www.pse.com

PUGET SOUND ENERGY
The Energy To Do Great Things

Puget Sound Energy, Inc.
P.O. Box 97034
Bellevue, WA 98009-9734

Filed via WUTC Electronic Web Portal

October 5, 2012

Mr. David W. Danner
Executive Director and Secretary
Washington Utilities and Transportation Commission
1300 South Evergreen Park Drive S.W.
P.O. Box 47250
Olympia, WA 98504-7250

Subject: **PSE Reply Comments and Responses to Statements of Proposed Issues**
Docket No. UG-121207
Commission Investigation into Natural Gas Conservation Programs

Dear Mr. Danner:

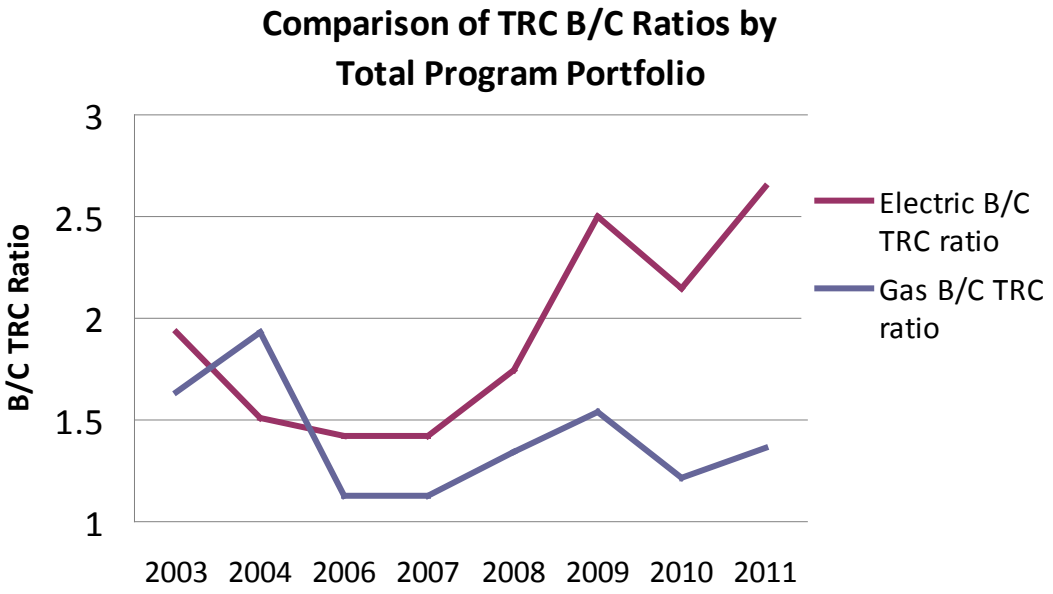
In response to the Commission Notice seeking written comments on issues related to natural gas conservation in Docket UG-121207, Puget Sound Energy, Inc. ("PSE" or the "Company") offers the following overall comments and specific responses to statements of proposed issues the Commission noted in its opportunity to file written reply comments and responses.

Overall Comments

Historical Perspective

PSE believes that it is important to understand the historical differences between the benefit-cost ratio ("B/C") of the Total Resource Cost ("TRC") of the portfolio of natural gas conservation programs compared to the same B/C ratio of the portfolio of electric conservation programs. As indicated in the chart below, the natural gas portfolio generally had a lower TRC ratio than electric. This is primarily due to the fact that natural gas measures are more expensive. By virtue of having a TRC B/C ratio closer to the threshold value of 1.0, gas measures are more sensitive to natural gas prices than electric measures. So

it is not a new phenomenon that natural gas conservation measures are highly sensitive to commodity price changes.



Demand-side (conservation) analysis needs to match supply-side analysis

PSE believes that the Commission should cautious in proscribing changes to the assumptions or factors in the avoided cost calculations for natural gas conservation programs that would deviate from the "least cost" mix rule of WAC 480-90-238. Requiring utilities to use such different assumptions in the demand-side (conservation) analysis versus the supply-side analysis would conflict with the following language of the first sentence in WAC 489-90-238 (1)(a) (emphasis added):

> Purpose. **Each natural gas utility regulated by the commission has the responsibility to meet system demand with the least cost mix of natural gas supply and conservation.** In furtherance of that responsibility, each natural gas utility must develop an "integrated resource plan."

