BEFORE THE WASHINGTON
UTILITIES AND TRANSPORTATION COMMISSION

WASHINGTON UTILITIES AND TRANSPORTATION COMMISSION, Complainant, v. PUGET SOUND ENERGY, INC. Respondent.	DOCKETS UE-240004 & UG-240005 (CONSOLIDATED)

REPLY BRIEF OF PUBLIC COUNSEL

December 4, 2024

Shaded Information is Designated as Confidential per WAC 480-07-160

TABLE OF CONTENTS

TABLE OF AUTHORITIES

ATTORNEY GENERAL OF WASHINGTON
PUBLIC COUNSEL
800 5TH AVE., SUITE 2000
SEATTLE, WA 98104-3188
(206) 464-7744

Other Jurisdictions

Books & Reports

LIST OF TABLES

I. INTRODUCTION

1. Puget Sound Energy (PSE or the Company) requests substantial rate increases for both its electric and natural gas services. If PSE's request is granted, electric customers will see a rate increase of $477.4 million, and natural gas customers will see a rate increase of $221.4 million.

2. Customers will be heavily impacted by rate increases in their day-to-day lives. Over 300 customers wrote in opposition to the proposed increases. They expressed that the increases are disproportionate to inflation and cost of living increases. For example, Social Security payments increased by only 3 percent this year.[1] Customers were also concerned over the lack of transparency regarding how PSE justifies its adjustments and the allocation of funds. They urge the Washington Utilities and Transportation Commission (Commission) to consider how much of the rate increase will contribute to executive salaries, dividends, profits, and other expenses that do not directly benefit the consumer.

3. Roger T., a Washington senior, lamented his prohibitively high energy costs. Combined with rising rent and medication expenses, "[i]t won't be long before I will have to make choices, food, medications, [or] housing."[2] Many residents, including seniors and others on a fixed income, described the same predicament, pointing out the impossibility of absorbing large rate increases. Leslie N. wrote, "[h]ow do you expect household budgets to also absorb a double digit energy price increase when average salary and Social Security increases are in the low single digits[?]"[3] Nancy B., an 80-year-old widow, was "very concerned" about rate increases due to

---

[1] Jeffrey Buckner, *Social Security benefits increase in 2024*, Social Security Administration. https://blog.ssa.gov/social-security-benefits-increase-in-2024/ (Dec. 12, 2024).
[2] Public Counsel Bench Response No. 1 at 32 (Public Comment Exhibit) (filed Nov. 12, 2024).
[3] *Id*. at 16

her fixed income that affords her a spot just outside the window for assistance.[4] And Barbara S., a 72-year-old who only heats her home to a chilly 60 degrees due to cost, hopelessly declared that "[p]erhaps this world would be better off if all of us seniors just froze to death[…] It certainly is pointing us in that direction."[5]

4. The Commission has an obligation to prioritize equity and energy justice, ensuring affordable energy access for all residents, especially low-income customers. To that end, the Washington Attorney General's office Public Counsel Unit (Public Counsel) recommends approving a lower return on equity (ROE) and a capital structure with a lower equity percentage than what PSE requests. Public Counsel also recommends adjustments to PSE's revenue requirement, including limiting storm expense normalization, rejecting increases in incentive compensation, and modifying downward Operations and Maintenance (O&M) expense forecasts. Public Counsel further challenges PSE's claims of financial instability and asserts that PSE's current credit ratings demonstrate adequate financial health and the ability to attract capital.

II. STANDARD OF REVIEW

5. The Commission is charged with regulating investor-owned utilities like PSE and must regulate in the public interest.[6] Rates must be fair, just, reasonable, and sufficient, and the Commission is authorized to set rates after hearing by order.[7] The Commission has defined fair, just, reasonable, and sufficient to mean:

> <u>[F]air</u> to customers and to the Company's owners; <u>just</u> in the sense of being based solely on the record developed in the proceeding following principles of due

[4] *Id*. at 23.
[5] *Id*. at 24.
[6] RCW 80.01.040(3).
[7] RCW 80.28.020.

> process of law, reasonable in light of the range of possible outcomes supported by the evidence, and sufficient to meet the needs of the Company to cover its expenses and attract necessary capital on reasonable terms.[8]

The Commission's findings must be based on evidence in the record.[9]

6. In assessing the public interest, the Commission foregrounds the issue of equity and energy justice. In 2021, when the Legislature authorized multiyear rate plans, it directed that the Commission determine whether rates were in the public interest.[10] Following the Legislative directive, the Commission acknowledged that its definition of public interest included "equity considerations."[11] The Commission determined to "apply an equity lens in all public interest considerations going forward."[12] Integral to equity in ratemaking, the Commission explained, was the concept of "energy justice and its core tenets" which included whether "individuals have access to energy that is affordable, safe, sustainable, and affords them the ability to sustain a decent lifestyle."[13]

7. The legislative and regulatory focus on equity concerns naturally directs attention to a utility's low-income customers. The Legislature specifically identified its concern with the "energy burden of low-income residential customers" and provided that for any increase in rates, the Commission "must approve an increase in the amount of low-income bill assistance."[14] In tying rate increases to corresponding increases in low-income assistance, the Legislature

---

[8] *Wash. Utils. & Transp. Comm'n v. Puget Sound Energy, Inc.*, Dockets UE-090704 and UG-090705 (*consol.*), Order 11, ¶ 18 (Apr. 2, 2010) (emphasis added).
[9] RCW 34.05.461(4).
[10] RCW 80.28.425(1).
[11] *Wash. Utils. & Transp. Comm'n v. Cascade Nat. Gas Corp.*, Docket UG-210755, Order 09: Final Order ¶¶ 52–58 (Aug. 23, 2022) (hereinafter *Cascade Final Order*).
[12] *Id.* ¶ 58.
[13] *Id.* ¶ 56.
[14] RCW 80.28.425(2).

emphasized the necessary balancing of ratepayer interests with those of PSE's shareholders. What is "fair to customers and utility shareholders"[15] must consider how rate increases will impact low-income customers.

8. The Commission's task requires it to balance consumer and investor interests.[16] This does not, however, mean that the Commission determines what is best for investors; to the contrary, the Commission considers what is necessary such that "the regulated utilities earn enough to remain in business."[17] This includes a rate of return sufficient to maintain credit and financial integrity while assuring PSE is financially motivated to provide fair prices and service to customers.[18] Thus, while a higher rate of return or upward adjustments to a revenue requirement might be beneficial to PSE's bottom line, it is only a relevant consideration if it is necessary to maintain PSE's financial integrity.

9. As with all requests for increased rates, PSE bears the burden to prove the requested rates are fair, just, reasonable, and sufficient.[19] This includes both the burden of production and the burden of persuasion, and requires PSE to demonstrate a revenue deficiency in the rate effective years following both the "known and measurable" and "used and useful" standards.[20] The Commission has long held that this requires a utility to make an affirmative showing of the reasonableness and prudence of its costs, even in the absence of a challenge.[21]

---

[15] *Puget Sound Energy*, Docket UE-090704 & UG-090705, Order 11, ¶ 18.
[16] *U.S. West Commc'ns, Inc. v. Wash. Utils. & Transp. Comm'n*, 134 Wn.2d 74, 121 (1997).
[17] *Id*. at 121.
[18] *Id.* at 121.
[19] RCW 80.04.130(4).
[20] *Cascade Final Order* ¶ 108.
[21] *Wash. Utils. & Transp. Comm'n v. Puget Sound Power & Light Co.*, Dockets UE-920499 & UE-921262 Eleventh Suppl. Order, at 19 (Sept. 21, 1993).

10. As a necessary corollary to this general principle, this means that the Commission should hold any failure to produce evidence on a topic or gaps in the evidentiary record against PSE. The intervening parties and Utilities and Transportation Staff (Staff) bear no burden of proof to disprove the need for a rate increase. If, when questioned, PSE chooses not to answer or admits that it did not produce evidence or analysis, that is a sufficient reason to reject a requested rate increase. Thus, for example, it is not enough to assert that PSE might face a ratings downgrade. Conjecturing that there might be an adverse impact is insufficient as a matter of law; to meet its burden, PSE must prove that the adverse consequence will happen absent the specifically requested rate increase.

III. CAPITAL STRUCTURE

11. Public Counsel witness Dr. J. Randall Woolridge testified that ROE of 9.375 percent and a capital structure with 49 percent equity would be reasonable and appropriate.[22] Increasing PSE's authorized ROE above the current level is unsupported by the evidence.[23] Public Counsel recommends that the Commission reject PSE's terms and adopt Public Counsel's recommendation on cost of capital and capital structure.

