

**BEFORE THE  
WASHINGTON UTILITIES AND TRANSPORTATION COMMISSION**

**WASHINGTON UTILITIES AND  
TRANSPORTATION COMMISSION,**

**Complainant,**

**v.**

**PUGET SOUND ENERGY,**

**Respondent.**

**Docket No. UE-170033  
Docket No. UG-170034  
(consolidated)**

**INITIAL BRIEF OF  
PUGET SOUND ENERGY**

**OCTOBER 18, 2017**

# PUGET SOUND ENERGY

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## I. INTRODUCTION

1. Puget Sound Energy (“PSE”) respectfully requests that the Commission approve (i) the Multi-Party Settlement Stipulation and Agreement (“Settlement Agreement”); (ii) PSE’s electric reliability plan (“ERP”) and PSE’s request for an electric cost recovery mechanism (“ECRM”) to improve reliability on PSE’s distribution system; (iii) continuation of the decoupling mechanisms with minor adjustments proposed by PSE; and (iv) PSE’s proposals with respect to the contested electric and natural gas cost of service, rate spread, and rate design issues.
2. The Settlement Agreement is an historic agreement that, among other things, addresses and resolves challenging issues regarding the Colstrip generating units (“Colstrip”) that the Commission and parties have grappled with for more than a decade. The ten parties joining the Settlement Agreement (“Settling Parties”)<sup>1</sup> have diverse interests, and yet they have come together, compromised, and reached agreement on a settlement that will benefit PSE, customers, the State, and the region. The Settlement Agreement is a carefully crafted compromise—each piece is vital to one or more of the Settling Parties. If provisions are removed or altered as Public Counsel proposes, the Settlement Agreement may unravel. The Settlement Agreement:
  - sets the depreciable life for Colstrip Units 3 and 4 at December 2027, advancing the current depreciable life by eighteen years, and responding to customer requests that PSE move away from coal-fired generation;
  - proposes a plan for funding (i) the decommissioning and remediation of the Colstrip units, (ii) recovery of the remaining Colstrip plant balances, and (iii) transition payments to the Colstrip community to assist with plant closures; and
  - responds to the Commission’s directive that PSE set forth a plan for decommissioning and remediation of Colstrip.

Remarkably, the Settling Parties have accomplished this, and much more, with less than a one percent increase in electric rates and nearly a four percent decrease in natural gas rates.

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<sup>1</sup> The Settling Parties are PSE, the Commission’s regulatory staff (“Commission Staff”), the Industrial Customers of Northwest Utilities (“ICNU”), NW Energy Coalition/Renewable Northwest/Natural Resource Defense Council (the “Coalition”), The Energy Project, Sierra Club, Federal Executive Agencies, The Kroger Co., the State of Montana, and Northwest Industrial Gas Users (“NWIGU”).

3. A foundational principle underlying the Settlement Agreement is intergenerational equity. This can be seen in the manner that Colstrip obligations are funded, treating both today's and tomorrow's customers fairly through the use of production tax credits ("PTCs"). It is also a key principle behind the environmental remediation amortizations in the Settlement Agreement.
4. With respect to the remaining contested issues, the ECRM responds to customers' desire for improved reliability and targets two key threats to electric reliability on PSE's distribution system—the failing high molecular weight ("HMW") cables and the worst performing circuits ("WPCs"). The ECRM models the Gas CRM, approved in 2013, which has functioned well. It is within the Commission's authority, and in the public interest, to approve the ECRM.
5. The Commission's approval of PSE's decoupling mechanisms in 2013 has furthered the State Energy Policy by removing the throughput incentive that otherwise exists for energy providers. The decoupling mechanisms have operated as intended, as the third-party review and other evidence demonstrates. PSE recommends continuation of the decoupling mechanisms with a few adjustments that allow the decoupling mechanisms to operate in a more balanced manner.
6. Finally, PSE has proposed reasonable positions with respect to the contested cost of service, rate spread, and rate design issues for electric and natural gas customers. PSE requests the Commission approve these for use in the current case. PSE will work with interested stakeholders in the workshops Staff has commenced to address these issues for future cases.

## **II. LEGAL STANDARD**

7. The ultimate legal question in a general rate case is whether the rates and charges proposed by a utility are fair, just, reasonable, and sufficient.<sup>2</sup> In making these determinations, the Commission is bound by the statutory and constitutional mandate that a regulated utility is entitled to (i) reasonable and sufficient compensation for the service it provides,<sup>3</sup> and (ii) the

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<sup>2</sup> RCW 80.28.020; *People's Org. for Wash. Energy Res. v. WUTC*, 104 Wn.2d 798, 808 (1985) (en banc) ("POWER").

<sup>3</sup> *POWER*, 104 Wn.2d at 808; *Puget Sound Traction Light & Power Co. v. Pub. Serv. Comm'n*, 100 Wn. 329, 334 (1918) (en banc); RCW 80.28.010(1).

opportunity to earn “a rate of return sufficient to maintain its financial integrity, attract capital on reasonable terms, and receive a return comparable to other enterprises of corresponding risk.”<sup>4</sup>

8. Washington law and Commission precedent strongly support and encourage “the resolution of contested issues through settlement when doing so is lawful and consistent with the public interest.”<sup>5</sup> In evaluating a proposed settlement, “[t]he Commission will approve settlements when doing so is lawful, the settlement terms are supported by an appropriate record, and when the result is consistent with the public interest in light of all the information available to the Commission.”<sup>6</sup> And, “in settlements, as in fully-litigated rate cases, the Commission must determine that the resulting rates are fair, just, reasonable, and sufficient, as required by state law.”<sup>7</sup> The Commission evaluates (i) whether any aspect of the proposal is contrary to law; (ii) whether any aspect of the proposal offends public policy; and (iii) whether “the evidence supports the proposed elements of the settlement as a reasonable resolution of the issues at hand.”<sup>8</sup> However, “[r]atemaking is not an exact science”<sup>9</sup> and settlements are “by nature compromises of more extreme positions.”<sup>10</sup> Settlement is appropriate where “the overall result in terms of revenue requirement is reasonable and well supported by the evidence.”<sup>11</sup>

9. In this case, nearly all of the parties have reached a Settlement Agreement that addresses most of the outstanding issues in this case, is well-supported by the evidence, and is in the public interest. Moreover, for the issues left unresolved through settlement—the ECRM, decoupling, certain cost of service, rate spread and rate design issues—the positions proposed by PSE set forth herein most equitably balance the benefits to the public and PSE’s right to earn a reasonable rate of return and should be approved.

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<sup>4</sup> *WUTC v. Avista Corp.*, Dockets UE-991606, *et al.*, Third Supp. Order ¶ 324 (Sept. 29, 2000).