Demand-side analysis needs to be the lowest reasonable cost to utility and ratepayers

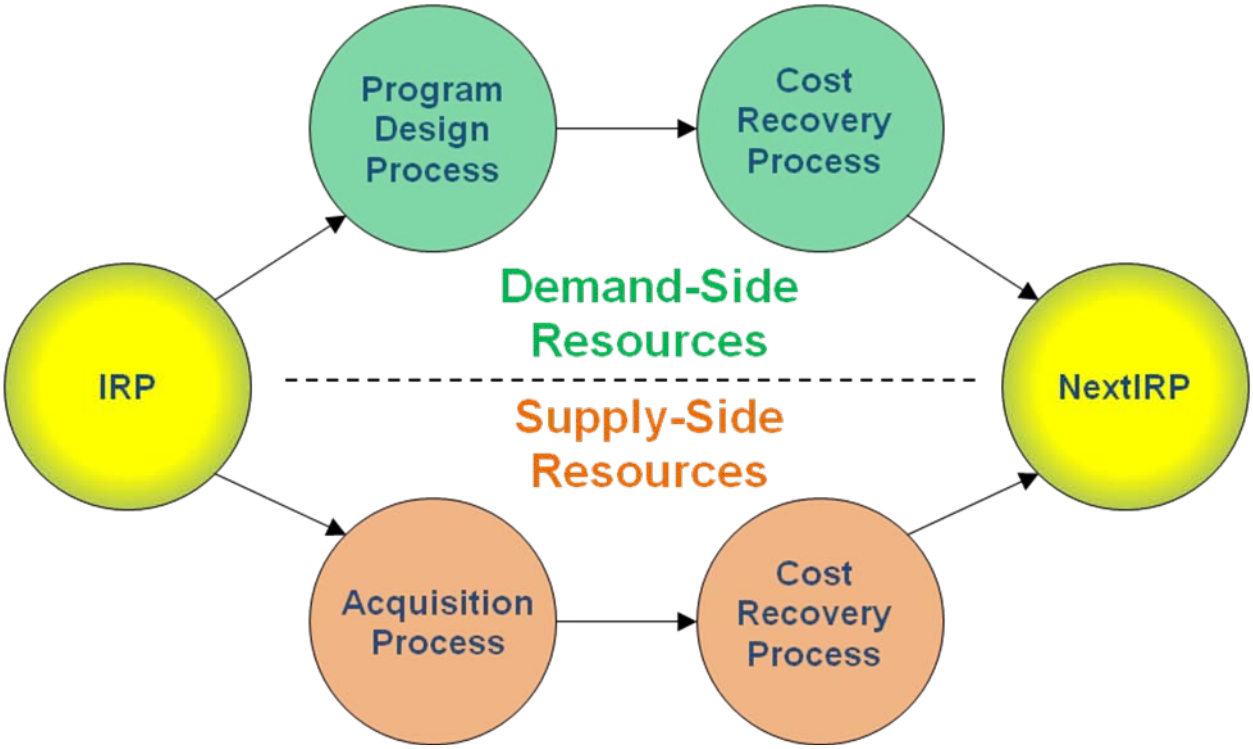
PSE believes that the Commission should exercise caution in proscribing new "societal" benefits or changes to the discount rate in the avoided cost calculations for natural gas conservation programs that would deviate from the "least cost" mix rule of WAC 480-90-238. Requiring utilities to use new, unquantified benefits or risk preferences reflected through the discount rates that go beyond benefits to the utility and the ratepayers (such as so-called "societal" benefits or societal discount rates) would appear to conflict with the plain language of WAC 489-90-238 (2)(a) (emphasis added):

"…a plan describing the mix of natural gas supply and conservation designated to meet current and future needs at the lowest reasonable cost **to the utility and its ratepayers**."

There are two distinct processes that analyze conservation cost-effectiveness

As described below, there are two distinct, but separate processes that perform conservation cost effectiveness analysis -- the IRP and the program design process. PSE is unclear which process, or set of rules, are being discussed in this CR-101 process. PSE believes that it is not advisable for the Commission to introduce disconnects in assumptions between the IRP and the program design process.

The first process where cost effectiveness of conservation is addressed is in the Integrated Resource Plan ("IRP")—a compliance filing under WAC 480-90-238. The second is the program design process, which uses inputs from the IRP process to determine specific conservation programs to be executed. The connection between the processes is summarized below in Diagram 1.