A. Equity in PSE's capital structure should be 49 percent.

12. Capital structure consists of the mix of debt and equity that a utility has used to fund its operations. Debt and equity have different costs, so funding decisions made by a utility have a substantial impact on customer rates and investor returns.[24] A capital structure weighted too

[22] Response Testimony of J. Randall Woolridge, Exh JRW-1T at 109:6–21.
[23] *Id.* at 109:22–23 & 110:1.
[24] *Wash. Utils. & Transp. Comm'n v. Puget Sound Energy*, Dockets UE 111048 & UG-111049, Order 08 ¶ 35 (May 7, 2012).

strongly towards equity can result in unreasonably high costs for the ratepayer. On the other hand, a capital structure weighted too strongly towards debt can jeopardize the utility's access to capital markets and financial viability.[25]

13. The Commission judges a utility capital structure on how it balances economy and safety. "Safety" refers to the idea that a capital structure with more equity and less debt may result in higher overall costs and higher rates for customers but has enhanced financial integrity. "Economy" refers to the idea that a capital structure with more debt and less equity may result in lower overall costs and lower rates for customers.[26] The Commission must "strike an appropriate balance between debt and equity on the bases of economy and safety."[27] A capital structure used for ratemaking purposes should present an optimal mix of equity and debt to balance capital costs with financial risk.[28] The Commission requires the capital structure of privately held utilities, such as PSE, to appropriately balance debt and equity.[29] If a capital structure is too heavily capitalized with equity, the costs are unfair to ratepayers, creating an unfair burden.[30]

14. In this case, PSE initially requested a capital structure of 50.0 percent equity for year one and 51.0 percent equity for year two. Public Counsel witness Dr. Woolridge determined an appropriate capital structure for PSE's rates should have 49 percent equity. He considered the average common equity ratios for the Electric, Bulkley, and Gas Proxy Groups. The Electric Proxy Group consisted of 24 publicly held electric utilities. The Bulkley Proxy Group, developed

[25] *Pioneer Natural Res. USE, Inc. v. Pub. Util. Comm'n of Texas*, 303 S.W.3d 363, 373 (Tex. App. 2009).
[26] *Puget Sound Energy*, Dockets UE 111048 & UG-111049, Order 08 ¶ 35.
[27] *Wash. Utils. & Transp. Comm'n v. Puget Sound Energy*, Dockets UE-220066, UG -220067, & UG-210918 (*consol.*) Final Order 24/10. ¶ 123 (Dec. 22, 2022).
[28] *In re Zia Natural Gas Co.,* 128 N.M. 728, 731, 998 P.2d 564, 567 (2000).
[29] *Puget Sound Energy*, Dockets UE 111048 & UG-111049, Order 08 ¶ 35.
[30] *Wash. Utils. & Transp. Comm'n v. PacifiCorp,* Docket UE-130043, Order 05, ¶¶ 41–42 (Dec. 4, 2013).

by PSE witness Anne Bulkley, consisted of 20 gas and electric utility companies. The Gas Proxy Group consisted of eight natural gas distribution companies.[31] As of December 31, 2023, each proxy group had average common equity ratios significantly lower than PSE's proposed 50.0 percent for rate year one and 51.0 percent for rate year two. The Electric Proxy Group had an average common equity ratio of 40.9 percent. The Bulkley Proxy Group had an average common equity ratio of 42.3 percent. The Gas Proxy Group had an average common equity ratio of 43.2 percent.[32]

15. PSE has not demonstrated that increasing PSE's equity share would produce fair, just, and reasonable rates. Public Counsel recommends that the Commission maintain PSE's current authorized capital structure with a common equity ratio of 49.0 percent. Dr. Woolridge testified that a capital structure with 49.0 percent is:

> (1) consistent with the Company's historic capitalization, which PSE has used to finance its operations and maintained its credit ratings; (2) consistent with the Commission past policies on utility capitalizations; and (3) more reflective of the capital structures of proxy groups of electric, combination electric and gas, and gas distribution companies.[33]

16. Staff Witness David Parcell illustrates PSE's recent capitalization in Exhibit DCP-6.[34] Both PSE and its parent company, Puget Holdings, maintained stable equity ratios over the last five years.[35] PSE has been able to reasonably finance its operations during this time period.

[31] Woolridge, Exh. JRW-1T at 28:1–20 & 29:1–20.
[32] *Id*. at 31:17–19.
[33] *Id*. at 32:8–12.
[34] *See also* Testimony of David Parcell, Exh. DCP-1T at 25:2–12. Staff witness Parcell testified that PSE's capitalization should be set at 48.5 percent equity. Parcell, Exh. DCP-1T at 29:8–18.
[35] *Id*. at 25:8–9.

Moreover, PSE has maintained positive credit ratings that are as good as or better than the three proxy group companies.[36]

17. Public Counsel's recommended capital structure is in line with the Commission's policy of weighing safety and economy. In PSE's 2022 rate case, the Commission authorized 49.0 percent common equity.[37] In the three rate cases preceding 2022, the Commission authorized PSE's capital structure with 48.5 percent equity.[38]

18. PSE's proposed equity ratios of 50 and 51 percent are above the average of the proxy groups, meaning that the proposed capital structure includes more equity and less financial risk, but higher cost, than the proxy groups.[39] While Public Counsel's recommended capitalization for ratemaking purposes is also higher than the proxy groups' average common equity ratio, it is closer to the proxy groups than PSE's proposal. Because our recommendation is consistent with PSE's actual capitalization and how the Commission has balanced safety and economy, Public Counsel does not recommend reducing equity in PSE's capital structure for ratemaking purposes.

19. Conversely, increasing PSE's common equity ratio to 50 and 51 percent, respectively, results in a capital structure that is tilted too heavily towards safety at the expense of ratepayers. Additionally, the current regulatory environment is viewed as "more favorable," which suggests that a reduction in equity ratio is warranted, if any change is required.[40]

---

[36] *See* Woolridge, Exh. JRW-1T at 12:21–22.
[37] *Puget Sound Energy*. Dockets UE-220066, UG -220067, & UG-210918 (*consol*.) Final Order 24/10. ¶¶ 119–128.
[38] Dockets UE-17033/UE-170034; Dockets UE-180899/UG-180900; Dockets UE-190529/UG-190530. *See* Direct Testimony of David C. Parcell, Exh. DCP-19, *Wash. Utils. & Transp. Comm'n v. Puget Sound Energy,* Docket UE-220066, UG-220067 & UG-210918 (*consol.*) (filed July 28, 2022).
[39] Woolridge, Exh. JRW-1T at 31:21–23.
[40] Parcell, Exh. DCP-1T at 28:7–14.

B. PSE's Requested Return on Equity is Excessive and Should Be Rejected

20. Return on equity is the allowed rate of profit for a regulated company.[41] Regulators must provide regulated utilities with the opportunity to earn a fair return within the guiding principles established in two seminal United States Supreme Court cases, *Hope*[42] and *Bluefield*.[43] Through these cases, the United States Supreme Court recognized that rates for regulated monopoly utilities must incorporate a fair rate of return on equity that is comparable to returns investors would expect to receive on other investments of similar risk, sufficient to assure confidence in the utility's financial integrity, and adequate to maintain and support the company's credit and to attract capital at reasonable costs.[44] To set a utility's return on equity, the Commission must determine the market-based cost of capital.[45] Economic models used by cost of capital experts seek to use market-based information to set an appropriate return on equity for regulated utilities. Examples of such models are the Discounted Cash Flow (DCF) Model and Capital Asset Pricing model (CAPM).

21. Cost of capital, both debt and equity, are determined in part by economic and financial conditions.[46] Over the past decade, authorized returns on equity for electric and gas utilities declined nationally.[47] Despite market volatility during this time-period,[48] utility ROEs continued to be higher than the market-based cost of capital. Dr. Woolridge analyzed utility market-to-book

---

[41] Woolridge Exh. JRW-1T at 3:6–7.
[42] *Federal Power Comm'n v. Hope Natural Gas Co.,* 320 U.S. 591, 64 S. Ct. 281 (1944).
[43] *Bluefield Waterworks & Improvement v. Public Service Comm'n of West Virginia,* 262 U.S. 679, 43 S. Ct. 675 (1923).
[44] Woolridge, Exh. JRW-1T at 3:15–21.
[45] *Id*. at 4:1–2.
[46] Parcell, Exh. DCP-1T at 8:20–21.
[47] Woolridge, Exh. JRW-1T at 25:17–20 & 26:1–5; Parcell, Exh. DCP-1T at 11:8–9 & 12:1–12.
[48] *Id*. at 13:8–20:18.

ratios, which illustrates the relationship between earned ROE and actual cost of equity.[49] A ratio of 1.0X indicates that a company is selling common stock at book value.[50]

22. Over the past five years, the average earned electric ROE has been between 9.0 and 10.0 percent. The average market-to-book ratio increased for electric utilities, peaking at 2.0X in 2019, declined to the 1.75X range between 2020 and 2022, and declined to 1.50X in 2023.[51] The market-to-book ratios indicate that utilities have been selling stock over book value.

