

EXHIBIT NO. __ (EAF-1T)
Docket Nos. UE-121697/UG-121705
WITNESS: Edward A. Finklea

BEFORE THE
WASHINGTON UTILITIES AND TRANSPORTATION COMMISSION

In the Matter of the Petition of

PUGET SOUND ENERGY, INC.
and NW ENERGY COALITION

Dockets UE-121697 and UG-121705
(Consolidated)

For an Order Authorizing PSE To
Implement Electric and Natural Gas
Decoupling Mechanisms and To Record
Accounting Entries Associated With the
Mechanisms

RESPONSE TESTIMONY OF EDWARD A. FINKLEA

ON BEHALF OF

THE NORTHWEST INDUSTRIAL GAS USERS

April 26, 2013

1 settlement of issues related to Dockets UE-121697 and UG-121705 (the “Decoupling
2 Docket”), Docket UE-121373 (relating to the acquisition of Coal Transition Power), and
3 PSE’s Expedited Rate Filing (“ERF”) in Dockets UE-130137 and UG-130138. This
4 settlement proposal is also referred to as the “Global Settlement.”

5 **Q. PLEASE DESCRIBE IN SUMMARY TERMS WHAT THESE DOCKETS MEAN**
6 **FOR NATURAL GAS CUSTOMERS.**

7 As stated in the testimony of Michael Deen on behalf of NWIGU, these dockets represent
8 an expedited rate filing which updates natural gas margin revenues from the last general
9 rate case to a test year ending June 2012 and a decoupling proposal that includes annual
10 2.2% increases for delivery related costs (i.e. non- purchased gas costs) for the two to
11 three year duration of the proposed settlement. Issues related to PSE’s proposed
12 acquisition of Coal Transition Power are also addressed in the Global Settlement but
13 those issues are strictly related to electricity service and have no significance for natural
14 gas customers.

15 **Q. DOES YOUR TESTIMONY RELATE TO EITHER THE ERF DOCKET OR THE**
16 **COAL TRANSITION POWER DOCKET?**

17 **A.** No. NWIGU’s testimony relating to the ERF Docket and the Coal Transition Power
18 Docket is being submitted through Michael Deen. My testimony will address issues
19 relating only to the Decoupling Docket.

20 **Q. PLEASE SUMMARIZE YOUR RECOMMENDATIONS FOR THE**
21 **DECOUPLING DOCKET.**

22 **A.** NWIGU has found that the Global Settlement as proposed, which adopts the proposed
23 Decoupling Mechanism without modification, is not in the public interest and would not

1 produce fair, just, and reasonable rates for natural gas service from PSE to its customers.
2 The proposed decoupling mechanism does not provide any gas conservation benefits.
3 The proposal also attempts to provide PSE with the benefits of guaranteed cost recovery
4 without capturing any benefits of lower capital and equity costs that should otherwise
5 flow to PSE's gas customers. Moreover, the record is void of any legitimate basis for
6 applying the Decoupling Mechanism to PSE's industrial customers – especially those
7 industrial customers on a transportation schedule.

8 For these reasons, and reasons stated in the testimony of Michael Deen, NWIGU
9 recommends that the Global Settlement and its constituent parts should be rejected in
10 their entirety. However, if the Commission wishes to continue with the Global
11 Settlement construct, NWIGU has a number of recommendations to make the proposal
12 more balanced for consumers, in addition to the recommendation presented in the
13 testimony of Michael Deen:

- 14 • The Decoupling Mechanism should be modified to exclude its application to
15 gas customers on schedules 85/85T and 87/87T.
- 16 • Cost of capital should be considered as an issue in the Global Settlement.

17 **II. ANALYSIS OF THE DECOUPLING MECHANISM**

18 **Q. WHAT IS THE PURPOSE OF PSE'S DECOUPLING MECHANISM?**

19 **A.** According to page 4 of the Amended Petition, the primary purpose of the Decoupling
20 Mechanism is to “substantially diminish the throughput incentive that exists under PSE’s
21 current ratemaking structure.” As a variation on this purpose, that same portion of the
22 Amended Petition describes an effort to solve a “predicament” whereby PSE alleges it is
23 unable to recover delivery costs when it successfully implements its conservation
24 programs.

1 **Q. YOU DESCRIBED A “PRIMARY” PURPOSE. IS THERE ANOTHER PURPOSE**
2 **BEHIND PSE’S DECOUPLING MECHANISM.**

3 **A.** Yes. Independent of PSE’s efforts to address an alleged “throughput incentive,” and as
4 stated on page 4 of the Amended Petition, the Decoupling Mechanism is also intended to
5 address “revenue shortfall between rate cases that the decoupling mechanism on its own
6 does not resolve.”

