit No. ___ (DJR-2), Staff's response to the
3 Commission's Bench Request in Docket UE-111048 and UG-111049, Staff
4 identified a Conservation Test that would implement this policy. That test could
5 apply to Avista as well.

6

7 **Q. Does NWECC's proposal condition Avista's revenue recovery under decoupling**
8 **with achieving the Company's conservation targets?**

9 A. No.

10

11 **E. NWECC's Proposal Does Not Identify Comparable Conservation Benefits to**
12 **Low-Income Customers**

13

14 **Q. What is the Commission's policy on conservation for low income customers in**
15 **the context of full decoupling?**

16 A. The Commission's policy is:

17 *Low-income.* A utility proposing a full decoupling mechanism must
18 demonstrate whether or not its conservation programs provide benefits to
19 low-income ratepayers that are roughly comparable to other ratepayers and, if
20 not, it must provide low-income ratepayers targeted programs aimed at
21 achieving a level of conservation comparable to that achieved by other
22 ratepayers, so long as such programs are feasible within cost-effectiveness
23 standards.²⁸

24

25

²⁸ Id. at 19, Criterion 4, ¶ 28.

1 **Q. Does NWEC's proposal satisfy this Commission policy?**

2 A. No. In response to Staff Data Request 12, NWEC states that "Mr. Cavanagh has not
3 conducted such an analysis."
4

5 **Q. Did Staff independently determine whether Avista's conservation programs
6 provide benefits to low-income ratepayers that are roughly comparable to other
7 ratepayers?**

8 A. No. Staff does not have the information available to conduct such analysis.
9

10 **F. NWEC's Proposal Does Not Describe Incremental Conservation**
11

12 **Q. What is the Commission's policy regarding a utility's acquisition of more
13 conservation than it would have acquired absent decoupling?**

14 A. The Commission requires a decoupling proposal to contain: "Evidence describing
15 any incremental conservation the company intends to pursue in conjunction with the
16 mechanism".²⁹
17

18 **Q. Does Mr. Cavanagh address this policy?**

19 A. No. The only specific levels of conservation Mr. Cavanagh refers to are
20 conservation targets that are in place for Avista today, absent decoupling.³⁰
21

²⁹ Id. at 19, Criterion 3, ¶ 28.

³⁰ Cavanagh, Exhibit No. ___ (RCC-1T) at 7:1-13.

1 **G. NWEC's Proposal Does Not Account for the Net Benefits of Off-System Sales**
2 **and Costs Avoided Due to the Utility's Conservation Efforts**
3

4 **Q. What is the Commission's policy on increased wholesale sales as a result of**
5 **decoupling?**

6 A. The Commission requires a full decoupling mechanism to account for certain off-
7 system sales and avoided costs, and to net the benefits as part of the true-up:

8 *Accounting for Off-System Sales and Avoided Costs.* A description of the
9 method the company intends to use to determine the financial benefits
10 associated with off-system sales or avoided costs attributable to the utility's
11 conservation efforts and then to net these benefits against the true-up
12 provided in this mechanism.³¹
13

14 In the related footnote, the Commission explains:

15
16 In principle, for every megawatt hour saved through the operation of the
17 utility's conservation program, it has the opportunity to either sell the same in
18 the appropriate market (off-system sales), or avoid having to purchase or
19 produce electricity to meet its load requirements. The accounting of this
20 form of found revenue differs between electric utilities with power cost
21 adjustment mechanisms and those without. After rates have been set for an
22 electric utility that does not have a power cost adjustment mechanism, the
23 marginal avoided cost of producing or buying electricity, or the marginal
24 revenue (net of marginal cost) from the sale of electricity made surplus by
25 conservation not incorporated into the calculation of the power costs, is a
26 direct benefit to the utility shareholders. For utilities with a power cost
27 adjustment mechanism, loads are projected in a future test year, with
28 reductions in the load for the expected conservation levels. Consequently, for
29 the effective rate year following the setting of rates, only conservation above
30 the expected level of conservation would result in an opportunity to reduce
31 power costs or realize additional revenues from incremental sales. In the
32 years after the projected rate year, the marginal avoided cost of producing or
33 buying electricity, or the marginal revenue (net of marginal cost) from a sale
34 of electricity made surplus by conservation, is a direct benefit.³²
35

³¹ Decoupling Policy Statement at 17, Element 4, ¶ 28.