The IRP Process: The IRP is a "…a plan describing the mix of natural gas supply and conservation designated to meet current and future needs at the lowest reasonable cost to the utility and its ratepayers."[1] All gas utilities under the Commission's jurisdiction use the Sendout model to support IRP compliance. Sendout allows utilities to take into account complex economic tradeoffs, such as reflecting the impact of flexible storage operation on

[1] WAC 480-90-238 (2)(a).

costs, fixed versus variable cost tradeoffs, and tradeoffs in timing over the long-term, in a way that would be difficult (if not impossible) to reproduce in spreadsheet analysis.

The Program Design Process: The IRP analysis does not reflect the level of detail needed to design executable conservation programs—just like the IRP does not reflect enough detail to be stand-alone support for a supply-side acquisition. The program design process uses outputs from the IRP process in a simplified way (relative to the Sendout Model) to allow a focus on operational details pertinent to developing commercially executable and successful programs. Such details can include refinements of measures and market penetration rate assumptions, bundling of specific measures, fine-tuning timing for execution, etc.

Not advisable to create disconnections
PSE believes that it is not advisable for the Commission to introduce disconnects in assumptions between the IRP and the program design process. If the Commission mandates a different discount rate or environmental adders be applied in the Program Design process, the IRP will be targeting a different resource mix than the program design process. Furthermore, PSE believes that requiring utilities to use such different assumptions in the program design process would conflict with the following language in WAC 480-90-238 (1)(a) (emphasis added):

> Purpose. **Each natural gas utility regulated by the commission has the responsibility to meet system demand with the least cost mix of natural gas supply and conservation.** In furtherance of that responsibility, each natural gas utility must develop an "integrated resource plan."

This provision requires PSE, in the IRP, to examine costs from the standpoint of the utility and its ratepayers. Therefore, requiring use of assumptions that create a disconnect between the program design process and IRP not only creates a disconnect in planning, it would conflict with the gas utilities' obligation to provide least cost service.

Nothing is Broken
PSE has not seen any irreconcilable differences between the IRP and program design process at PSE. Those teams within PSE work together very effectively, to ensure assumptions going into the IRP are reasonable and that outputs are reasonable from a commercially achievable perspective, including cost effectiveness. The process works. PSE does not believe there is any problem that needs to be addressed at PSE.

Possible Alternative to Developing Problematic "Avoided Cost" Rules
In its 2013 IRP, PSE will expand upon timing and ramp rates questions that began in our 2011 IRP. The Company plans to test things like whether it is cost effective to defer implementation of all conservation, to defer higher-cost conservation, or defer higher cost conservation while accelerating the lowest cost conservation measures—all to the extent such activities would be commercially achievable. PSE recommends that Commission defer actions on developing "Avoided Cost" rules until the 2013 IRP is completed.

As mentioned above, creating new or inconsistent "Avoided Cost" rules for natural gas conservation would not be in the public interest. There may, however, be a reasonable policy the Commission could adopt to address the underlying concern about natural gas conservation programs. Something like:

> Dynamic market conditions create challenges to planning for, developing, and executing cost-effective gas conservation programs. To accommodate such dynamic conditions, utilities are permitted to conduct rigorous analytical updates or additional analytical support. This could include something like a comprehensive IRP-level analysis check-in. An "IRP check-in" would not require all assumptions to be updated, but needs to provide sufficient assurance that the revised level of conservation will continue to meet requirements of WAC 480-90-238 (1) "…to meet system demand with the **least cost mix of natural gas supply and conservation."**

It should be noted that policy would still be consistent with the standard practice under PSE Conservation Tariff Schedule (Schedule 183) which already allows PSE to terminate a non-cost-effective natural gas conservation program immediately.

Responses to specific issues

1. What are the appropriate assumptions or factors to include in natural gas avoided cost calculations?

For PSE, the appropriate assumptions or factors to include in natural gas avoided cost calculations are highlighted in Schedule 183 of PSE's Natural Gas Tariff:

> "**Avoided Cost**, also known by the terms Conservation Cost Effectiveness Standard or Energy Efficiency Cost Effectiveness Standard herein for Conservation/energy efficiency activities and/or Measures is based on forecast gas commodity market prices and includes the credits for avoided pipeline capacity and transport costs and avoided storage and distribution costs."

PSE has previously submitted a description of PSE's current process for calculating the avoided cost for natural gas conservation programs. This description is similar to what was included in our most recent Biennial Conservation Plan ("BCP").