7 **Q. HAS THE COMMISSION PROVIDED GUIDANCE ON WHAT FACTORS, IF**
8 **ANY, IT WILL CONSIDER AS PART OF A FULL DECOUPLING**
9 **MECHANISM?**

10 **A.** Yes. PSE’s and NWECA’s justification for the proposed Decoupling Mechanism relies
11 heavily on the Commission’s investigation into energy conservation mechanisms as part
12 of Docket U-100522 in 2010. The outcome of that docket was a policy statement that
13 would be used to guide the Commission’s consideration of future decoupling proposals.¹
14 Although the commission expressed some reluctance in the Policy Statement to consider
15 full decoupling in the future, it did state that a properly constructed proposal could be a
16 useful tool. Specifically, the Commission saw potential benefits to customers because
17 decoupling would reduce a company’s debt and equity costs.² Those benefits would flow
18 to customers by yielding rates that would be lower than they otherwise would be to
19 account for a reduction in overall risk to the utility.³

¹ *In re WUTC Investigation into Energy Conservation Incentives*, Docket U-100522, Report and Policy Statement on Regulatory Mechanisms, including Decoupling, to Encourage Utilities to Meet or Exceed Their Conservation Targets (Nov. 4, 2010) (hereinafter, “Policy Statement”).

² *Id.* at p. 16.

³ *Id.* at pp. 16-17.

1 **Q. CAN YOU DESCRIBE THE ELEMENTS OF FULL DECOUPLING THAT THE**
2 **COMMISSION’S POLICY STATEMENT ANTICIPATED?**

3 **A.** The Commission clearly stated in the Policy Statement that it would consider a full
4 decoupling proposal in the context of a general rate case. Moreover, the Commission
5 stated that a full decoupling mechanism would have to be conditioned upon a utility’s
6 level of achievement with respect to its conservation target. The Commission then set
7 out some minimum elements that must be included in such a decoupling mechanism: (1)
8 a true-up mechanism; (2) an evaluation of impact on rate of return; (3) a proposed
9 earnings test; and (4) accounting for off-system sales and avoided costs.

10 **Q. WHAT IS MEANT BY “CONDITIONED UPON A UTILITY’S LEVEL OF**
11 **ACHIEVEMENT WITH RESPECT TO ITS CONSERVATION TARGETS”?**

12 **A.** The Commission has made it clear that a decoupling mechanism should be approved only
13 where it results in a quantifiable increment of conservation that would not otherwise be
14 achieved. The Commission lists that expectation as one of the criteria for approval in the
15 Policy Statement.

16 **Q. DOES THE PROPOSED DECOUPLING MECHANISM INCLUDE THE**
17 **MINIMUM ELEMENTS THE COMMISSION SET FORTH IN THE POLICY**
18 **STATEMENT?**

19 **A.** No. The proposed Decoupling Mechanism lacks any evaluation on the mechanism’s
20 impact on rate of return.⁴ This oversight is significant in light of the Commission’s
21 statement that it is willing to consider full decoupling only because of the potential
22 reduction in a company’s debt and equity costs.

⁴ See Exhibit No. __ (JAP-1T) at 33:3-5.

1 **Q. DOES THE PROPOSED DECOUPLING MECHANISM CONTAIN ANY OTHER**
2 **FLAWS?**

3 **A.** Yes. As noted earlier in my testimony, the Commission stated that full decoupling would
4 be conditioned upon a utility’s level of achievement with respect to conservation targets.
5 More precisely, the Commission contemplated that a full decoupling proposal would
6 result in some additional increment of conservation achievements. PSE and NWECC
7 appear to acknowledge this in the Amended Petition on page 5 where they argue that
8 decoupling will remove disincentives for conservation and that “the decoupling
9 mechanism proposed in this petition will require PSE to stretch even farther – **beyond its**
10 **Commission-approved target** – to accelerate conservation savings.”⁵ The promise to
11 stretch even farther, however, is a hollow one with respect to PSE’s gas operations. PSE
12 has simply failed to describe *any* additional conservation that will result from the
13 decoupling proposal. In fact, PSE has been quite candid that its gas conservation
14 achievements will remain identical with or without the decoupling mechanism.⁶

15 **Q. IN ADDITION TO THE LACK OF ANY INCREMENTAL GAS**
16 **CONSERVATION ACHIEVEMENTS, DOES NWIGU FIND ANY OTHER**
17 **FLAWS IN THE PROPOSAL?**

18 **A.** Yes. PSE has provided no rationale, consistent with the goals of the proposal, for
19 applying the mechanism to gas transportation customers. A common goal of any
20 decoupling mechanism is to break the link between a utility’s recovery of fixed costs and
21 its revenue from volumetric charges. Or, as PSE and NWECC describe it, the goal is to
22 remove the “throughput incentive,” which is the utility’s incentive to sell higher volumes

⁵ Emphasis added.