<sup>5</sup> RCW 34.05.060; WAC 480-07-700, -740–750; *WUTC v. Cascade Natural Gas Co.*, Docket UG-060256, Order 05 ¶ 24 (Jan. 12, 2007) (internal citations omitted); *see also WUTC v. Verizon Northwest, Inc.*, Docket UT-061777, Order 01 ¶ 11 (June 30, 2008).

<sup>6</sup> *WUTC v. Avista Corp.*, Dockets UE-150204 & UG-150205, Order 05 ¶ 20 (Jan. 6, 2016).

<sup>7</sup> *Id.*

<sup>8</sup> *Id.* ¶ 21.

<sup>9</sup> *Cascade Natural Gas Co.*, Docket UG-060256, Order 05 ¶ 24 (internal citations omitted).

<sup>10</sup> *Id.*

<sup>11</sup> *Id.*

### **III. THE MULTIPARTY SETTLEMENT IS IN THE PUBLIC INTEREST AND SHOULD BE APPROVED**

#### **A. Introduction**

10. The Settlement Agreement addresses important issues for PSE, customers, the state, and the region and does so with a small rate increase on electric service and a decrease on gas service. The only party that testified against the terms of the Settlement Agreement is Public Counsel, whose testimony is unreasonable and not persuasive. In essence, Public Counsel’s “alternative viewpoint” accepts benefits the Settlement Agreement offers, but does not accept provisions that require compromise by Public Counsel. The Commission should approve the Settlement Agreement in its entirety, rather than cherry-picking elements, as Public Counsel proposes.

#### **B. Colstrip Issues Addressed in the Settlement Agreement**

11. One of the pivotal achievements of the Settlement Agreement is the manner in which the Colstrip Units 1-4 are addressed. The Settlement Agreement addresses and resolves the thorny issues of (i) depreciation expense and timing,<sup>12</sup> (ii) unrecovered plant balances,<sup>13</sup> (iii) decommissioning and remediation,<sup>14</sup> and (iv) transition issues for the Colstrip community related to the ultimate shutdown of the Colstrip units.<sup>15</sup> The Settling Parties compromised on the depreciation amounts for Colstrip Units 1-4 and on the assumed end of useful life dates for Colstrip Units 3 and 4. The Settling Parties agreed to repurpose hydro Treasury Grants and PTCs and apply the nearly \$400 million from these sources to fund decommissioning and remediation, unrecovered plant balances, and Colstrip transition, as described in more detail in the Settlement Agreement, with today’s customers experiencing only a minimal rate increase on the electric side of less than one percent. The Settlement Agreement also establishes reporting requirements and a transmission system operational study and transmission system workshop. Despite these

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<sup>12</sup> See Settlement Agreement at ¶¶ 24-26.

<sup>13</sup> See *id.* ¶¶ 25, 117.

<sup>14</sup> See *id.* ¶¶ 116-17.

<sup>15</sup> See *id.* ¶ 117.

impressive benefits, Public Counsel takes issue with several aspects of the Settlement Agreement as relates to Colstrip. These attacks on the Settlement should be rejected as discussed below.

### **1. Depreciation Life for Colstrip Units 3 and 4**

12. Public Counsel states that the December 31, 2027 depreciation schedule for Colstrip Units 3 and 4 “seems early” based on the ranges proposed in the litigated case.<sup>16</sup> Remarkably, Public Counsel, the representative of residential customers, ignores the numerous comments submitted by residential customers urging PSE to move away from coal-fired power even if there is additional cost associated with this move.<sup>17</sup> PSE faces continued pressure from residential customers, municipalities, and many commercial and industrial customers to move away from coal or to face loss of customers and service territory.<sup>18</sup> The business risks PSE faces are real, and the earlier depreciation life for Colstrip Units 3 and 4 helps to mitigate the risk. Although it is true that Colstrip Units 3 and 4 may not close by December 31, 2027, setting that date as the depreciable life provides a better opportunity for depreciation expense to be recovered, given the economic and political forces that make coal-fired generation less viable in the future. Public Counsel is in the awkward position of arguing for a longer depreciable life for Colstrip units, in the same case where the parties and the Commission must deal with the ramifications of Public Counsel’s position a decade ago that inaccurately predicted a longer life for Colstrip Units 1 and 2 and left PSE with significant unrecovered plant balances as a result.<sup>19</sup> Approving the Settlement Agreement will help to avoid a repeat of the Colstrip Units 1 and 2 predicament.

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<sup>16</sup> See McCullar, Exh. RMM-12T at 6:13-14.

<sup>17</sup> Public Comment Exh. BR 5; *see, e.g.*, K. Erickson email (strongly urging the UTC to set the depreciation schedule for PSE to pay off obligations to Colstrip coal plant as quickly as possible); D. Burger web comment (supporting 2022 decommissioning of Colstrip Units 1 and 2 and recommending 2025 decommissioning of units 3 and 4); W. Beattie Aug. 31, 2017 letter (fully supporting higher rates to implement 2025 transition away from Colstrip).

<sup>18</sup> *See, e.g., WUTC v. Puget Sound Energy*, Docket UE-161123, Final Order ¶ 58 (July 13, 2017) (approving special contract allowing retail wheeling for Microsoft and noting that “Microsoft’s primary motivation for obtaining power from providers other than PSE is to further Microsoft’s corporate clean energy goals”).

<sup>19</sup> *See* Barnard, KJB-17T at 15:8-16:12 (citing Public Counsel witness King, Exh. CWK-1T at 3, in Docket UE-072300, proposing a 60-year depreciable life for Colstrip, rather than the 44- and 45-year lives proposed by PSE).

## **2. The Use of PTCs is Appropriate**

13. The Settlement Agreement provides that monetized PTCs will be used first for community transition planning, second to offset unrecovered plant balances, and third for decommissioning and remediation. Public Counsel does not object to the use of PTCs, but argues they should be used first for decommissioning and remediation. PSE disagrees. First, a significant source of funding for decommissioning and remediation will be available to cover the majority of the estimated costs for Colstrip Units 1 and 2, before tapping into the PTCs. The Settlement Agreement provides that approximately \$95 million in Treasury Grants will be made available for Colstrip Units 1 and 2 decommissioning and remediation in a fund authorized by RCW 80.84.020.<sup>20</sup> This will nearly cover the current estimate of PSE's share of the cost for decommissioning and remediation of Colstrip Units 1 and 2, which is approximately \$110 million in real dollars.<sup>21</sup> Second, the unrecovered plant balances for Colstrip Units 1 and 2 will need to be addressed prior to decommissioning and remediation for Colstrip Units 3 and 4, even if the earliest retirement date proposed in this case for Colstrip Units 3 and 4—2025—were to occur. Finally, the use of funds for community transition planning was a key element to some Settling Parties and the allocated \$5 million is a small portion of the monetized PTCs.