23. Comparing authorized ROEs with 30-year treasury yield, authorized ROEs did not decline or adjust to the same extent. Washington authorized ROEs did not decrease as much as Treasury yields declined.[52] Washington authorized ROEs did not decrease below 9.4 percent through 2021 and increased to 9.54 percent by 2022.[53]

24. Cost of capital is an opportunity cost and is prospective looking. As a result, cost of capital must be estimated.[54] To set an appropriate ROE, the Commission must determine the market-based cost of capital for the utility. The market-based cost of capital represents the return investors could expect from other investments of similar risk.[55] Expert witnesses and regulators rely on economic models and formulas that use market data of firms with similar risk to estimate and set a regulated utility's ROE.[56] Dr. Woolridge presents the DCF Model and the CAPM, both of which are rigorously tested and frequently relied upon to estimate the market-based cost of

---

[49] *Id*. at 11:20–22 & 34:10–35:1–5; Woolridge, Exh. JRW-4 at 3, Panel A.
[50] *Id.* at 11:21–22 & 34:10–12.
[51] *Id.* at 13:20–22; Woolridge, Exh. JRW-4 at 3.
[52] *Id*. at 22:7–14, Table 4.
[53] *Id*. at 22:7–16, Table 4.
[54] Parcell, Exh. DCP-1T at 8:9–10.
[55] Woolridge, Exh. JRW-1T at 4:2–4.
[56] *Id.* at 4:4–9.

capital. Indeed, the Commission has assigned greater weight to DCF results relative to other models.[57]

25. PSE proposes an ROE of 9.95 percent in year one of the Multi Year Rate Plan (MYRP) and 10.50 percent for year two.[58] Public Counsel argues that PSE's authorized ROE should be considerably lower and recommends that the Commission authorize a more reasonable 9.375 percent ROE. Dr. Woolridge concluded that the market-based cost of equity for PSE is between 9.0 and 9.75 percent.[59]

26. He bases this range on the results of his DCF and CAPM analysis of the three proxy groups. The CAPM results ranged from 8.25 to 8.30 percent. The DCF results ranged from 8.75 to 8.90 percent.[60] Dr. Woolridge gave primary weight to the DCF results, consistent with the Commission's reliance on DCF analysis results.[61] As a result, Dr. Woolridge testified that he recommends an equity cost of 9.375 percent for PSE.[62] Dr. Woolridge's complete cost of capital analysis results in the following recommendation:

Table 1: Public Counsel's Rate of Return Recommendation[63]

Capital Source	Capitalization Ratios	Cost Rate	Weighted Cost Rate
Short-Term Debt	1.55%	4.575%	0.07%
Long-Term Debt	49.45%	4.698%	2.32%

[57] *Wash. Utils. & Transp. Comm'n v. Avista Corp.*, Dockets UE-200900, UG-200901, & UE-200894 (*consol.*), Order 08/05. ¶ 103 (Sept. 27, 2021).
[58] Woolridge, Exh. JRW-1T at 4:19–23 & 5:2.
[59] *Id.* at 6:16–17 & 109:17–18.
[60] *Id*. at 73:19–74:1, Table 10.
[61] *Id*. at 74:3; *Avista Corp.*., Dockets UE-200900, UG-200901, & UE-200894 (*consol*.), Order 08/05 ¶ 3 (quoting James C. Bonbright, *et al., Principles of Public Utility Rates*, 317-18 (Pub. Utils. Reps. 2nd Ed. 1988)).
[62] Woolridge, Exh. JRW-1T at 74:6–7.
[63] *Id.* at 7:4, Table 2.

Common Equity	49.00%	9.375%	4.59%
Total	100%		6.99%

27. PSE's proposed ROE is overly generous to shareholders, and it takes no steps to move towards a fairer result. The proposal would result in ratepayers bearing higher rates than necessary or fair because of the excessive ROE. Approving Public Counsel's recommendations would result in fairer rates for customers.

C. Impact of Public Counsel's Cost of Capital and Capital Structure Recommendation Reduces the PSE's Proposed Revenue Requirement for Electric and Natural Gas Service

28. Public Counsel's recommendation reduces the ROE and equity in PSE's capital structure from PSE's proposal. To implement Public Counsel's recommendation, the revenue requirements must be reduced. Considering only the base rates and not the costs placed in trackers or otherwise removed from base rates, the following tables show the revenue impact of Public Counsel's recommendations. Further adjustments may be needed for costs removed from rates.

Table 2 Impact of Public Counsel ROR Recommendation (Electric)[64]

#	Electric	2025	2026
1	Company's Proposed Rate Base	$6,606,402,752	$7,416,985,017
2	Public Counsel Rate of Return	9.375	9.375
3	Impact of Change to Cost of Capital – Change to ROE Only	($25,060,458)	($56,764,177)
4	Revenue Conversion Factor	0.751313	0.751313

[64] *See* Greg R. Meyer, Exh. GRM-3C (Electric Revenue Requirement Tabs 2 (ROR 2025) and 3 (ROR 2026)).

5	Impact of Change to Cost of Capital – Changing Cap Structure and ROE	($5,160,199)	($11,711,371)
6	Total Impact of Changes with 49% common equity	**($30,220,657)**	**($68,475,547)**

Table 3 Impact of Public Counsel ROR Recommendation (Gas)[65]

#	Electric	2025	2026
1	Company's Proposed Rate Base	$2,866,503,993	$2,863,128,296
2	Public Counsel Rate of Return	9.375	9.375
3	Impact of Change to Cost of Capital – Change to ROE Only	($10,831,869)	($21,828,035)
4	Revenue Conversion Factor	0.754213	0.754213
5	Impact of Change to Cost of Capital – Changing Cap Structure and ROE	($2,224,879)	($4,493,570)
6	Total Impact of Changes with 49% common equity	**($13,056,748)**	**($26,321,605)**

IV. REVENUE REQUIREMENT ADJUSTMENTS

29. Public Counsel requests that the Commission make several downward revenue adjustments to PSE's revenue requirement. The Commission should limit PSE's storm expense normalization adjustment to the six-year average storm costs. The Commission should reject PSE's proposed increases to short and long-term incentive compensation. The Commission should reject PSE's proposed O&M adjustments related to its use of a two-year escalation factor for non-labor and labor expenses. The Commission should also approve Public Counsel's adjustments to PSE's administrative and general (A&G) non-labor forecast. The Commission should adjust two of PSE's proposed amortizations related to depreciation and carrying charges

[65] *See* Meyer, Exh. GRM-4C (Gas Revenue Requirement Tabs 3 (ROR 2025) and 4 (ROR 2026)).

from its revenue requirement and adjust PSE's proposed Advanced Metering Infrastructure (AMI) plant recovery. A full list of the revenue adjustments appears in the response testimony of Public Counsel's witness Greg R. Meyer.[66] All of these proposed adjustments are appropriate.

1. The Commission Should Limit PSE's Storm Expense Normalization Adjustment to Six-Year Average Storm Costs

30. PSE proposed an increase to PSE's normalized storm expense from $8,978,655 to the $10 million threshold.[67] Public Counsel witness Meyer states that the proposed $1,021,345 revenue increase is unsupported as the $10 million threshold exceeds PSE's six-year average storm costs and PSE has not demonstrated a need to increase costs above the six-year average.[68] Limiting PSE's storm expense normalization adjustment to six-year average storm costs would lower PSE's electric revenue requirement by $1,021,345.[69]

2. The Commission Should Reject PSE's Proposed Increases to Short and Long-Term Incentive Compensation

31. In this case, PSE included $8.9 million in short-term incentives and associated payroll tax for its electric revenue requirement and approximately $3.3 million for its gas revenue requirement.[70] While the Commission approved a similar plan in PSE's 2019 case, the Commission should reconsider its position in the current case.[71] These incentive payments are based on financial performance and are notably not tied to service quality, reliability, or public and employee safety. Therefore, these payments are inappropriate to include in cost of service

---

[66] Meyer, Exhs. GRM-2 & GRM-3.
[67] Direct Testimony of Susan E. Free, Exh. SEF-1T at 86:14–16.
[68] Direct Testimony of Greg R. Meyer, Exh. GRM-1CT at 8:1–5.
[69] *Id.* at 8:5–7.
[70] *See* Free, Exh. SEF-6 at 11 & Exh. SEF-11 at 11.
[71] Meyer, Exh. GRM-1CT at 15:9–14.

because they benefit PSE shareholders rather than ratepayers.[72] Public Counsel recommends that the Commission reduce expenses associated with PSE's short-term incentive compensation plan by 50 percent. This results in a reduction of approximately $4.5 million for PSE's electric revenue requirement and approximately $1.7 million for PSE's gas revenue requirement.[73]