³² Id. at n. 45.

1 **Q. Is this Commission policy appropriate?**

2 A. Yes. When customers conserve energy, the utility should market the electricity the
3 utility would have sold to its own retail customers. Moreover, the utility incurs
4 lower costs due to the wholesale sales, such as reduced line losses, reduced
5 uncollectible expense, and avoidance of the Public Utility Tax, which effectively
6 applies only to retail sales.

7 Under full decoupling, ratepayers guarantee the utility's recovery of a
8 specified level of revenues per customer. It is appropriate for the decoupling
9 mechanism to recognize the benefits of enhanced wholesale sales that may result
10 from decoupling.

11

12 **Q. Can this policy be practically applied?**

13 A. Yes, but not within the decoupling mechanism itself. Rather, this policy could be
14 implemented by revising the ERM. One possible revision could be to eliminate the
15 dead band from the ERM.³³ However, doing that would also eliminate a key feature
16 of the ERM: to provide rate stability to consumers except under extreme
17 circumstances, while giving the Company a very strong incentive to manage power
18 supply costs to avoid such extreme circumstances. Needless to say, addressing this
19 policy will require more detailed analysis than has been presented thus far.

20

³³ In the absence of an energy cost adjustment clause, this part of the decoupling policy would be very difficult and administratively burdensome to apply.

1 **Q. Does NWECA's proposal apply this Commission policy?**

2 A. No. Mr. Cavanagh suggests the Commission ignore this policy on the basis of his
3 belief that Avista's ERM "already responds to this concern" regarding enhanced
4 wholesale sales.³⁴ In short, Mr. Cavanagh chooses to not apply the Commission's
5 decoupling policy on wholesale sales, without adequately supporting that choice.

6

7 **Q. Is Mr. Cavanagh's characterization of Avista's ERM correct?**

8 A. No. Because Avista's ERM has a "dead band" and "sharing bands", the practical
9 result under full decoupling is that ratepayers would not receive the full benefit of
10 incremental wholesale sales occasioned by any reductions in retail sales. This is
11 because any revenues from such wholesale sales likely would fall within the dead
12 band and, therefore, Avista would retain the benefits.³⁵

13

14 **Q. Is it consistent with the Decoupling Policy Statement to allow decoupling while
15 also maintaining Avista's current ERM?**

16 A. No. The current structure of the ERM and the Commission's decoupling policy on
17 enhanced wholesale sales are not compatible. If the Commission wishes to
18 implement full decoupling for Avista, there are two choices: change the ERM, or do
19 not apply the Commission's decoupling policy on wholesale sales.

20

³⁴ Cavanagh, Exhibit No. ___ (RCC-1T) at 12:7-13.

³⁵ Exhibit No. ___ (DJR-2), at 18.

1 **Q. What choice should the Commission make and why?**

2 A. Should the Commission choose to implement full decoupling for Avista, it should
3 maintain its policy regarding wholesale sales. However, Staff believes the
4 Commission does not have a sufficient record in this docket to both address full
5 decoupling and appropriately revise the ERM. Therefore, any decision to adopt full
6 decoupling should await full examination of any required revisions to the ERM.

7

8

IV. CONCLUSION

9

10 **Q. Please summarize your position on the full decoupling proposal offered by**
11 **NWEC.**

12 A. The Commission should reject in its entirety NWEC's full decoupling proposal as
13 inconsistent with the several elements I have identified from the Commission's
14 Decoupling Policy Statement.