### **C. The Depreciation Methodology Adopted in the Settlement Is Reasonable and Public Counsel's Unconventional and Outcome-Oriented Approach Should Be Rejected**

14. The Settlement Agreement accepts the depreciation study provided by PSE, with certain modifications relating to Colstrip. In contrast, Public Counsel asks the Commission to use the depreciation study of Public Counsel's expert witness, Roxie M. McCullar, but Ms. McCullar's study relies on unconventional depreciation methodologies designed to keep depreciation rates low today at the expense of tomorrow's customers. This is the same perspective that contributed

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<sup>20</sup> See Settlement Agreement at ¶ 116.

<sup>21</sup> See Roberts, Exh. RJR-1CT at 46:18-47:8, 54:1-166; Exh. RJR-23 at 2 (estimating \$6.7 million in decommissioning and \$103 million in remediation costs).

to the current unrecovered plant balances for Colstrip Units 1 and 2, which must be dealt with in this case.<sup>22</sup> Mr. Spanos testifies regarding the flaws in Ms. McCullar’s methodology.<sup>23</sup>

15. In addition, Ms. McCullar’s proposal to transfer a portion of the Colstrip Units 1 and 2 book reserves to other plant—specifically, combined cycle facilities—has several defects. The theoretical reserve she uses as a basis for this calculation has errors. For many of the PSE combined cycle plants, the vintages Ms. McCullar used to calculate the reserve imbalances were the acquisition dates rather than the dates the plants were placed in service.<sup>24</sup> More fundamentally, the net salvage estimates she relies on for these theoretical reserves are inconsistent with the manner in which the National Association of Regulatory Utility Commissioners (“NARUC”),<sup>25</sup> regulatory commissions around the country,<sup>26</sup> and authoritative depreciation texts,<sup>27</sup> calculate net salvage. Her proposed depreciation approach would either push out the recovery of depreciation for Colstrip Units 1 and 2 another 25 years after the units close, creating significant intergenerational inequities,<sup>28</sup> or it would create other under-recoveries.

16. Further, Ms. McCullar argues, unconvincingly, that the depreciation amounts in the Settlement Agreement are too close to the depreciation amounts in PSE’s direct filing,<sup>29</sup> but she ignores several key facts. First, although the depreciation expense for electric has only decreased \$298,823 from PSE’s direct filing, it also now includes higher depreciation expense for Colstrip Units 3 and 4 resulting from the shorter depreciable life that was not included in PSE’s filed case. This reflects the uncertainties that could shorten the lives of Colstrip Units 3 and 4.<sup>30</sup> Second, and more fundamentally, Public Counsel fails to understand the concept of a

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<sup>22</sup> See Barnard, Exh. KJB-17T 15:8-16:12.

<sup>23</sup> Spanos, Exh. JJS-4T at 12:1-14:2, 16:13-38:20.

<sup>24</sup> *Id.* at 16:14-17:13.

<sup>25</sup> See Spanos, Exh. JJS-4T at 22:1-23:25; McCullar, Exh. RMM-13X (NARUC Manual at 157).

<sup>26</sup> See, e.g., *In the Matter of the Application of Consumers Energy Company for Accounting Approval of Depreciation Rates for Gas Utility Plant*, Case No. U-15629, p. 12 (Mich. Pub. Serv. Comm’n Sept. 29, 2009).

<sup>27</sup> See Spanos, Exh. JJS-4T at 24:1-8; Barnard, Exh. KJB-56X (Wolf & Fitch, *Depreciation Systems* at 7, 261).

<sup>28</sup> See *id.* at 12:18-23.

<sup>29</sup> See McCullar, Exh. RMM-12T at 2:4-15.

<sup>30</sup> See Howell, Tr. 612:14-615:3.



compromise. In the Settlement Agreement, PSE compromised significantly on power costs, for example, where residential customers benefitted from a \$26 million reduction in power costs<sup>31</sup> from PSE's supplemental filing even though Public Counsel did not advocate for this adjustment in its litigated case. In contrast, for depreciation, the compromises were less significant in terms of overall decreases to revenue requirement because of the need to fund activities related to the Colstrip units. Public Counsel cannot focus on one adjustment only. The Settlement Agreement must be reviewed in its entirety.

**D. The Storm Damage Adjustment Is Reasonable**

17. The Settlement Agreement strikes a reasonable balance with respect to PSE's storm deferral mechanism. It allows PSE to amortize the storms that have been deferred under the existing catastrophic storm standard.<sup>32</sup> It adjusts the standard, going forward, to address concerns that too many storms are being deferred, while allowing PSE an automatic deferral for qualifying storms.<sup>33</sup> It resets the six-year average for normalized storm expense based on the most recent six years.<sup>34</sup> Public Counsel's objection appears to be that the Settlement Agreement does not accept Public Counsel's proposal to increase the amortization period to ten years for the January 2012 catastrophic storm, sometimes referred to as "Snowmageddon."<sup>35</sup> The negotiated six-year amortization period is reasonable. The deferred expense for this storm is approximately 60 percent of the Hanukkah Eve storm expense that was amortized over ten years.<sup>36</sup>

**E. The Compromise on SQI-5 Reflected in the Settlement Agreement Is Reasonable**

18. Public Counsel takes issue with the compromise metric for SQI-5 agreed to by the Settling Parties, which would require PSE's call center to answer 80 percent of calls within 60 seconds. This modifies the current SQI-5 metric, which was set two decades ago, when the

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<sup>31</sup> See Commission Staff, Exh. TES-4T at 13:1-21.

<sup>32</sup> See Settlement Agreement at ¶ 77.

<sup>33</sup> See *id.* ¶ 78.

<sup>34</sup> See *id.* ¶ 79.

<sup>35</sup> See Colamonici, Exh. CAC-1T at 11:3-7.

<sup>36</sup> See Barnard, Exh. KJB-17T at 68:8-13.

methods available to customers to contact PSE were very different than today. It is appropriate for the parties, in this case, to agree to an updated metric reflecting the fact that many of the more basic calls are now handled through automated systems such as Integrated Voice Response.<sup>37</sup> It is also reasonable for the Settling Parties to reach a compromise metric for SQI-5 that is consistent with the metric recently approved for Avista. Public Counsel was a party to the Avista collaborative process and agreed to the same metric in the Avista case that is included in the Settlement Agreement.<sup>38</sup> Public Counsel has failed to articulate any reason why PSE's standard should be more stringent than the standard set for Avista two years ago, particularly when, unlike Avista, PSE faces a \$1.5 million annual penalty for failure to comply with its standard.<sup>39</sup>

**F. Other Proposals By Public Counsel Are Unnecessary**

**1. Public Counsel Misconstrues the Purpose of the Get To Zero Initiatives**

19. Although PSE's filed case does not request Commission action with respect to its Get-To-Zero initiatives ("GTZ"), Public Counsel continues a false narrative that GTZ is intended to phase out PSE's call center. This false claim was rebutted by David Mills. "[T]he express goal of Get to Zero is to provide the customer with their preferred and simplified pathway to address their needs with PSE,"<sup>40</sup> but it does not involve phasing out the call center, as Public Counsel claims. PSE will continue to staff and maintain a fully functioning call center with trained and experienced agents to address customer issues.<sup>41</sup> Public Counsel's concerns that the call center will be eliminated are unfounded.