32. PSE proposed an increase to its electric and gas cost of service to recover 10 percent of PSE's Long-Term Incentive Plan (LTIP) expenses for executive compensation.[74] [redacted].[75] As with PSE's short-term incentive plan, LTIP is primarily an incentive plan designed to align the interests of executives with shareholders.[76] PSE has historically excluded LTIP expenses from its cost of service since Docket UE-090704, where the Commission found these costs should not be paid for by customers.[77]

33. PSE's proposed LTIP recovery in this case is based on a new set of performance goals derived from goals specified by the Clean Energy Transformation Act (CETA). PSE has asserted that customers should fund the 10 percent of LTIP tied to environmental goals because achievement of these goals benefits customers.[78] The primary means by which PSE executives will achieve the environmental goals is by increasing rate base. It is inappropriate to ask customers to pay for incentive compensation that increases earnings for shareholders as PSE

Shaded Information is Designated as Confidential per WAC 480-07-160

[72] *Id.* at 15:17–20 & 16:1–2.
[73] *Id.* at 18:6–11.
[74] *Id.* at 8:11–13.
[75] Meyer, Exh. GRM-5C at 2 (PSE's Response to Public Counsel Data Request No. 87, Confidential Attachment A).
[76] Meyer, Exh. GRM-1CT at 11:1–2.
[77] Free, Exh. SEF-1T at 82.
[78] Direct Testimony of Thomas M. Hunt, Exh. TMH-1T at 20:9–11.

expands its rate base.[79] Additionally, because achievement of the environmental goals is uncertain, the true costs of PSE's long-term incentives are not known and measurable, which means they should be excluded from ratemaking cost of service.[80]

34. Public Counsel recommends that the Commission exclude 100 percent of PSE's proposed LTIP adjustments for both electric and natural gas. Disallowing 100 percent of PSE's LTIP costs would lower PSE's electric revenue requirement by $563,097 in Rate Year 1 and by an additional $19,708 in Rate Year 2, for a total reduction of $582,805. Public Counsel's proposed LTIP adjustment would also lower PSE's gas revenue requirement by $403,759 in Rate Year 1 and by an additional $14,132 in Rate Year 2, for a total reduction of $417,890.[81]

3. The Commission should reject PSE's proposed Operations and Maintenance (O&M) Adjustments Related to Its Use of a Two-Year Escalation Factor.

35. PSE forecasted its O&M expenses based on approved levels in its Board of Directors' plan. PSE's forecast relied heavily on escalation factors, including inflation. Public Counsel believes that PSE's use of a two-year compounding escalation factor is inappropriate for both non-labor and labor costs. For non-labor costs, it is unreasonable for PSE to include two years of O&M inflation in the first year of its multi-year rate plan (MYRP) when PSE has demonstrated its ability to manage these costs. For labor costs, PSE misapplies the wage inflation escalator to capture costs with currently unfilled positions.[82]

36. Public Counsel recommends that the Commission limit PSE's non-labor O&M cost increases for the first year of the MYRP to one year of inflation. PSE held its overall non-labor

---

[79] Meyer, Exh. GRM-1CT at 11:15–18.
[80] *Id.* at 12:9–11.
[81] *Id.* at 13:12–17.
[82] *Id.* at 24:9–14.

2024 O&M costs at 2023 levels by offsetting cost increases in some areas with cost decreases in others.[83] PSE stated that its non-labor O&M costs in 2024 were expected to be $1.3 million lower than 2023.[84] Applying two years' worth of inflation to its 2024 costs to forecast non-labor O&M for 2025 is inconsistent with PSE's approach to its forecasting approach for 2026 costs– PSE only escalates 2025 costs by one year of inflation.[85]

37. Public Counsel proposes using a one-year inflation rate of 0.78 percent, as developed by witness Meyer by averaging the 2024 and 2025 inflation rates used by PSE and using PSE's same escalator methodology.[86] Public Counsels' adjustments lower PSE's non-labor O&M costs by $2,361,000 for 2025, with a reduction of $1,997,000 to electric non-labor O&M and a reduction of $363,000 to gas non-labor O&M.[87] Although Public Counsel did not alter PSE's inflation rates PSE used to escalate 2025 non-labor costs, Public Counsel's revised 2025 costs resulted in a small incremental adjustment to the forecasted 2026 non-labor O&M expenses.[88]

38. Turning to PSE's labor forecast, Public Counsel believes that the 7.83 percent inflation rate PSE applied between 2024 and 2025 is excessive because PSE did not limit its use of the escalation factor to capture wage increases but also included hiring considerations.[89] PSE's forecasted labor expense is based on an unknown number of employees, which are neither known nor measurable and should therefore be excluded from the test year labor expense.[90] In

[83] *Id* at 24:3–5.
[84] Meyer, Exh. GRM-7 at subpart d (PSE's response to Public Counsel Data Request 216).
[85] Meyer, Exh. GRM-1CT at 2
[86] *Id.* at 26:2–8.
[87] *Id.* at 26:8–12.
[88] *Id.* at 26:13–16, & 22 Table (Native format of this Table can be found in Exhibit GRM-4C).
[89] *Id.* at 26:19–22 & 27:1–2.
[90] *Id.* at 27:9–11.

discovery, PSE stated that it does not use employee headcount or Full-Time Equivalents (FTE) in its forecasting process.[91] PSE's forecast includes unfilled positions with no known hire date which would lead PSE to over-recover its actual labor expense.

39. PSE used a two-year compounding escalation factor to calculate a single year of labor costs by assuming any budgeted O&M expenses exceeding salary increases for existing employees would be used to hire new employees. PSE's 7.83 escalation factor combined 2024 and 2025 wage rate inflation rates. Public Counsel believes a wage inflation rate should not be used to forecast increases in labor costs driven by new hires. Additionally, PSE has failed to account for employee attrition in its forecast. If PSE assumes it will only add employees in 2025, then PSE has overstated its forecasted labor costs by failing to account for labor cost decreases due to employee attrition.

40. Public Counsel proposes a revised labor expense forecast applied only to existing employees. Removing unfilled positions from PSE's 7.83 percent labor escalator lowers PSE's O&M costs in 2025 by approximately $9,841,000 with a reduction to electric labor of approximately $4,191,000 and a reduction to gas of approximately $5,650,000.[92] Public Counsel proposes using the same 3.25 wage escalator used by PSE to escalate 2025 costs to 2026, however, witness Meyer's revised 2025 expense forecast results in an approximate $320,000 incremental decrease to PSE's 2026 expenses.[93]

---

[91] Meyer, Exh. GRM-8 (PSE's Response to Public Counsel Data Request 92).
[92] Meyer, Exh. GRM-1CT at 29:5–10.
[93] *See* Meyer, Exhs. GRM-3C & GRM-4C.

4. The Commission Should Approve Public Counsel's Adjustments to PSE's Proposed A&G Non-Labor Forecast Expenses.

41. PSE forecasted significant increases in A&G salaries over historical expenses for 2025 and 2026 for both its electric and natural gas operations. Although Public Counsel requested an explanation for the substantial growth in expenses not attributed to inflation, PSE gave no reason for the increases in its response.[94] Public Counsel witness Meyer outlined these increases in his testimony.[95] As explained by witness Meyer, typically, most expenses associated with this account are related to labor charges. While the account does contain labor expenses, the non-labor expenses remain unexplained and unjustified by PSE.

42. For its electric operations, Public Counsel proposes reducing PSE's forecasted A&G expenses to the highest level experienced over the past three years. This adjustment results in an annual expense level of $19,321,840 (2023 actual level) for 2025 and 2026 expenses. This adjustment lowers the electric revenue requirement in 2025 to $61,964,568 and to $55,479,465 in 2026.[96]

43. For gas operations, Public Counsel proposes limiting the 2026 expense to $9,673,648, projected for 2025. This adjustment does not change the 2025 rate year. This adjustment results in a reduction of $8,522,257 for 2026.[97]

5. The Commission Should Adjust PSE's Proposed Amortizations related to Depreciation, Carrying Charges, and AMI Plant Recovery.