15

16 **Q. Should the Commission nevertheless decide to implement full decoupling at this**
17 **time, what issues should be addressed prior to implementation?**

18 A. The Commission should:

- 19 • Require additional evidence quantifying the change in the overall rate of return
20 occasioned by the specific decoupling mechanism adopted by the Commission,
21 or the amount of equity in the ratemaking capital structure the Commission
22 deems appropriate, or both.

- 1 • Adopt the Earnings Test as outlined in Exhibit No. ___ (DJR-2), modifying the
2 Earnings Test dead band as appropriate.³⁶
- 3 • Adopt the Conservation Test as outlined in Exhibit No. ___ (DJR-2).³⁷
- 4 • Require third party evaluation of conservation achievement, which will also
5 identify any incremental conservation.
- 6 • Require third party evaluation of comparable benefits for low-income customers.
- 7 • Require revision of the ERM.

8

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

10 **A. Yes.**

11

12

³⁶ Exhibit No. ___ (DJR-2) includes an earnings test for discussion purposes that was essentially the same as that addressed by Mr. Cavanagh. It is also very similar to the earnings test in Avista's gas decoupling mechanism, although Avista's gas mechanism does not contemplate the 25 basis point dead band. I would clarify, however, that whatever dead band is chosen by the Commission, it should be based on a rate of return set in the general rate case that implements decoupling. In addition, the dead band should be carefully crafted to provide upside earnings only if the Company can demonstrate a connection between achieved efficiencies beyond those required by statute and its earnings at the high end of any range determined to be fair.

³⁷ Exhibit No. ___ (DJR-2), at 13-14, and Appendix 1 Workpapers, Electric, at 1b.

Exhibit No. ___ (DJR-3T)
Docket UE-111048/UG-111049
Witness: Deborah J. Reynolds

BEFORE THE WASHINGTON UTILITIES AND TRANSPORTATION COMMISSION

**WASHINGTON UTILITIES AND
TRANSPORTATION COMMISSION,**

Complainant,

v.

PUGET SOUND ENERGY, Inc.

Respondent.

**DOCKET UE-111048
DOCKET UG-111049**

(Consolidated)

CROSS-ANSWERING TESTIMONY OF

Deborah J. Reynolds

**STAFF OF
WASHINGTON UTILITIES AND
TRANSPORTATION COMMISSION**

Responding to the Decoupling Proposal of the NW Energy Coalition

January 17, 2012



1 only after, the utility actually decreases its equity ratio. He claims the Ratepayer
2 Assistance Project (“RAP”) agrees with him on this timing issue.¹⁶

3
4 **Q. Should the Commission agree that PSE’s cost of equity likely will be higher**
5 **under full decoupling and that it should wait for any capital structure benefits**
6 **to actually occur, before recognizing any cost of capital benefit from**
7 **decoupling?**

8 A. No. The Commission should reject Mr. Cavanagh’s proposal as inconsistent with an
9 important element of the Decoupling Policy Statement: customers should receive the
10 benefits of the risk reduction resulting from decoupling.

11 Moreover, the Brattle Group study upon which Mr. Cavanagh relies did not
12 attempt to exclude any other variables that may have contributed to the higher cost of
13 equity for the studied utilities, such as market perceptions about the consistency of
14 the regulatory agencies that implement decoupling.¹⁷ Consequently, its conclusion
15 about higher cost of equity for decoupled gas utilities is suspect.

16 In addition, the financial impact of full decoupling on the utility’s revenues is
17 immediate, and the utility should capitalize itself properly due to this important
18 change to its operations. Waiting only causes ratepayers to pay for risks twice: first,
19 by having those risks shifted to ratepayers from investors, and again, by keeping the
20 capital structure the same as if the utility was subject to those risks.

¹⁶ Id. at 20:12-17.

¹⁷ See Regulatory Assistance Project, Revenue Regulation and Decoupling: A Guide to Theory and Application (June 2011), at 38, section 10.2. “If the risk mitigation measure is put in place only for a limited period, or the regulatory commission has a record of changing its regulatory principles frequently, the ratings agency may not recognize the measure.”