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<sup>37</sup> See Schooley, Tr. 606:19-607:18; see also Collins, Tr. 608:1-7.

<sup>38</sup> *WUTC v. Avista Corp.*, Dockets UE-140188 & UG-140189, Order 06 ¶ 5 (June 25, 2015).

<sup>39</sup> See *WUTC v. Puget Sound Energy*, Docket UE-072300, Order 29 ¶ 13 (June 17, 2016) (referencing amendment to SQI program in 2007 general rate case that increased penalties to \$1.5 million) *cf. Avista Corp.*, Dockets UE-140188 and UG-140189, Order 06 ¶¶ 13, 16-20 (declining to include penalties for Avista's service quality metric program).

<sup>40</sup> Mills, Exh. DEM-4T at 5:21-6:2.

<sup>41</sup> *Id.* at 5:19-21.

## 2. Outage Reporting Was Addressed in the 2016 SQI-3 Settlement

20. Public Counsel’s complaint that the Settlement Agreement does not mandate further notifications to customers regarding the need to report outages<sup>42</sup> is another Public Counsel solution in search of a problem. Just last year, Public Counsel, Staff and PSE engaged in settlement discussions addressing SQI-3 and part of that dialog addressed the need for customers to report outages in order to receive payments under the outage guarantee program. Commission Staff and PSE reached a settlement in that case (the “2016 SQI-3 Settlement”),<sup>43</sup> which the Commission approved. Now, Public Counsel seeks to revise terms that were approved just last year in the 2016 SQI-3 Settlement. As part of the 2016 SQI-3 Settlement, PSE committed to raise customer awareness of the service guarantees and the need for customers to report outages through customers communications on the topic,<sup>44</sup> and Public Counsel expressed satisfaction with that element of the 2016 settlement.<sup>45</sup> There is no need to revisit this issue one year later.

### G. The Settlement Agreement Sets Parameters for the Expedited Rate Filing

21. The Settlement Agreement provides that PSE may file one expedited rate filing (“ERF”) within one year after the effective date of the tariffs in this case.<sup>46</sup> Public Counsel acknowledges this aspect of the Settlement Agreement is a compromise from PSE’s litigated position and “moves in the direction” of Public Counsel’s testimony.<sup>47</sup> Even so, Public Counsel opposes the ERF and repeats the concerns it raised in response testimony, which were rebutted by PSE.<sup>48</sup> Notably, Public Counsel has reversed course from its position in 2013, when it opposed PSE’s multi-year rate plan and proposed multiple ERFs as an alternative.<sup>49</sup> Moreover, there is nothing

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<sup>42</sup> See Alexander, Exh. BRA-26T at 9:13-22.

<sup>43</sup> See *Puget Sound Energy*, Docket UE-072300, Order 29 ¶ 26.

<sup>44</sup> See Koch, Exh. CAK-4T at 23:6-21; Koch, Exh. CAK-6.

<sup>45</sup> See Koch, Exh. CAK-4T at 21:11-22:2; see *Puget Sound Energy*, Docket UE-072300, Order 29 ¶ 31.

<sup>46</sup> See Settlement Agreement at ¶ 115.

<sup>47</sup> See Brosch, Exh. MLB-11T at 7:4-7.

<sup>48</sup> See Barnard, Exh. KJB-17T at 92:16-98:18.

<sup>49</sup> See *In re PSE and NW Energy Coalition For an Order Authorizing PSE To Implement Electric and Natural Gas Decoupling Mechanisms and To Record Accounting Entries Associated With the Mechanisms*, Dockets UE-121697 & UG-130137, Order 07 ¶ 166 (June 25, 2013) (noting Public Counsel’s proposal allowing PSE to file up to two additional ERFs prior to its next general rate case).

in the Commission rules that would prohibit an ERF, provided that the filing is not seeking a rate increase of three percent or more and there is no request for a change in return on equity (“ROE”) or capital structure.<sup>50</sup> The Settlement Agreement simply sets parameters for the 2018 ERF.

22. Public Counsel complains about a lack of symmetry, as PSE can choose whether or not to file an ERF. However, this is true with most rate case filings; it is rare that a company is mandated to file a rate case. Moreover, there are other areas in rate regulation where asymmetry exists and works to the benefit of customers. For example, PSE’s earnings sharing mechanism requires PSE to share earnings in excess of PSE’s authorized rate of return, but does not require customers to pay higher rates when PSE fails to earn its authorized rate of return.<sup>51</sup>
23. Public Counsel also confuses attrition and the ERF. Public Counsel argues the ERF should be denied because PSE has not shown evidence of attrition. But the Settlement Agreement does not establish an attrition adjustment, and PSE did not seek such an adjustment in this case.<sup>52</sup> An attrition adjustment is forward looking, while the ERF is based on a historical test year.<sup>53</sup> It is not necessary for PSE to demonstrate attrition before filing an ERF.
24. Although Public Counsel argues that 120 days is too short of a time period for the ERF, the ten Settling Parties have agreed to this time period. PSE’s previous ERF was decided in approximately 150 days from the filed date, and it was combined with a contentious proposal for decoupling mechanisms and a rate plan.<sup>54</sup> In contrast to that case, the 2018 ERF filing will be straightforward, based on a Commission Basis Report, and will follow the same basic procedure as in 2013. The parameters set for the ERF are reasonable and should be approved.

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<sup>50</sup> See WAC 480-07-505(1).

<sup>51</sup> See Doyle, Exh. DAD-1T at 21:7-25:18.

<sup>52</sup> See Barnard, Tr. 580:6-581:3.

<sup>53</sup> See Barnard, Exh. KJB-1T at 72:17-73:5 (noting ERF incorporates the Commission’s preferred historical ratemaking approach using known and measurable costs, in contrast to an attrition adjustment that estimates the attrition that will occur between the test year and the rate year based on historical trends).

<sup>54</sup> See Barnard, Tr. 578:7-18.

25. The Settlement Agreement provides that the ROE adjudicated in this case will be held constant for the ERF,<sup>55</sup> and this provision is consistent with past Commission orders and Washington law that allows the Commission to maintain the existing cost of capital for two years following adjudication.<sup>56</sup> Holding the ROE constant, as well as excluding pro forma adjustments and limiting restating adjustments to those approved by the Commission, will allow for an expedited procedure and will protect customers since the majority of pro forma adjustments tend to increase the revenue requirement.<sup>57</sup> Finally, the use of end of period rate base for the 2018 ERF is reasonable and consistent with past practice.