44. PSE improperly included a full year of two amortizations, one for depreciation and one

---

[94] *See,* Meyer, Exh. GRM-11.
[95] Meyer, Exh. GRM-1CT at 31 Table GRM-5.
[96] *Id.* at 31:11–12 & 32:1–5.
[97] *Id.* at 32:6–8.

for carrying charges, set to expire in January 2026 in its revenue requirement. By including the full year of these amortizations, PSE overstated its 2026 revenue requirement. PSE requested recovery of $2,787,552 for a depreciation amortization and a recovery of $116,817 for a carrying charge amortization.[98] The calculated expense is based off of a twelve-month period instead of only month of expense. Public Counsel proposes a reduction to the annual level of amortization expense to reflect the termination of said expenses on January 15, 2026. This reduction would apply only to the electric cost of service and would reduce PSE's electric amortization expense by approximately $2.8 million.[99]

45. In 2016, PSE installed AMI meters to replace outdated Automated Meter Reading (AMR) meters.[100] PSE was not allowed to include both debt and equity returns on these investments in their rates.[101] In the previous 2022 rate case, PSE was permitted to begin recovering the debt return on its AMI investment but was ordered to defer the equity return.[102] In this rate case, PSE requested amortizing both the equity and debt returns previously deferred over a three-year period.[103]

46. Public Counsel recommends that if the Commission approves PSE's request to recover deferred equity and debt returns, that it set the amortization period at six years. Public Counsel believes that the six-year period is more consistent with the period over which the deferred returns accumulated, and is therefore, more appropriate. Using a six-year amortization period

---

98 *Id.* at 19:4–5.
99 *Id.* at 19:12–15.
100 Direct Testimony of Roque B. Bamba, Exh. RBB-1T at 15:7–8.
101 *Wash. Utils. & Transp. Comm'n v. Puget Sound Energy, Inc.*, Dockets UE-190529 & UG-190530 et al., Final Order 08/05/03 ¶ 153 (July 8, 2020).
102 *Id.*
103 Free, Exh. SEF-1T at 74:15–18.

reduces PSE's electric cost of service by approximately $4.8 million and its gas cost of service by approximately $2.4 million.[104]

V. FINANCIAL INTEGRITY

47. PSE Witness Daniel Doyle notes that PSE must make significant capital investments over the next three to five years to achieve the clean energy requirements outlined in CETA.[105] He states these investments require PSE to access external capital funding at a level that cannot be accomplished without a stronger financial profile.[106] He specifically requests cost of service that will result in additional cash flow to PSE, which he recommends achieving through a higher authorized return on equity, a higher equity ratio in its ratemaking capital structure, the inclusion of Construction Work in Progress (CWIP) in rate base (as opposed to accruing an Allowance for Funds Used During Construction (AFUDC), and recognition of PSE's ability to earn a return on PPAs.[107]

48. Yet, Doyle ignores the need to manage rate affordability. Managing rate affordability is not only fair and reasonable, but the utility has an obligation to prioritize rate affordability in managing its capital expenditures and operating expenses budgets to maintain safe and reliable service, all of which are critical factors in managing the utility's financial integrity and credit standing.[108] Public Counsel's expert, Michael Gorman, states that managing rate affordability stabilizes revenue and promotes operational efficiency; affordable rates stabilize revenue by

---

[104] Meyer, Exh. GRM-1CT at 20:10–19.
[105] Direct Testimony of Daniel A. Doyle, Exh. DAD-1CT at 26:11–23.
[106] *Id*.
[107] *Id*.
[108] Direct Testimony of Michael P. Gorman, Exh. MPG-1CT at 6:3–7.

enabling customers to more easily afford to pay their utility bills on time and in full; and predictable revenue streams allow for more stable and predictable strong amounts of internal cash generation, enhanced financial planning and greater ability to make timely debt service payments.[109] In turn, these factors support the financial integrity of the Company.

49. From this standpoint, the Commission should carefully weigh the impact on customers' rates against the proposed changes in regulatory mechanisms which erode customers' tariff rate protections. The implementation of regulatory mechanisms that increase customer bills to support stronger cash flows and earnings that PSE alleges are needed to support improved credit ratings metrics and financial integrity is unsupported by the evidence. Further, in discussing the enhanced regulatory mechanisms proposed by PSE, the Company fails to acknowledge the importance of preserving customer rate-setting protections and managing rate affordability as a continuing and critical planning factor that must also be reflected in its compliance with the CETA and wildfire risk mitigation planning.

A. PSE is Financially Stable

50. All credit rating agencies' outlooks for PSE's bond rating are "Stable," and agencies make positive comments about the implementation of a multiyear rate plan to support PSE's ability to recover its cost of service. As part of S&P's "Stable" BBB credit rating outlook for PSE, it states:

> The stable outlook on PSE reflects that of parent [Puget Energy] and 9 our expectation that ratemaking under the WUTC, including the 10 multiyear rate plan, will reduce regulatory lag and cash flow 11 volatility. Under our base case, we expect [Puget Energy]'s FFO to 12 debt will be 13%-14% through 2026.[110]

[109] *Id*. at 6:7–13.
[110] S&P Global Ratings: *Puget Sound Energy Inc.*, at 2 (May 16, 2024).

51. In reaching this position, S&P reviewed PSE's significant increase in capital spending necessary to comply with CETA, and its elevated wildfire risk requiring more proactive management of wildfire risk, including monitoring for wildfire risk events and responding to the improved wildfire risk mitigation operating procedures.[111]

52. Moody's also has a "Stable" Baa1 credit rating outlook for PSE, stating:

> Puget Sound Energy, Inc's (PSE) credit profile is supported by its rate regulated utility operations that benefit from a number of credit supportive cost recovery mechanisms authorized by its primary regulator, the Washington Utilities and Transportation Commission (WUTC). PSE's credit quality continues to be constrained by high holding company debt at its parent, Puget Energy, Inc. (Puget, Baa3 25 stable).
>
> PSE's 2022 general rate case (filed January 2022) concluded in a multiparty settlement for a two year rate plan. In early January 2023, the WUTC approved the settlement with new rates effective in January 2023. We view the conclusion of the 2022 general rate case as credit positive and indicates that Washington regulation has become more consistent following the state's passage of SB 5116 and SB 5295 in 2019 and 2021, respectively.
>
> As of the last twelve months ending June 2023, PSE's credit metrics improved including a ratio of cash flow from operations before changes in working capital (CFO pre-WC) to debt to about 19% from 16% at the end of 2022. The improvement is driven by stronger cash flow generation primarily because of the new rates as well as collection of the purchase power and fuel costs that were deferred in 2022. We expect credit metrics to be sustained between 18% and 20% over the next two years.[112]

53. Likewise, Fitch Ratings also has a "Stable" BBB+" credit rating outlook for both PSE and "BBB" for its parent Puget Energy Inc. Commenting on the "Stable" credit outlook for PSE, Fitch notes a positive regulatory environment suggesting regulatory treatment of PSE can

---

[111] *Id*.
[112] Direct Testimony of Cara G. Peterman, Exh. CGP-9 at 20 (Moody's Investor service, Credit opinion, Puget Sound Energy, Inc. Sept. 15, 2023).

support improvement to its current corporate bond rating.[113] Fitch Ratings states,

> Puget Energy Inc.'s (PE) ratings are driven by the regulated gas and electric utility operations at subsidiary Puget Sound Energy, Inc. (PSE). PSE is regulated by the Washington Utilities and Transportation Commission (WUTC).
>
> The approval of PSE's first multiyear rate plan has resulted in improved credit metrics for PE and PSE. Nonetheless, Fitch considers the WUTC to have a mixed record of credit-supportive decisions. Additionally, Washington is one of the most progressive states and imposes stringent environmental regulations and aggressive renewable and social objectives that, without appropriate recovery mechanism, can negatively affect credit.[114]

54. As demonstrated by these "Stable" ratings, ratings agencies have sufficient confidence in the Company and PSE can attract capital at reasonable rates.

B. Rate Affordability is Critical to Support Credit Ratings and Financial Integrity.

55. Customer affordability is not just a peripheral concern for utilities, but a fundamental strategic imperative that directly impacts long-term sustainability. Customer affordability is not a charitable consideration but an essential objective with legal, economic, and social ramifications.

