BEFORE THE
WASHINGTON UTILITIES AND TRANSPORTATION COMMISSION

WASHINGTON UTILITIES AND TRANSPORTATION COMMISSION,	)	
Complainant,	)	
v.	)	**DOCKETS UE-170033 and UG-170034 (Consolidated)**
PUGET SOUND ENERGY,	)	
Respondent.	)	

INITIAL POST-HEARING BRIEF OF THE FEDERAL EXECUTIVE AGENCIES

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OVERVIEW AND SUMMARY OF CASE

The Federal Executive Agencies ("FEA") hereby submits its initial post-hearing brief in this docket. The United States Department of the Navy ("Navy") represents the Department of Defense and all other Federal Executive Agencies in this proceeding. The FEA is one of the largest consumers of electricity in the service territory of Puget Sound Energy ("PSE" or "the Company") and takes electric service from the Company primarily on Schedule 49. The FEA participated in the hearing on contested issues and the hearing on the Multi Party Partial Settlement in this proceeding ("Settlement") that were convened by the Washington Utilities and Transportation Commission ("Commission"). The FEA also filed response and cross-answering testimony in this docket, as well as testimony in support of the Settlement.

The FEA's testimony in this proceeding focused on certain aspects of PSE's proposed electric class cost of service and rate design. Specifically, the FEA's testimony addressed the following areas:

- PSE's electric revenue decoupling mechanism ("RDM");
- The classification and allocation of electric generation and transmission fixed costs;
- The allocation of any changes in electric base rate revenues approved in this case, particularly the allocation to Schedule 49; and
- PSE's proposal to implement a formalized, expedited rate filing ("ERF") process.

The FEA is a signatory to the Settlement in this proceeding. That Settlement addresses the allocation of changes in electric base rate revenues to Schedule 49, as well as PSE's ERF proposal. Accordingly, the two remaining contested issues raised by the FEA in its testimony that were not addressed by the Settlement concern the Company's RDM proposal (other than the method of recovering fixed production costs within the mechanism) and the classification and allocation of generation and transmission fixed costs. These two contested issues are the focus of the FEA's initial post-hearing brief. The FEA's brief also supports adoption of the Settlement in this proceeding.

With respect to revenue decoupling, the FEA objects to PSE's proposal to continue its electric RDM. In the event the Commission decides to continue RDM, we urge the Commission to exclude Schedules 40, 46 and 49 from the mechanism on a prospective basis. In addition, the Commission should impose a hard 3% annual electric RDM rate cap to limit the rate increases associated with the mechanism. Moreover, the Commission should impose other limitations on the operation of RDM as set forth in this brief to ensure that the mechanism is limited to the impacts of reduced energy sales resulting from the Company's energy efficiency programs.

With respect to the classification and allocation of generation and transmission fixed costs, the FEA urges the Commission to reject the Company's proposal to update the peak credit method classification assumptions, which would modify the demand and energy classification percentages specified in the agreement in Docket No. UE-141368. Instead, the Commission should honor the terms of this settlement agreement by establishing the demand/energy classification percentages for generation and transmission fixed costs at 25% demand and 75% energy.

Finally, the FEA respectfully requests that the Commission approve the Settlement in the instant proceeding, as it reflects a reasonable compromise of the competing interests of the settling parties and results in rates that are just and reasonable.

The balance of the Navy's initial post-hearing brief addresses each of the foregoing issues in greater detail.

ELECTRIC DECOUPLING MECHANISM

The Company proposes that its electric RDM become permanent and that the mechanism continue until PSE proposes, and the Commission approves, to have it discontinued or modified.[1/] PSE contends that decoupling is needed to mitigate the incentive that the Company has to increase electricity sales rather than reduce such sales through energy efficiency efforts. The Company also proposes to increase the rate cap for all electric customers subject to RDM from three percent to five percent.[2/] The Company contends that it is appropriate to increase the

[1/] Docket Nos. UE-170033 and UG-170034, Prefiled Direct Testimony of Jon A. Piliaris on behalf of Puget Sound Energy, January 13, 2017, page 146.