#### **H. The Cost of Capital Is a Reasonable Compromise Supported By the Evidence**

26. There is substantial evidence in this case supporting the cost of capital agreed to in the Settlement Agreement. The Commission has a full record before it from which it can determine that the 9.50 percent ROE is within the range of reasonableness. Using various methodologies, Dr. Morin's ROE estimates range from 9.3 percent to 10.7 percent.<sup>58</sup> Staff witness Mr. Parcell recommends an ROE between 8.85 percent and 9.5 percent, and under his comparable earnings ("CE") methodology for determining ROE, he estimated a ranges of 9.0 percent to 10.0 percent.<sup>59</sup> The current ROE for Avista and PacifiCorp are also set at 9.5 percent.<sup>60</sup> The average allowed ROE authorized by state utility commissions for electric utilities in 2017 is 9.9 percent.<sup>61</sup> Although the ROE range proposed by Mr. Woolridge is much lower, his

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<sup>55</sup> Settlement Agreement, Exh. I.

<sup>56</sup> See *WUTC v. PacifiCorp d/b/a Pac. Power & Light Co.*, Dockets UE-140762, *et al.*, Order 08 ¶ 181 (Mar. 25, 2015) (relying on RCW 80.04.200 and declining to adjust the equity ratio and rate of return when the Commission had decided this issue five months before the filing of the current case); *see also US West Commc'ns, Inc. v WUTC*, 134 Wn.2d 74, 105 (1997) (it is within the Commission's discretion under RCW 80.04.200 to decide whether to rehear issues within a two year stay-out period following their adjudication).

<sup>57</sup> Barnard, Tr. 577:12-16.

<sup>58</sup> See Morin, Exh. RAM-12T at 96:13-15.

<sup>59</sup> See Parcell, Exh. DCP-1T at 3:19-4:5; See Morin, Exh. RAM-12T at 82. When corrected for errors, Mr. Parcell's actual range using the DCF, CAPM and CE is between 9.0 and 10.0. *See id.* at 82:1-6.

<sup>60</sup> *WUTC v. Avista Corp.*, Dockets UE-160228 & UG-160229, Order 06 ¶ 67 (Dec. 15, 2016); *WUTC v. PacifiCorp d/b/a Pac. Power & Light Co.*, Docket UE-152253, Order 12 ¶¶ 9, 310 (Sept. 1, 2016).

<sup>61</sup> See Morin, Exh. RAM-12T at 7:21-8:1.

methodologies have been found to be unreasonably low in other jurisdictions.<sup>62</sup> For example, he recommended an ROE of 8.80 percent in 2017 in a proceeding for Gulf Power Company in Florida, and the Florida Commission authorized an ROE of 10.25 in that case.<sup>63</sup> In 2016 he estimated the ROE for Delmarva Power Company to be 8.60 percent, but the Maryland Commission authorized a 9.60 ROE in that case.<sup>64</sup>

### **I. Public Counsel’s Remaining Objections to the Settlement Agreement Lack Merit**

27. Public Counsel raises several miscellaneous complaints about the Settlement Agreement, all primarily focused on the fact that the Settlement Agreement does not accept Public Counsel’s litigated position. With respect to pension plan expense, Ms. Barnard’s rebuttal testimony demonstrates that PSE’s approach, which was accepted in the Settlement Agreement, follows the long-held regulatory treatment of using a four-year average of cash contributions for setting rates and is the appropriate methodology.<sup>65</sup> There is not a compelling reason to alter this approach.
28. Regarding environmental remediation, the Settling Parties used PSE’s adjustment for both electric and natural gas, which applies a portion of the insurance recoveries to current costs and holds a portion of these recoveries for future costs, which are certain to be incurred as part of the ongoing cleanup at several sites.<sup>66</sup> Public Counsel’s view that 100 percent of the proceeds recovered from insurance carriers and third parties should offset the costs incurred as of September 30, 2016<sup>67</sup> disregards the fact that many of these recoveries were obtained through insurance buybacks and settlements and are expressly agreed to cover all past, present, and

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<sup>62</sup> See, e.g., *In the Matter of Application by Virginia Elec. & Power Co., d/b/a Dominion N. Carolina Power, for Adjustment of Rates & Charges Applicable to Elec. Util. Serv. in N. Carolina*, Docket No. E-22, Sub 532, at 98-99 (N.C. Util. Comm’n Dec. 22, 2016) (determining that Mr. Woolridge’s conclusion is “outside the bounds of reasonableness” and that his proposal “would put the Company at a significant disadvantage in competitive capital markets when attempting to raise capital needed to fund its operations”).

<sup>63</sup> *In re Petition for Rate Increase by Gulf Power Co.*, 337 P.U.R.4th 233, Docket 160186-EI, Order No. PSC-17-0178-S-EI (Fl. Pub. Serv. Comm’n May 16, 2017).

<sup>64</sup> *In re Application of Delmarva Power & Light Co. for Adjustments to Its Retail Rates for the Distribution of Electric Energy*, Docket 9424, Order No. 88033 (Md. Pub. Serv. Comm’n Feb. 15, 2017).

<sup>65</sup> See Barnard, KJB-17T at 38:16-47:20.

<sup>66</sup> See Exh. PSE-1JT at 9:9-16; Rork, JKR-1T at 10:15-16. For a detailed description of the allocation methodology, see Free, Exh. SEF-1T at 24:16-26:4.

<sup>67</sup> See Colamonici, Exh. CAC-1T at 10:9-14 (citing Smith, Exh. RCS-1CT at 65:5-7).

future clean-up costs.<sup>68</sup> Public Counsel’s position would harm future customers who would be required to pay the costs of the future environmental remediation without any offset from these recoveries that are intended to cover future costs as well as past costs.<sup>69</sup> The Settlement Agreement provides for this issue to be addressed through a collaborative process to determine a methodology for allocating recoveries that does not compromise PSE’s litigation position in future cases.<sup>70</sup>

29. Public Counsel persists in arguing for the removal of two properties in Plant Held For Future Use. PSE demonstrated that the particular transmission line upgrade for which the properties were required is anticipated to be in place by 2019. The project timeline was extended due to the transition of service territory to the Jefferson County Public Utility District in 2013.<sup>71</sup>

30. The Settlement Agreement provides that “PSE will participate in a collaborative with Commission Staff and other interested stakeholders to discuss the future of the water heater rental program . . . .”<sup>72</sup> Although Public Counsel did not take a position on this issue in its response testimony, Public Counsel now argues that the water heater rental program should be discontinued and that a collaborative process is not necessary. Public Counsel relies on the litigation position of Commission Staff, prior to settlement, in which Commission Staff testified that from its perspective, there was no longer a legitimate reason for the program to exist.<sup>73</sup> Public Counsel ignores the PSE testimony rebutting Commission Staff’s testimony and discussing the legitimate and important reasons why the water heater program should continue.<sup>74</sup> The decision to hold a collaborative process to consider the future of the water heater rental program is a reasonable and appropriate compromise of positions in this case.