⁶ Exhibit No. __ (EAF-3) at p.1 (PSE’s Response to NWIGU DR No. 011).
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1 in order to recover its fixed costs. That linkage, however, does not exist for gas
2 transportation customers because those customers purchase their own gas and the utility
3 provides no incentives to those customers to invest in conservation measures. Gas
4 transportation customers, under well-established commission precedent, do not
5 participate in company funded conservation programs. Simply put, PSE does not face
6 any risk that company-funded conservation investments will result in lower cost recovery
7 from gas transportation customers.

8 **Q. HOW DO PSE AND NVEC RESPOND TO THAT CRITICISM?**

9 **A.** When asked in a data request, neither PSE nor NVEC could state how the proposed
10 Decoupling Mechanism actually reduces the Company's throughput incentive with
11 respect to gas transportation customers. Instead, PSE and NVEC each avoided that
12 question and offered a separate reason, unrelated to the throughput incentive, for applying
13 the mechanism to gas transportation customers. Specifically, each stated that the
14 mechanism would stabilize the Company's revenue by serving as a disincentive for
15 customers to switch back and forth between rate schedules.⁷ This is not a well-reasoned
16 response. First, that response fails to explain how switching rate schedules creates any
17 impact to the Company, and fails to grapple with the fact that there are customer benefits
18 to having flexibility in a choice of schedules. Second, PSE's tariffs are already structured
19 in a way to prevent arbitrary switching between rate schedules that could otherwise be
20 used to "game the system." For example, PSE's tariffs impose conversion penalties that
21 essentially commit a customer to a specific rate schedule for a specified time period.
22 Third, the better way to address the problem PSE has identified with potential switching

⁷ Exhibit No.__(EAF-3) at pp. 2-3 (PSE Response to NWIGU DR No. 013 and NVEC Response to NWIGU DR No. 3).

1 is to not apply the decoupling mechanism to Schedule 85 and 87 sales and transportation
2 customers.

3 **Q. ARE THERE OTHER REASONS GAS TRANSPORTATION CUSTOMERS**
4 **SHOULD NOT BE INCLUDED IN THE MECHANISM?**

5 **A.** Yes. Another expressly stated goal for full decoupling put forward by PSE and NWECC is
6 to reduce the impact of Company-sponsored conservation on the Company's ability to
7 recover fixed costs. The decoupling proposal ignores the fact that gas transportation
8 customers do not pay into or receive any benefits from company-sponsored conservation.
9 To the extent that the Company's ability to recover revenue is limited by its conservation
10 efforts, that dynamic is unique to non-transportation customers and cannot be used as a
11 basis for applying the mechanism to gas transportation customers.

12 **Q. PSE AND NWECC APPEAR TO RELY HEAVILY ON THE FACT THAT THE**
13 **COMMISSION HAS ALREADY ANALYZED AND PROVIDED TACIT**
14 **APPROVAL FOR THE PROPOSED MECHANISM. WHAT IS YOUR**
15 **TESTIMONY WITH RESPECT TO THAT POSITION?**

16 **A.** On page 11 of the Amended Petition, PSE and NWECC state the following: "In
17 sum, the Commission has recently completed a full analysis of decoupling in general and
18 for PSE specifically, including a decoupling proposal that included most elements of the
19 decoupling proposal that PSE and the Coalition are presenting in this case." This is a
20 common theme in the Amended Petition and the supporting testimony, and also appears
21 to be the basis for Staff's approval of the Global Settlement, which would adopt the
22 Amended Petition without any modification. That viewpoint, however, is highly
23 misleading. The Commission's review of NWECC's prior proposal in PSE's last rate case

1 was not a “full” analysis because it did not include a proposal for the Company’s gas
2 operations. Mr. Cavanaugh acknowledges as much in his testimony and in response to a
3 data request on this matter.⁸ The Commission’s only other recent review of a decoupling
4 mechanism in the gas context was in Avista’s last general rate case. The distinction
5 there, obviously, is that the Avista decision was made as part of a general rate case, when
6 the Commission had the ability to take into consideration all of the various costs
7 components impacting that utility’s operations. The Commission was able to expressly
8 consider rate of return with that proposal, unlike here, where PSE has gone to great
9 lengths to avoid any consideration of rate of return. It is disingenuous for the Company
10 and NWECC to act as if there is no new ground being broken here. Not only is the
11 proposal new ground for this Commission, but I am not aware of any decoupling program
12 in Washington or other states that applies to gas transportation customers. When asked,
13 NWECC was also unable to identify any existing program that applies to gas transportation
14 customers.⁹

15 **Q. DOES THIS CONCLUDE YOUR TESTIMONY?**

16 **A.** Yes.

⁸ See, e.g., Exhibit No.__(RCC-3T), 2:3-5.

⁹ Exhibit No.__(EAF-3) (NWECC Response to NWIGU DR No.5).