56. Credit rating agencies have been emphasizing rate affordability, maintaining adequate financial coverages of debt obligations, and supporting utilities' overall investment grade bond ratings. In a recent industry report, Moody's Investors Service (Moody's) explained that the regulated electric and gas utilities' outlook remains "Negative" largely due to increased pricing pressures on customers. Moody's stated that it changed its outlook from "Positive" to "Negative" due to the following:

> We have revised our outlook on the US regulated utilities sector to negative from stable. We changed the outlook because of increasingly challenging business and financial conditions stemming from higher natural gas prices, inflation and rising interest rates. <u>These developments raise residential customer affordability issues,</u>

[113] *Id*. at 1.
[114] *Id*.

increasing the level of uncertainty with regard to the timely recovery of costs for fuel and purchased power, as well as for rate cases more broadly.[115]

57. Fitch similarly notes bill affordability concerns for ratepayers, and regulators' ability to balance the rate requests with increasing customer bills.[116]

C. Including CWIP in Rate Base Before the Resource is Placed in Service Causes Intergenerational Equity Problems

58. Mr. Gorman testified that including CWIP in rate base will create economic harm to the customers that are obligated to pay a current return on CWIP in rate base but will not receive any benefits from the operating output that commences after the unit is placed in-service.[117] Specifically, customers obligated to pay a return on the Beaver Creek wind facility CWIP will not benefit by the reduced energy charges via the operation of the wind facility energy output and accredited capacity benefits and will not receive any benefits from production tax credits (PTC) available based on that energy generation after the resource is placed in-service.[118]

59. The proposed inclusion of CWIP in the rate base represents a fundamentally unjust financial mechanism that imposes immediate economic burdens on ratepayers while denying them corresponding benefits. By requiring customers to finance the Beaver Creek wind facility's construction through current rate payments, yet precluding them from receiving the future economic advantages—including reduced energy charges, capacity benefits, and production tax credits—the approach constitutes a clear regulatory inequity. This arrangement effectively transfers the financial risk and investment costs to current ratepayers without providing them any

[115] Moody's Investors Service Outlook, *Regulated Electric and Gas Utilities – U.S. 2023 outlook negative due to higher natural gas prices, inflation and rising interest rates*, at 1 (Nov. 10, 2022) (emphasis added).
[116] Fitch Ratings, *North American Utilities, Power & Gas Outlook 2024* at 1 (Dec. 6, 2023).
[117] Gorman, Exh. MPG-1CT at 20:3–10.
[118] *Id*.

compensatory value, thereby creating an asymmetrical and potentially predatory financial structure that undermines principles of fair utility cost allocation.

D. The Traditional AFUDC Approach is More Appropriate.

60. AFUDC allows the Company to capitalize financing costs during construction, spreading them over the asset's useful life rather than immediately burdening ratepayers. This approach also more precisely reflects the true cost of financing capital projects by calculating the weighted average cost of debt and equity. It prevents current customers from paying full returns on assets not yet generating revenue, ensuring more equitable cost allocation. By smoothing out financing costs, AFUDC reduces immediate rate pressures and supports more stable long-term pricing strategies.

61. Operation of a wind facility like Beaver Creek produces energy at no fuel cost, producing a zero-cost component.[119] Further, Production Tax Credits (PTC) are available based on energy produced and further reduce the costs of the utility's energy during operation of the renewable resource.[120] Hence, while customers pay slightly higher rates to compensate the Company for construction period AFUDC charges, they receive significant benefits from the operation of the renewable resource after it is placed in-service. In contrast, customers that would be asked to pay a current return on CWIP balance of the renewable resource pay higher rates to compensate the Company for these construction period carrying charges but receive none of these energy benefits from the resource.

62. Mr. Gorman further testified that under traditional AFUDC treatment of CWIP carrying

---

[119] *Id*. at 20:11–16.
[120] *Id*.

costs, customers will pay slightly higher rates after Beaver Creek is placed in-service due to the capitalization of AFUDC carrying costs, but those same customers will benefit through lower energy charges produced by both operation of zero-cost fuel sources and by the PTCs for qualifying energy generation.[121] There are slightly higher costs under traditional ratemaking practices to capitalize AFUDC, but these costs are balanced by the operating benefits of the resource. These are critical elements in assessing the balance between paying the Company a current return on CWIP investment versus the traditional practice of allowing the utility to accrue an AFUDC return on that investment.

63. Mr. Gorman's testimony reveals a critical economic inequity in the proposed rate base treatment. By requiring current customers to finance Beaver Creek's construction through CWIP without corresponding benefits, the proposal creates a fundamentally unfair financial burden. Customers will be compelled to pay returns on an investment from which they will derive no immediate economic advantage—neither through reduced energy charges, accredited capacity benefits, nor production tax credits. This approach represents a clear violation of rate-making principles of equity and prudence, effectively transferring financial risk to ratepayers who receive no corresponding value. The proposed mechanism unjustly socializes the financial risk while privatizing potential future benefits, a stance that cannot be justified under sound regulatory principles. Accruing AFUDC during construction is the traditional, widely accepted ratemaking practice.

[121] Gorman, Exh. MPG-1CT at 21:4–8.

E. The Commission Should Not Approve a Return on Power Purchase Agreement

64. The Commission should reject PSE's proposal to earn a return on Power Purchase Agreements (PPAs) as unjustified and unreasonable. Offering a return on PPAs provides no direct cost benefit and increases the cost of PPA agreements to customers.[122] Moreover, PSE also seeks a higher common equity ratio in its ratemaking capital structure, in addition to requesting a return on PPAs. Permitting both a higher equity ratio and an equity return on PPAs would result in a double charging of customers to raise the utility's cash flow coverage of total leveraged debt higher than necessary.[123] PSE has failed to provide sufficient evidence to support the need for an increased common equity ratio to manage its overall leverage risk.[124] The financial leverage associated with PPAs is already accounted for in PSE's current capital structure.[125] If the Commission chooses to provide a return on PPAs, Public Counsel recommends a rate of return no higher than the utility's cost of debt.[126]

VI. DEPRECIATION

65. With respect to depreciation, the Commission should adjust PSE's proposed annual accrual downward by $70 million to account for PSE's failure to meet the burden of proof that its proposed depreciation rates are not excessive and that its predicted useful lives underlying its proposals are reasonable. PSE proposed an increase in its annual depreciation accrual of $71 million on plant balances as of the depreciation study date – December 31, 2022.[127] This

---

[122] *See* Public Counsel's Bench Response No. 3 at 2 (filed Nov. 22, 2024).
[123] *Id.*
[124] Gorman, Exh. MPG-1CT at 25:14–16.
[125] *Id.* at 26:11–13, Public Counsel Response to BR-3 at 2.
[126] *Id.* at 26:6-7.
[127] Response Testimony David J. Garrett, Exh. DJG-1T at 3:6–8.

represents a 42 percent increase from the current accrual.[128] Public Counsel witness David Garrett proposed depreciation rates that reduced PSE's proposed depreciation accrual by approximately $70 million, which still results in a slight increase, $485,983, from the current depreciation accrual.[129]

A. Public Counsel's Depreciation System Conforms to Appropriate Regulatory Standards

66. In *Lindheimer v. Illinois Bell Telephone Co.*, the U.S. Supreme Court defined depreciation as "the loss, not restored by maintenance, which is due to all the factors causing the ultimate retirement of the property. These factors embrace wear and tear, decay, inadequacy, and obsolescence."[130] In the same case, the Court also recognized that the original cost of plant assets, rather than present value, or some other measure, is the proper basis for calculating depreciation expense.[131] Most importantly, in *Lindheimer*, the Court found:

> [T]he company has the burden of making a convincing showing that the amounts it has charged to operating expenses for depreciation have not been excessive. That burden is not sustained by proof that its general accounting system has been correct. The calculations are mathematical, but the predictions underlying them are essentially matters of opinion.[132]

---

[128] *See* Garrett, Exh. DJG-3 (Summary Rate and Accrual Adjustment).
[129] *See* Garrett, Exh. DJG-1T at 3:14–16 & 4:1–2, Figure 1.
[130] *Lindheimer v. Illinois Bell Tel. Co.*, 292 U.S. 151, 167, 54 S. Ct. 658, 78 L. Ed. 1182 (1934).
[131] *Id.* at 168 (Referring to the straight-line method, the *Lindheimer* Court stated that "[a]ccording to the principle of this accounting practice, the loss is computed upon the actual cost of the property as entered upon the books, less the expected salvage, and the amount charged each year is one year's pro rata share of the total amount."). The original cost standard was reaffirmed by the Court in *Fed. Power Comm'n v. Hope Nat. Gas Co.*, 320 U.S. 591, 606, 64 S. Ct. 281, 88 L. Ed. 333 (1944). The *Hope* Court stated: "Moreover, this Court recognized in [*Lindheimer*], *supra*, the propriety of basing annual depreciation on cost. By such a procedure the utility is made whole, and the integrity of its investment maintained. No more is required." *Id.*
[132] *Lindheimer*, 292 U.S. at 169.

67. PSE fails to meet the burden of proof that its proposed depreciation rates are not excessive and that its predicted useful lives underlying its proposals are reasonable.

68. While the legal standards cited above do not require a specific procedure for conducting depreciation analysis, they do direct analysts to use a system for estimating depreciation rates that will result in the systematic and rational allocation of capital recovery for the utility.[133] In this case, Public Counsel witness Garrett employed a depreciation system that combined the straight line method, the average life procedure, the remaining life technique, and the broad group model to analyze PSE's actuarial data.[134] Witness Garrett's system conforms to regulatory standards and is commonly employed by depreciation analysts in regulatory proceedings.[135]

B. PSE's Proposed Depreciation Rates are Excessive and its Predicted Average Service Lives Are Unreasonably Short and Should be Rejected.