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<sup>68</sup> See Exh. PSE-1JT at 9:9-10:2; Free, Exh. SEF-12T at 18:16-19:11, 21:3-22:3.

<sup>69</sup> See Exh. PSE-1JT at 9:9-10:2; Free, Exh. SEF-12T at 18:16-19:11, 21:3-22:3.

<sup>70</sup> See Exh. PSE-1JT at 10:3-12.

<sup>71</sup> See Barnard, Exh. KJB-17T at 83:3-10.

<sup>72</sup> Settlement Agreement at ¶ 123.

<sup>73</sup> See Colamonici, Exh. CAC-1T at 14:19-15:7.

<sup>74</sup> See, generally, Einstein, Exh. WTE-1T.

**J. The Contingent Calculations For the PCA Baseline Rate and Decoupling Should Be Approved**

31. Two contingent calculations have been provided in this case to reflect the future scenario in which Microsoft takes service under Schedule 451: (i) a contingent PCA baseline rate, and (ii) a contingent allowed revenue per customer calculation. The need for these contingent calculations and the method of calculation is discussed in Mr. Piliaris's testimony.<sup>75</sup> Paragraph 92 and Exhibit H to the Settlement Agreement set forth the PCA baseline rate that will be in effect once the Settlement Agreement is approved. It also provides (i) the PCA baseline rate that will result once Microsoft takes service under a special contract, and (ii) the calculation of the impact on Schedule 95 rates that would occur in a filing to be made once Microsoft takes service under the special contract. Paragraph 98 of the Settlement Agreement provides that when Microsoft is removed from Schedule 40, the allowed revenue per customer for other schedules will be recalculated consistent with the contingent allowed revenue calculations in Exhibit JAP-43. The Commission should approve these contingent calculations.

**IV. ELECTRIC COST RECOVERY MECHANISM**

32. To better serve its customers and improve its reliability, PSE has proposed the ERP and ECRM, by which PSE will aggressively and conclusively address two aspects of its electric distribution system that have been plagued by unreliability for decades—HMW cables and the WPCs. Patterned after the existing Gas CRM, the ECRM would provide PSE an efficient and transparent mechanism by which PSE could more quickly recover capital investments made to address HMW cables and the WPCs in a manner and speed not currently possible under PSE's existing capital budgets and under traditional ratemaking principles. The ERP and ECRM will allow PSE to accelerate the resolution of these reliability issues, which will benefit customers. While the other parties to this case have objected to PSE's ECRM proposal, the overwhelming need and benefits to this program demonstrate that the program is in the public interest and PSE respectfully requests that the Commission approve of the ECRM.

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<sup>75</sup> See Piliaris, Exh. JAP-1T at 151:17-156:18.



**A. PSE Has Addressed Reliability Issues Associated With HMW Cable and the WPCs For Decades But Has Been Unable To Adequately Resolve The Issues**

**1. PSE Has Been Repairing and Replacing Failing HMW Cable, But Without Accelerated Spending, the Failure Rate Will Exceed the Replacement Rate**

33. PSE first installed HMW cable in the mid-1960s and approximately 4,800 miles of cable was installed throughout PSE's service territory until about 1985.<sup>76</sup> By the mid-1980s, PSE discovered that HMW cable installed prior to 1982 was susceptible to the formation of "water trees" which allowed groundwater to migrate into the conductor causing cable failures.<sup>77</sup> The industry now recognizes that the failure of these cables is generic to all HMW cables installed during this time and utilities across the nation have implemented cable replacement programs.<sup>78</sup>

34. In 1988, the HMW cable was failing in 17 years, with failure rates of 25 failures per 100 miles.<sup>79</sup> Since 2011, HMW cable failure rate has increased significantly. Between 2011 and 2013, PSE experienced a four percent failure rate, and between 2013 and 2015, the failure rate had doubled to eight percent.<sup>80</sup> In comparison to the cable failure rate in 1988, in 2015, the failure rate for HMW cable had doubled to more than 50 failures per 100 miles.<sup>81</sup> This rate has increased dramatically, despite PSE spending over \$100 million alone on replacing underground cable from 2011 through September 2016.<sup>82</sup> Today, PSE experiences about 1,000 underground cable failures per year, of which 95 percent are caused by failing HMW cable.<sup>83</sup>

35. In 1990, PSE began addressing the failing HMW cable through a variety of methods.<sup>84</sup> PSE attempted to address failing cable by repairing failed sections or by injecting the cable with silicone to extend the cable's life.<sup>85</sup> However, repairing the cable and using silicone injections

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<sup>76</sup> Koch, Exh. CAK-3C at 1.

<sup>77</sup> *Id.*

<sup>78</sup> *Id.* at 3.

<sup>79</sup> *Id.* at 2.

<sup>80</sup> Koch, Exh. CAK-1CT at 13:19-20; Koch, Exh. CAK-3C at 2.

<sup>81</sup> Koch, Exh. CAK-3C at 2-3.

<sup>82</sup> Koch, Exh. CAK-1CT at 15:3-5.

<sup>83</sup> Koch, Exh. CAK-3C at 2.

<sup>84</sup> Koch, Exh. CAK-1CT at 13:19-21.

<sup>85</sup> Koch, Exh. CAK-3C at 3.

has proven to be ineffective over the long term leaving replacement as the only viable option.<sup>86</sup> Over the course of the last 25 years, PSE has successfully replaced or injected approximately 2,500 miles of failing HMW cable, leaving approximately 1,800 miles to be replaced.<sup>87</sup>

36. PSE has tracked cable failures by type and year to aid in the estimation of remaining useful life to calculate failure rates in two scenarios: (i) replacement of the failing cable at an accelerated pace as proposed in the ERP or (ii) continued replacement at historical levels.<sup>88</sup> Using a conservative linear failure rate of four percent, PSE estimates that under the ERP spending model, the failure rate of over 1,000 failures per year will reduce to less than 400 per year by 2026; whereas if accelerated spending does not occur and replacement remains at historical levels, the failure rate will *increase* to approximately 1,600 failures per year.<sup>89</sup>

37. Under PSE's current reliability capital spending model, HMW cable replacement is occurring, but not at the accelerated pace that PSE is proposing with the ERP. PSE's capital budget is impacted by a variety of factors, including cash flow from operations, debt equity, and other capital demands on PSE's system.<sup>90</sup> While PSE anticipates spending approximately \$78 million in 2017 to address both WPCs and HMW cables, PSE undertook this level of spending anticipating the approval of the ECRM, and this amount is unsustainable over the long term without the ECRM.<sup>91</sup> At the historical pace of approximately 50-70 miles of underground cable replacement each year, replacement will not occur for approximately 25 years.<sup>92</sup> During this time, failure rate of existing cable will continue to increase exponentially, significantly increasing the level of unreliability on PSE's electric distribution system.