[2/] Docket Nos. UE-170033 and UG-170034, Prefiled Direct Testimony of Jon A. Piliaris on behalf of Puget Sound Energy, January 13, 2017, page 5.

electric rate cap to address the potential impact of expanding the scope of the electric RDM to include fixed power costs.

The FEA urges the Commission to reject the continuation of revenue decoupling in this proceeding. As FEA witness Ali Al-Jabir explained in his response testimony, revenue decoupling is an inappropriate and unwarranted departure from traditional ratemaking principles. Under the traditional ratemaking process, the Commission establishes the Company's revenue requirement in a general rate case by relying on a snapshot of the Company's costs and revenues for a given test year. The revenue levels are derived using the Company's test year sales levels, adjusted for weather and other known and measurable changes. Once base rates are set to recover the allowed test year revenue requirement, these rates traditionally remain fixed until the next general rate case. This creates a powerful incentive for the Company's management to operate cost-effectively and promote economic development in its service area, because economic growth results in increased revenues that improve the Company's bottom line between general rate cases.

Revenue decoupling dramatically alters the traditional ratemaking process by allowing the Company to automatically adjust its base rates outside of a general rate case to reflect the impact of changing sales levels over time. In contrast to the strong economic incentives associated with sales growth that are created by the traditional ratemaking process, full revenue decoupling would essentially make the Company's shareholders indifferent to the impact of fluctuations in sales levels in its service area.[3/]

In his response testimony, Mr. Al-Jabir further explains that revenue decoupling should be rejected because it would frustrate the voluntary efforts of customers to reduce energy

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[3/] Docket Nos. UE-170033 and UG-170034, Response Testimony of Ali Al-Jabir, June 30, 2017, page 6.

consumption, transfer traditional utility business risks to customers, reduce the Company's motivation to be responsive to the needs of its customers and create unnecessary rate volatility and uncertainty.[4/] Taken together, these considerations provide ample justification for rejecting the continuation of RDM.

If the Commission nevertheless continues RDM for the Company's electric operations, the FEA urges the Commission to exclude Schedules 40, 46 and 49 from the mechanism on a prospective basis. As Mr. Al-Jabir explained in his response testimony, the fixed revenue erosion concerns that motivate revenue decoupling proposals may be a relevant consideration for residential and small commercial customers because PSE recovers its fixed costs from these customers through energy charges. This heightens the risk of fixed revenue erosion resulting from the implementation of energy efficiency programs.

By contrast, large customers operate under a rate structure that includes both a demand charge and an energy charge. Therefore, any fixed revenue erosion concerns associated with large customers can be addressed by ensuring that all fixed costs associating with serving large customers are appropriately recovered through demand charges or customer charges, rather than energy charges that fluctuate with energy consumption.[5/] Consistent with this approach, the Settlement in this proceeding moved in the right direction of recovering fixed costs from demand and customer charge components of the total rates by applying increased revenues to only the demand and customer charges for Schedules 46 and 49.

An additional consideration is that many large customers are government agencies or large industrial companies that already have government mandates or strong economic incentives

[4/] Docket Nos. UE-170033 and UG-170034, Response Testimony of Ali Al-Jabir, June 30, 2017, pages 7-9.

[5/] Docket Nos. UE-170033 and UG-170034, Response Testimony of Ali Al-Jabir, June 30, 2017, pages 11-12.

to pursue independent energy efficiency efforts. Based on these considerations, it is inappropriate to include PSE's large customers in RDM. The Commission should therefore exclude Schedules 40, 46 and 49 from the electric RDM on a prospective basis.