In addition, there are some assumptions and factors that are different on the natural gas side than the electric side. This should be no surprise, and should not be an issue of concern. For example, in the electric calculation, there is the use of a 10% environmental adder, this factor is only appropriate to be used on the electric side and not on the natural gas side. There are no regulatory requirements for applying this to natural gas. This has issue has been transparent with our stakeholders and has a long-time precedent within PSE's Commission-acknowledged Integrated Resource Plan.

PSE believes that the Commission should exercise caution in proscribing changes to the assumptions or factors in the avoided cost calculations. Any such short-term changes should

not be viewed as "policy" decisions, but rather as a fundamental change in the methodology of calculating avoided costs. Any such short-term changes could have serious implications upon how both customers and stakeholders view the veracity of whether or not conservation programs are appropriate programs to fund. In short, PSE believes that nothing is fundamentally "broken" with the avoided cost calculation for natural gas conservation that necessitates fixing.

2. Should companies use a combination of cost tests in evaluating the cost-effectiveness of natural gas conservation programs?

PSE is comfortable with the way the uses and interactions of the cost tests are described in the tariff book, and does not believe that anything is broken and needs to be fixed. For PSE, the cost test that is highlighted in Schedule 183 of PSE's Natural Gas Tariff is the Total Resource Cost ("TRC") Test:

> "Conservation/energy efficiency activities will be consistent with cost-effectiveness as defined by a Total Resource Cost Test."

The same tariff schedule also discusses the Utility Cost Test ("UCT"):

> "Company funding for services will be limited to cost-effectiveness defined by a Utility Cost Test using the Company's Energy Efficiency Cost Effectiveness Standard, also known as the Conservation Cost Effectiveness Standard."

The same tariff schedule also describes how individual conservation measures must be consistent with both the TRC and the UCT:

> "In addition to meeting the definition of Measure in Section 4 a Measure must reasonably be expected to satisfy the Total Resource Cost Test and the Utility Cost Test."

It should also be noted that some specific Conservation programs have to meet the TRC test for example all regional market transformation programs, such as NEEA must be cost-effective from a TRC perspective. As indicated in PSE natural gas conservation schedule 183:

b. Regional Market Transformation: Northwest regional programs include projects aimed at advancing new promising technologies or changes to standards, codes and practices, which are anticipated to be cost-effective from a Total Resource Cost Test perspective over time.

PSE believes that the Commission should exercise caution in proscribing changes to the uses and interactions of the cost tests in PSE's tariff books, settlements and PSE commission orders, and the well-established CRAG process. Any such short-term changes to the uses of these costs tests should not be viewed as "policy" decisions, but rather as a fundamental

change in the methodology. Any such short-term changes could have serious implications upon how both customers and stakeholders view the veracity of whether or not conservation programs are appropriate programs to fund. In short, PSE believes that nothing is fundamentally "broken" with the uses and interactions of the cost tests for natural gas conservation that necessitates fixing.

Other Issues

Environmental Adder
As noted above, the natural gas calculation has been consistently different than the electric calculation. In the electric calculation, there is the use of a 10% environmental adder, this factor is only appropriate to be used on the electric side and not on the natural gas side. The only reason it is applied to electric, because there is a law proscribing it for the Council. Beyond that law there is no reason to do so. There are no regulatory requirements for applying this to natural gas. So applying it to natural gas would be arbitrary. This has issue has been transparent with our stakeholders and has a long-time precedent within PSE's Commission-acknowledged Integrated Resource Plan.

Cost Effectiveness Standard for Low- Income Weatherization Programs
Low-Income weatherization programs need to meet ***some*** level of cost-effectiveness. In the case of PSE, Commission-approved tariff schedules for the low-income weatherization programs provide that these programs must have a TRC of 0.667:

a. Low Income: Low Income Customers are qualified by government agencies, using federal low income guidelines. Approved Low Income agencies may receive Measure funding equal to the lesser of one hundred percent (100%) of the Measure Cost or the value that will result in a Total Resource Cost Benefit/Cost ratio of a minimum of 0.667. Funding is in accordance with funding described in Electric Energy Efficiency Schedule 201.

Carbon Regulation
The Commission has declined to mandate a specific carbon tax amount for utilities to model. A range of potential future carbon taxes is already modeled within the IRP, so those assumptions are already in the IRP and the program design process.

PSE appreciates the opportunity to present these comments. Please direct any questions regarding these comments to Eric Englert at (425) 456-2312 or the undersigned at (425) 462-3495.

Sincerely,

/s/ Tom DeBoer

Tom DeBoer
Director – Federal & State Regulatory Affairs