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<sup>86</sup> Koch, Exh. CAK-1CT at 14:3-8.

<sup>87</sup> *Id.* at 13:19-21.

<sup>88</sup> Koch, Exh. CAK-3C at 4-5.

<sup>89</sup> *Id.*

<sup>90</sup> Doyle, Exh. DAD-7T at 26:4-21; Doyle, Tr. 172:8-173:14.

<sup>91</sup> Koch, Exh. CAK-4T at 10:9-15; Doyle, Exh. DAD-7T at 23:14-19.

<sup>92</sup> Koch, Exh. CAK-1CT at 13:26-14:2.

**2. Reliability Issues Related to the WPCs Are Not Being Addressed Fast Enough Because It is Not Cost-Effective in Comparison to Other Reliability Demands**

38. PSE has over 1,100 distribution circuits.<sup>93</sup> While PSE is consistently working to ensure that all distribution circuits meet PSE’s reliability standards, about 10 percent of PSE’s circuits—its WPCs—are impaired by an increased level of reliability problems as demonstrated by having the most customer minute interruptions.<sup>94</sup> Since 2011, 90 circuits have appeared on one or more of the annual list of WPCs, and PSE has developed various strategies to improve the reliability issues associated with those circuits,<sup>95</sup> investing approximately \$50 million on reliability improvement.<sup>96</sup> While efforts to address the WPCs have been moderately successful,<sup>97</sup> conclusively resolving all reliability issues with the WPCs has been difficult for several reasons.

39. As noted above, PSE’s capital reliability spending budget has limitations and, like any business, PSE is obligated to optimize its capital resources and manage its spending as efficiently as possible. As explained by the Commission, “PSE’s management [must] make the right decisions to aggressively control the Company’s earnings expectations and expenses, limit discretionary spending, and ensure that its capital investments are prudent.”<sup>98</sup> In order to most efficiently utilize PSE’s capital reliability budget, PSE’s reliability planning utilizes an optimization tool, “iDOT,”<sup>99</sup> which compares the relative costs and benefits (e.g. reliability, safety, external stakeholder input) of various reliability solutions.<sup>100</sup> Total value is optimized across the entire portfolio of electric and gas infrastructure projects, which results in a set of capital projects that provides maximum value to PSE’s customers and stakeholders.<sup>101</sup>

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<sup>93</sup> *Id.* at 15:10; Koch, Exh. CAK-3C at 8.

<sup>94</sup> Koch, Exh. CAK-1CT at 12:9-19, 15:10-15; Koch, Exh. CAK-3C at 9.

<sup>95</sup> Koch, Exh. CAK-3C at 8.

<sup>96</sup> *Id.* at 9.

<sup>97</sup> *Id.*

<sup>98</sup> *WUTC v. Puget Sound Energy*, Docket UE-111048, Order 8 ¶ 19 (May 7, 2012).

<sup>99</sup> Investment Decision Optimization Tool.

<sup>100</sup> Koch, Exh. CAK-1T at 4:12-5:1.

<sup>101</sup> *Id.*

40. While PSE's system optimizes reliability resources for the greatest number of customers, it necessarily places a lower priority on reliability problems that benefit fewer customers with higher cost.<sup>102</sup> WPCs are characterized by circuits in remote locations, with a low number of customers, and that tend to be in heavily-treed areas.<sup>103</sup> The cost to access, repair and improve reliability problems associated with these areas is high in comparison to the low number of customers.<sup>104</sup> As a result, PSE's prioritization process allocates less resources to these circuits than circuits with a greater number of customers and where costs to repair are lower.<sup>105</sup> While reliability investments are frequently made on the WPCs, the investment is typically insufficient to fully resolve reliability problems and tends to focus more on reactive repair rather than anticipatory replacement.<sup>106</sup> Thus, although PSE has invested millions to improve reliability on the WPCs, the spending has not been significant enough or fast enough given PSE's other reliability obligations that score much higher in optimizing value to PSE's customers.

41. Were PSE to readjust its optimization paradigm away from maximizing value to the most customers, it would affect PSE's ability to meet its reliability obligations to a majority of its customers and could call into question the prudence of PSE's reliability spending decisions.<sup>107</sup> The ERP and ECRM allow these targeted areas of demonstrated need—HMW cables and the WPCs—to be funded and fully addressed at an accelerated pace, even though they would be prioritized lower than other reliability demands using the optimization model.<sup>108</sup>

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<sup>102</sup> Koch, Exh. CAK-3C at 9; Koch, Tr. at 221:14-224:24.

<sup>103</sup> Koch, Exh. CAK-3C at 9-10.

<sup>104</sup> Koch, Tr. at 221:14-224:24.

<sup>105</sup> Koch, Exh. CAK-3C at 9; Doyle, Tr. at 180:9-181:4, 221:14-224:24; Koch, Exh. CAK-4T at 2:20-3:4.

<sup>106</sup> Koch, Exh. CAK-3C at 9; Doyle, Tr. at 180:9-181:4.

<sup>107</sup> Koch, Tr. at 221:14-224:24.

<sup>108</sup> Doyle, Tr. at 181:5-183:5.

**B. The ERP and ECRM Will Promote the Public Interest By Improving Reliability For Customers Served By HMW Cable and WPCs Beyond Historical Levels In a Manner That Cannot Be Accomplished Through Traditional Ratemaking**

**1. Traditional Ratemaking Principles Discourage Utilities from Investing in Non-Revenue Generating Distribution Plant that Exceeds Customer Growth**

42. In past cases, the Commission and stakeholders have questioned spending on non-revenue generating distribution plant, when the spending exceeded customer growth rates.<sup>109</sup> The level of spending PSE is proposing through the ECRM to accelerate replacement of HMW cables and for work on the WPCs is significant and exceeds the revenue currently generated from customer growth.<sup>110</sup> Thus, without Commission authorization of a mechanism and plan allowing for accelerated spending, PSE would not engage in the level of spending proposed in the ERP.<sup>111</sup>

43. Given these limitations under traditional ratemaking principles, PSE's investment in HMW cables and the WPCs has been limited to making more moderate investments that typically take the form of either repair or limited replacement.<sup>112</sup> This results in a more reactive approach to reliability spending instead of a proactive replacement strategy that typically requires greater up front capital investment. For HMW cable replacement, for example, this would take the form of a prolonged replacement program that would likely achieve cable replacement in approximately 25-30 years.<sup>113</sup> And for the WPCs, PSE would continue to invest in these circuits by repairing damaged distribution systems as needed or what may be viewed by customers as "band-aids," rather than make the significant capital expenditures necessary to fully address the reliability problems associated with these circuits.<sup>114</sup>

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<sup>109</sup> See, e.g., *Avista Corp.*, Dockets UE-150204 & UG-150205, Order 05 at ¶ 116; Koch, Exh. CAK-4T at 4:3-14.