It should be noted that the Commission's Decoupling Policy Statement in Docket No. UE-100522 clearly contemplates that a decoupling mechanism could exclude specific customer classes from the operation of the mechanism, where the Commission determines that such an approach is in the public interest and is not unlawfully discriminatory or preferential. Therefore, the FEA's proposal to exclude Schedules 40, 46 and 49 from the Company's electric RDM is not in conflict with the Commission's Decoupling Policy Statement.[6/]

If the Commission determines that it is appropriate to continue PSE's revenue decoupling mechanism, the Commission should also restrict RDM only to the revenue impacts resulting from PSE's implementation of energy efficiency programs to achieve mandated conservation targets. In addition, RDM surcharges should be permitted only where there is evidence of a decline in the absolute level of PSE's sales by rate class. These protections are needed to ensure that customers are not exposed to RDM surcharges that result from weather fluctuations or other factors that are unrelated to reduced energy sales attributable to PSE's energy efficiency programs.

Furthermore, if RDM is continued, the Commission should reduce PSE's allowed return on equity to recognize the lower business risks that the Company's shareholders face when revenues are decoupled from sales levels. Absent an adequate downward adjustment to the Company's return on equity to reflect the reduced business risks that revenue decoupling places

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[6/] Docket No. UE-100522, Decoupling Policy Statement, November 4, 2010, page 18.

on PSE, the Company's allowed rate of return would overcompensate the Company's shareholders to the detriment of ratepayers.

Moreover, the Commission should reject the Company's proposal to increase the 3% annual RDM soft cap to 5% for electric customers. Increasing the rate cap in the manner proposed by the Company would harm ratepayers by unduly increasing their exposure to cost increases as a result of RDM. The Company's proposal would also transfer additional business risk away from shareholders and onto customers.

PSE has not demonstrated that there is a need to increase the current 3% rate cap for non-residential electric customers in particular. As Mr. Al-Jabir noted in his response testimony, the independent third-party evaluation of the Company's RDM prepared by H. Gil Peach & Associates, LLC concluded that the current 3% rate cap has worked well for the electric decoupling groups and should be continued.[7/] Additionally, PSE performed a back cast of electric decoupling rate test impacts for the years 2014-2017. The Company's analysis determined that the existing 3% annual rate cap would not have been triggered for electric non-residential customers in any year over the period 2014-2017, even if fixed production costs had been incorporated into the electric decoupling mechanism.[8/] In light of this evidence, there is no reasonable basis for increasing the 3% annual RDM rate cap.

Instead, the Commission should transform the 3% annual soft cap into a 3% hard annual cap that would provide a stricter limitation on the exposure of customers to RDM-related cost increases. As Mr. Al-Jabir explained in his response testimony, PSE's 3% annual soft rate cap does not limit a customer's true exposure to rate increases resulting from RDM, but instead

[7/] Docket Nos. UE-170033 and UG-170034, Response Testimony of Ali Al-Jabir, June 30, 2017, page 17.

[8/] Docket Nos. UE-170033 and UG-170034, Rebuttal Testimony of Jon A. Piliaris on behalf of Puget Sound Energy, August 9, 2017, page 13.

spreads the pain of such rate increases over a longer period of time. If the 3% percent soft cap were transformed into a hard, annual 3% rate cap as proposed by the FEA, the Company's shareholders would bear the risk of any revenue shortfalls in excess of the 3% hard cap. This approach would provide added protection to ratepayers from RDM rate increases and would provide a more balanced allocation of the risks associated with revenue fluctuations relative to the current 3% soft cap.[9/]

CLASSIFICATION AND ALLOCATION OF GENERATION AND TRANSMISSION FIXED COSTS

As Mr. Al-Jabir discussed in his response testimony, PSE used the peak credit methodology to classify production costs into demand and energy components based on the ratio of the cost of a proxy peaking generating resource to the cost of a proxy base load generating resource. The Company allocated the demand-related component of fixed production and transmission costs using a 4CP allocation factor that is based on each class's contribution to the Company's system peak demand during the months of November and December 2015 and January and February 2016. PSE allocated the energy-related component of fixed production and transmission costs based on class energy consumption.

PSE classified 25% of fixed production and transmission costs as demand-related and 75% of such costs as energy-related. The Company based its cost classification proposal on the rate design settlement in Docket No. UE-141368. Paragraph 10 of that settlement agreement specifies that, in the Company's next general rate case, "PSE will adjust demand/energy cost allocation percentages to 25% demand and 75% energy."