VII. PSE'S PROPOSED AVERAGE SERVICE LIVES, AS PRESENTED BY WITNESS ALLIS, ARE TOO SHORT AND RESULT IN EXCESSIVE DEPRECIATION RATES

69. Public Counsel correctly lengthened PSE's average service lives for seven of its distribution plants, resulting in lower depreciation rates.[136] PSE's estimated service lives differ significantly from PSE's observed historical data, while witness Garrett chose an Iowa curve that fits better mathematically and visually to the observed historical retirement pattern derived from PSE's plant data.[137] Witness Garrett's more objective curve fitting results in estimates that are more consistent with the historical service life patterns observed in PSE's accounts.[138] The

[133] *See* Garrett, Exh. DJG-1T at 6:11–13 & 7:1.
[134] *Id*. at 7:6–9.
[135] *Id*. at 7:9–12.
[136] *Id*. at 4:9–14, Figure 2.
[137] *Id*. at 11:7–11.
[138] *Id*. at 11:13–15.

Commission should reject PSE's proposed depreciation rates as excessive and its proposed average service lives as unreasonable Power Costs.

70. With respect to power costs, the Commission should adjust costs downward by $3,562,650 to account for PSE's failure to meet its burden to prove the cost of capacity in the Sinclair Power Purchase Agreement (PPA) was reasonable. In terms of process, The Commission should reserve final prudence review of power cost to Gener Rate Cases (GRC). Finally, the Commission should reject Staff's proposal to include Climate Commitment Act (CCA) allowance cost estimates in actual power costs in annual power cost proceedings or in net power cost forecasts.

A. The Commission Should Reduce PSE's Forecast Power Costs by $3,562,650

71. In this general rate case, PSE is requesting prudence review of three PPAs, the HF Sinclair PSR Cogen Agreement, the Chelan Slice 38 Agreement, and Colville Slice Agreement Extension.[139] As with all requested rate increases, PSE bears the burden of prove that these PPAs are fair, just, reasonable, and sufficient.[140] The Commission has long held that this requires the utility to make an affirmative showing of the reasonableness and prudence of its costs, even in the absence of challenge.[141] In evaluating power acquisitions, the Commission applies a reasonableness standard based on what the Board and Company should have known at the time of the decision.[142] PSE must prove that there is a need for the resource, that it filled that need in a

---

[139] Prefiled Direct Testimony of Philip Haines, Exh. PAH-1CT at 28:7–36:17 (Sinclair); 36:18–43:9 (Chelan Slice); 50:6–57:15.
[140] RCW 80.04.130(4).
[141] *Puget Sound Power and Light Co.*, Dockets UE-920499 & UE-921262 Eleventh Suppl. Order, at 19 (Sept. 21, 1993).
[142] *Puget Sound Energy, Inc.*, Dockets UE-111048 & UG-111049 (*consol.*), Order 08 ¶ 408, (May 7, 2012).

cost effective manner, that it evaluated alternatives, involved the Board in the decision process, and that it kept adequate documentation.[143]

72. Public Counsel witness Dr. Robert Earle has accurately pointed out that two of these PPAs, HF Sinclair and Chelan Slice 38 have unexplained and inconsistent valuation for capacity/resource adequacy.[144] The HF Sinclair PPA values capacity at [redacted] while the Chelan Slice 38 PPA values capacity at [redacted].[145] Despite a huge difference in capacity valuation, [redacted], PSE and its Board approved these contracts at the same time without providing any contemporaneous explanation for the inconsistency.[146]

73. In rebuttal, PSE's post-hoc explanation for the disparity is inadequate. In conclusory fashion, PSE witness Philip Haines notes that HF Sinclair is a cogeneration plant and Chelan Slice 38 a hydro facility with different profiles.[147] Other than noting that they are not the same plant, Witness Haines offers no explanation for why the capacity valuation is so disparate. Such a banal observation is not dispositive. As Dr. Earle testified in the hearing, if anything one should expect that capacity valuation for a hydro facility would be higher than a gas generation plant.[148] On its own, PSE's failure to provide an explanation is a failure to carry their burden of proof, particularly where this disparity was not caught at the time. A reasonable Board or company management must seek clear explanations for this kind of disparity in valuation of PPAs.

Shaded Information is Designated as Confidential per WAC 480-07-160

[143] *Id.* ¶ 409
[144] Response Testimony of Robert Earle, Exh. RLE-1CT at 6:3–9.
[145] *Id* at 6:6–7.
[146] *Id*. at 6, fn.6 (noting Sinclair closed in March 2023 at the same time the PSE submitted is successful Chelan bid).
[147] Rebuttal Testimony of Philip Haines, Exh PAH-19CT at 7:3–5.
[148] Earle, TR. at 303:21–25.

74. PSE's supposed expertise is further called into question by their misuse of the WRAP CONE comparator from the Western Resource Adequacy Program for a new-entry.[149] This might be an independent source for value, but as Dr. Earle notes, it is not actually a valuation metric.[150] Moreover, even if it were a valuation, PSE would have to use the Net CONE value or the capacity valuation would be too high.[151] In the end, PSE's sole justification is "PSE knows best." Where, as here, there are inconstancies in PSE's own valuation, that bald assertion is insufficient for prudence.

75. PSE attempts, instead, to hide behind its methodology. The Commission should find, however, that PSE's methodology is an insufficient justification for capacity valuation where two contracts entered at the same time have such a disparity in valuation. As Dr. Earle explained, PSE primary valuation process is self-referential and circular; capacity is valued at what PSE values it.[152] This problem is heightened because PSE bids are bundled, making precise comparisons of capacity value fuzzy.[153] Far from disputing this, PSE argues that its valuation is based on PSE's "expertise and experience"[154] and "market acumen"[155] in bilateral trades. In short, PSE admits its valuation is self-referential to its own bids, but the Commission should just trust PSE's assertion. But expertise that is unable to explain itself when challenged would not meet PSE's burden of proof in an ordinary setting. Where that "expertise" produces two contracts with one value that is [redacted] it is inexcusable. PSE's burden requires a

Shaded Information is Designated as Confidential per WAC 480-07-160

149 Earle, Exh. RLE-1CT at 4:4–7.
150 *Id*. at 4:7–11.
151 *Id*. at 4:12–18.
152 *Id*. at 3:9–11.
153 *Id*. at 3:11–4:3.
154 Haines, Exh. PAH-19CT at 4:16.
155 *Id*. at 4:19.

fulsome explanation before the Commission can credit the higher valuation.

76. PSE does not answer this critique, but instead asserts Dr. Earle's "cavils" over the only four examples PSE offers as comparators should be dismissed because PSE used its expert valuation methodology.[156] But Dr. Earle did not choose the four poor comparators, and if there are in fact, more "data points in PSE's comprehensive valuation methodology," then where are those other data points?[157] If PSE has the keys to unlock the explanation about why two simultaneous contracts have such divergent values, the fault fort their failure to provide more data lies with PSE, not the Commission or Public Counsel.

77. PSE does not do itself any favors by badly misstating the 2022 general rate case order as a justification for its failure. Witness Haines correctly quotes that order that the settling parties agreed to the prudency of the resources described in the 2022 case.[158] Initially, this order does not expressly endorse PSE's methodology, and it is dubious to rely on a settlement to denote agreement to something that could have litigated. But in an egregious omission, Witness Haines failed to include the last statement of the paragraph, "We find that the record adequately supports the Settling Parties agreement but *emphasize that our approval of these terms is not precedential*."[159] Witness Haines attempt to rely on this order as precedential is in bad faith and should be rejected.

78. Unfortunately, it is part of the pattern of conduct that makes PSE's attempt to shift prudency determinations out of general rate cases, discussed more below, problematic. PSE uses

---

[156] *Id.* at 7:14–8:5.
[157] Haines, Exh. PAH-19CT at 7:14–15.
[158] *Id*. at 3:15–17, citing *Puget Sound Energy, Inc.,* Dockets UE-220066, UG-220067, & UG-210918 (*consol.*), Final Order 24/10 ¶ 258.
[159] *Puget Sound Energy, Inc.,* Dockets UE-220066, UG-220067, & UG-210918 (*consol.*), Final Order 24/10 ¶ 258.

a lack of objections in prior matters as a sword and shield in subsequent proceedings. But PSE's burden to prove prudence applies even in the absence of a challenge.[160] The fact that Dr. Earle noticed a flaw in PSE's methodology now is sufficient to trigger scrutiny and where, as here, PSE offers no real explanation, a finding that the higher capacity valuation in the Sinclair contract is unsupported.

79. Finally, the Commission should also reject PSE's attempt to shift the burden to Public Counsel to provide alternative comparators.[161] This reflects a fundamental misunderstanding of the regulatory process. It is the Company who must carry the burden of proof, not the intervenors. Dr. Earle found a clear problem with PSE's methodology as illustrated by contemporaneous contracts using different capacity valuation. PSE claims expertise in bilateral trades; it is incumbent on PSE's experts to find ways to independently value capacity or to create a methodology that creates repeatable consistent results. PSE is asking Public Counsel to prove a negative—as if in Public Counsel's spare time, it has conducted a survey of all power contract capacity valuations that proves PSE's internal valuation was flawed. Instead, the commission should require PSE to deploy is many data points in a comprehensive valuation system to provide an answer to Dr. Earle's reasonable critique.

80. Moreover, as Dr. Earle explained in his testimony, there is an easy and direct comparison from PSE itself—a contemporaneous contract valued at [redacted].[162] It is undisputed that if PSE had used a consistent valuation for capacity between the two contracts, PSE's Sinclair

Shaded Information is Designated as Confidential per WAC 480-07-160

[160] *Puget Sound Power & Light Co.*, Dockets UE-920499 & UE-921262 Eleventh Suppl. Order, at 19.
[161] Haines, Exh. PAH-19CT at 5:1–2.
[162] Earle, TR. 308:18–24.

contract is less valuable to PSE customers by $3,562,650. It is PSE's burden to prove its case, not Public Counsel.

B. Annual Power Cost Proceedings Should Be Streamlined

81. PSE proposed continuing the annual power cost update process adopted in 2022.[163] Under PSE's imagining, annual power costs filings would be separate from PCORC and GRC proceedings and would remove updates for variable costs from GRCs.[164] PSE is effectively requesting three sets of proceedings, one for variable power costs (annual power cost update), a second of fixed power costs (PCORC), and a contingent third filing for general rate case proceeding, with prudency review spread throughout the three proceedings depending on the timing of the filing and type of resource. The Commission should streamline the number and cadence of these filings by reserving fully prudence determinations to general rate cases.

82. The number of filings and their complexity is already straining the ability of non-Company parties to advocate on behalf of the public interest. As Dr. Earle explains, each filing creates a significant time and resource burden on Staff, Public Counsel, and intervenors.[165] This case illustrates the burdens associated with PSE's multiplicity of filings; PSE's filing includes nearly 40 witnesses and hundreds of exhibits. No other party has more than eight witnesses. Rate proceedings represent a fundamental and significant asymmetry in terms of information and resources, and permitting a rapid cadence magnifies that burden and undermines the ability to conduct meaningful review. Furthermore, permitting the continued proliferation of trackers and separate proceedings contravenes the purpose of multiyear rate case statute, which the

[163] Direct Testimony of Brennan D. Mueller, Exh. BDM-1T at 42:18–20.
[164] Mueller, Exh. BDM-1T at 48:3–13, 49:9–15.
[165] Earle, Exh. RLE-1CT at 12:22–13:8.

Legislature intended to reduce the administrative burden of incredibly complex annual rate filings.[166] PSE's proposal restores an annual cadence for complex proceedings, committing the Commission to review annual variable power costs on top of GRCs and PCORC filings.

83. If the Commission permits additional power cost filings, in order to preserve meaningful review, the Commission should reserve final prudency review to GRCs.[167] If PSE choses to address prudency of power costs in annual power cost updates or PCORCs, their approval should be provisional and subject to refund.[168] This would permit Staff, Public Counsel, and intervenor parties to prioritize their review on GRCs as intended by the multiyear rate plan statute.

C. The Commission Should Reject Staff's Proposal to Place CCA Allowance Costs into Rates

84. Staff next proposes to add CCA allowance costs into dispatch decisions in rates and to conduct prudence reviews in the annual power cost filings. The Commission should reject both proposals. While Public Counsel understands Staff's concerns with uneconomic dispatch and agrees with Staff that CCA allowance costs must be subject to prudency review, Staff's proposal is unworkable because there is currently no effective way to forecast allowance costs. While PSE must do its best to estimate allowance costs for planning purposes, permitting those guesses to be placed into rates places too much risk of overcollection on ratepayers.

85. Taking the proposals in reverse order, prudence reviews of CCA allowance costs have to be aligned with the CCA compliance period. As Dr. Earle explains, the CCA allowances purchased in one year can be used throughout the compliance period.[169] Because the compliance

---

[166] *Id*. at 12:2–12.
[167] *Id*. at 12:22–13:8.
[168] *Id*. at 14:13–15:5.
[169] Earle, Exh. RLE-6T at 7:9–17.

period is four years plus 10 months, this means it may not be possible to know whether a 2023 purchased allowance was cost effective or necessary until after the 2027 compliance period closes and PSE actually uses the allowance to meet a CCA obligation. It is akin to "declaring a winner after one quarter of the basketball game."[170] Staff Witness Wilson acknowledges that reality, admitting that the Commission could reasonably determine that "a final, retrospective prudency examination covering each four-year compliance window would be appropriate."[171] The Commission should accept this concession and reserve final prudence review of CCA costs until the end of the CCA compliance period.

86. Staff's proposal for placing CCA allowance costs into rates and for including CCA costs in dispatch decisions founders on the current inability to accurately forecast CCC allowance costs. Dr. Earles' review of CCA allowance costs in the California market illustrates the difficulty of forecasting an allowance market even in short time frames.[172] The Washington market's nascent year has been even more difficult to predict and will remain so as CETA seeks to transform the Washington power market.[173] PSE's position is unambiguous: "this uncertainty makes it currently impossible to forecast PSE's CCA allowance obligation and ultimate allowance costs with a reasonable level of confidence."[174] Unlike other operating expenses which have a long history on which to base reliable forecasts, the allowance market is too young for accurate forecasts.[175]

---

[170] *Id.* at 9:2–3.
[171] Wilson, Exh. JDW-1T at 29:14–15.
[172] Earle, Exh. RLE-6T at 11:10–15.
[173] *Id.* at 12:3–9.
[174] Mueller, Exh. BDM-23T at 34:3–5.
[175] Earle, Exh. RLE-6T at 14:1715:5.

87. Public Counsel acknowledges, and shares, Staff's concern with uneconomic dispatch if CCA allowance costs are not included in planning decisions. However, attempting force CCA allowance costs into rates makes the problem worse rather than better. In the absence of any way to forecast CCA allowance costs four years into the future, placing CCA allowances into rates would devolve in an expensive and fruitless fight over how to set a CCA allowance rate.[176] The Commission would have to evaluate what are, at best, competing guesses and enshrine those guesses into rates, which would necessarily create risk for ratepayers and the company.[177]

88. The more rationale solution to aligning PSE's profit motive with lower CCA allowance costs is the adoption of a risk-sharing mechanism in the current CCA tracker.[178] With respect to allowance prices, a well-designed sharing mechanism could rely on actual market outcomes and judge PSE's performance against them from an ex ante perspective.[179] Such a market performance mechanism avoids the need to impossible forecasting while incenting PSE to make rational market decisions.

89. Refusing to place allowance costs into rates does not relieve PSE of its obligation to plan for CCA related costs. As Dr. Earle explains, Staff's proposal conflates prudence review of the actual allowance costs PSE incurs with the planning decisions PSE makes within the four-year CCA compliance period.[180] Staff Witness Wilson is correct to note that PSE's decisions to buy, sell, hold, or use allowances are intertwined with dispatch and power purchase decisions.[181]

---

[176] *Id*. at 13:4–8.
[177] *Id*. at 13:10–11.
[178] *Id*. at 15:6–14.
[179] *Id*. at 14:11–14.
[180] *Id*. at 6:16–17.
[181] Wilson, Exh. JDW-1T at 27:3-13

Those estimates should be reviewed for reasonableness as part of prudent planning. Placing future allowance prices into rates requires precision in forecasting that is not currently possible no matter how much Staff wishes it were.[182] The Commission should not force rate payers, or PSE, to bear the risk of forecast error.

90. In conclusion, the Commission should reject PSE's proposed rate increases as they are inadequately supported by the evidence. Such rate increases would also pose a major financial burden on ratepayers, especially seniors and people with disabilities on a fixed income. Based on Public Counsel's expert testimony and the extensive record in this matter, we recommend approving a lower ROE, a capital structure with a lower equity percentage, and adjustments to PSE's revenue requirement, including limiting storm expense normalization, rejecting increases in incentive compensation, and modifying downward O&M expense forecasts.

DATED this 4th day of December 2024.

ROBERT FERGUSON
Attorney General

Jessica Johanson-Kubin

JESSICA JOHANSON-KUBIN, WSBA No. 55783
Assistant Attorney General

Attorney for Public Counsel Unit

Washington Attorney General's Office
Public Counsel Unit
800 Fifth Avenue, Suite 2000
Seattle, WA 98104
Jessica.Johanson-Kubin@ATG.WA.GOV

[182] Earle, Exh. RLE-6T at 4–12.