[9/] Docket Nos. UE-170033 and UG-170034, Response Testimony of Ali Al-Jabir, June 30, 2017, pages 9-10 and page 17.

In the current general rate case proceeding, PSE asserted that it would be appropriate to update the peak credit analysis using more recent proxy generation resource data. PSE's proposal to update the peak credit analysis would reduce the demand-related classification of production and transmission fixed costs relative to the settlement agreement from 25% to 18%. The energy-related classification of these costs would increase from 75% to 82%.[10/] PSE asserts that this modification would be consistent with the intent of the settlement agreement.

The Commission should reject the Company's proposal to update the peak credit method assumptions and to thereby modify the demand and energy classification percentages specified in the agreement in Docket No. UE-141368. As discussed in Mr. Al-Jabir's response testimony, paragraph 10 of the settlement agreement in Docket No. UE-141368 explicitly requires that the demand and energy classification percentages be set at 25% demand and 75% energy in this proceeding.[11/] Therefore, modifying these demand and energy classification percentages in this case would violate the terms of a prior settlement agreement that was approved by the Commission.

Moreover, by reducing the demand-related component of production and transmission fixed costs, the Company's proposal to update the peak credit classification assumptions would further deviate from sound, cost-based ratemaking principles that require all such fixed costs to be classified as demand-related.[12/]

[10/] Docket Nos. UE-170033 and UG-170034, Prefiled Direct Testimony of Jon A. Piliaris on behalf of Puget Sound Energy, January 13, 2017, page 29.

[11/] Docket Nos. UE-170033 and UG-170034, Response Testimony of Ali Al-Jabir, June 30, 2017, page 25 and Docket No. UE-141368, Order 03, Final Order Approving and Adopting Settlement Agreement, Appendix A, Paragraph 10, January 29, 2015.

[12/] Docket Nos. UE-170033 and UG-170034, Response Testimony of Ali Al-Jabir, June 30, 2017, page 26.

For the foregoing reasons, FEA urges the Commission to classify 25% of the Company's fixed production and transmission costs as demand-related and 75% as energy-related, consistent with the settlement agreement in Docket No. UE-141368.

SETTLEMENT AGREEMENT

The FEA is a signatory to the Settlement in this proceeding. The FEA supports the Settlement because it represents a reasonable compromise of the competing interests of the settling parties with respect to the matters addressed in the Settlement.

Moreover, as Mr. Al-Jabir explained in his testimony in support of the Settlement, the FEA supports the substance of the Settlement because it reduces the overall net electric revenue requirement increase from approximately $68 million (3.2%) under PSE's supplemental filing in this proceeding to approximately $20 million (0.9%) under the Settlement. The Settlement is also acceptable to FEA because it results in a movement in the direction of more cost-based rates for Schedule 49 in two respects. First, the Settlement moves Schedule 49 closer to parity by allocating 65%, rather than 75%, of the average percentage electric rate increase to this rate schedule. This has the effect of reducing the subsidy that Schedule 49 is currently providing to other rate classes on PSE's system. Second, the Settlement adopts the Commission Staff's proposal by applying increased revenues to only the demand and customer charges for Schedules 46 and 49. This results in a more cost-based rate design that sends more accurate price signals to customers on Schedule 49.[13/]

[13/] Docket Nos. UE-170033 and UG-170034, Testimony of Ali Al-Jabir in Support of the Settlement Agreement, September 18, 2017, page 2.

For the foregoing reasons, the FEA believes the Settlement results in rates that are just and reasonable and that the Settlement is in the public interest. Accordingly, the FEA urges the Commission to adopt the Settlement in its entirety.

CONCLUSION

The FEA respectfully requests that the Commission issue a final order in this proceeding that is consistent with the position set forth in this initial post-hearing brief. The FEA also requests all other relief at law or in equity to which it may be entitled.

Respectfully submitted,

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