<sup>110</sup> Koch, Exh. CAK-4T at 4:5-7.

<sup>111</sup> *Id.* at 4:1-14.

<sup>112</sup> Koch, Exh. CAK-4T at 6:11-22; Koch, Exh. CAK-3 at 1-6; Doyle, Tr. 180:9-181:14; Koch, Tr. 207:9-209:22.

<sup>113</sup> Koch, Exh. CAK-1CT at 13:17-14:8; Koch, Exh. CAK-10:9-11; Doyle, Tr. 182:14-21; Koch, Tr. 209:3-10.

<sup>114</sup> Koch, Tr. 207:9-209:22; Koch, Exh. CAK-4T at 2:8-3:8, 6:1-22, 15:1-16:14.

## 2. Traditional Ratemaking Delays Recovery of Capital Expenses

44. In addition to limiting capital spending to correspond to customer growth, traditional ratemaking based on a historical test year delays recovery of capital expenses when utilities invest in capital-intensive programs between rate cases. For example, under traditional ratemaking, from the time of incurring costs to the time those costs will start to be recovered in rates could take as long as 27-30 months.<sup>115</sup> While a certain amount of regulatory lag is intrinsic to traditional ratemaking,<sup>116</sup> regulatory lag is magnified when utilities incur significant capital expenditures or other significant costs without the ability to reasonably and efficiently recover those costs.<sup>117</sup> Excessive regulatory lag can have harmful collateral impacts as utilities are constantly struggling to recover their investments. As explained by the Commission:

The Commission historically has tolerated some degree of regulatory lag in its ratemaking practice, recognizing that it is a factor in encouraging utilities to operate efficiently. During recent periods, however, the impacts of regulatory lag on the ability of PacifiCorp and other utilities to earn their authorized revenue requirements have contributed to what the Commission has described as a “current pattern of almost continuous rate cases.”

This pattern of one general rate case filing following quickly after the resolution of another is overtaxing the resources of all participants and is wearying to the ratepayers who are confronted with increase after increase. This situation does not well serve the public interest and we encourage the development of thoughtful solutions.

....

[R]egulatory lag “has long been a concern of both the utilities and their regulators” that can have a “deleterious effect,” and that “as regulators we have the responsibility to mitigate that effect to the extent possible.”<sup>118</sup>

45. Under the ERP, PSE faces a massive and long-term capital expenditure program to replace failing HMW cable and to adequately resolve the problems associated with the WPCs. If PSE relies on traditional ratemaking to implement the ERP, it will face ongoing earning erosion

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<sup>115</sup> Barnard, Exh. KJB-17T at 100:3-101:2; Koch, Exh. CAK-4T at 3:9-18; Barnard, Tr. 250:10-252:3.

<sup>116</sup> *WUTC v. PacificCorp d/b/a Pac. Power & Light Co.*, Docket UE-130043, Order 05 at ¶ 181 (Dec. 4, 2013).

<sup>117</sup> See Barnard, Exh. KJB-17T at 100:3-101:2; Doyle, Exh. DAD-7T at 24:1-5.

<sup>118</sup> *PacificCorp d/b/a Pac. Power & Light Co.*, Docket UE-130043, Order 05 ¶¶ 181, 183.

due to regulatory lag, which is harmful to the Company.<sup>119</sup> The Commission has recognized this problem and that it has a duty to assist utilities in mitigating the effects of earning erosion:

We must also recognize that regulatory lag (the interim period elapsing between the filing of a rate case and its ultimate disposition) has long been a concern of both the utilities and their regulators, and regulatory lag may tend to erode the earnings of a utility. If regulatory lag has a deleterious effect, it is difficult to compensate for its overall adverse effect. However, as regulators we have the responsibility to mitigate that effect to the extent possible.<sup>120</sup>

46. PSE estimates that the financial impact associated with implementation of just its 2017-18 planned investment, absent the ECRM, will be approximately \$20 million due to the 27-month regulatory lag associated with a general rate case filing.<sup>121</sup>

### **C. The Commission Has the Authority to Approve the ECRM**

47. It is beyond dispute that the Commission has the authority to approve the ECRM. The Commission's statutory authority gives it ample discretion to adopt alternative ratemaking principles when it determines that doing so is in the public interest and that resulting rates are fair, just, reasonable, and sufficient.<sup>122</sup> The Commission need only be convinced that the record is sufficient to show that the potential advantages from a proposal such as the ECRM outweigh the potential disadvantages.<sup>123</sup> Indeed, the Commission has previously approved of alternative cost recovery mechanisms under a variety of circumstances including power cost adjustments, decoupling mechanisms, conservation riders, and REC trackers. These are only a few examples.

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<sup>119</sup> Koch, Exh. CAK-4T at 3:12-14; Barnard, Exh. KJB-17T at 100:3-101:2; Doyle, Exh. DAD-7T at 23:11-24:5; Doyle, Tr. 175:1-176:3, 181:15-182:5.

<sup>120</sup> *WUTC v. Wash. Natural Gas Co.*, Docket U-80-111, Third Supp. Order (Sept. 24, 1981).

<sup>121</sup> Koch, Exh. CAK-4T at 15-18; Barnard, Exh. KJB-17T at 100:19-101:2.

<sup>122</sup> RCW 80.28.020; *POWER*, 104 Wn.2d at 808.

<sup>123</sup> See, e.g., RCW 80.01.040 (duty to regulate in the public interest); RCW 80.28.020 (duty to establish just, reasonable, compensatory rates); see also, e.g., *In re Avista Corp.*, Docket UG-060518, Order 04 ¶¶ 19-20 (Feb. 1, 2007) (addressing Public Counsel's concern that decoupling proposal would violate matching principle through single-issue ratemaking and observing that, "[c]onsidering these concerns, we must examine carefully the stipulated proposal to determine whether the record is sufficient to prove the potential advantages from decoupling outweigh its potential disadvantages in this case"); *WUTC v. Puget Sound Power and Light Co.*, Docket U-81-41, Sixth Supp. Order (Dec. 19, 1988) (stating that test for propriety of recovering past expenses in true up mechanism for future rates "is not whether it constitutes retroactive ratemaking—it does not—but whether there are sound policy and evidentiary reasons for exercising the Commission's judgment to do so").

Perhaps most significantly, the Commission’s recent approval of the Gas CRM provides an example of a similar mechanism approved by the Commission.

48. Moreover, in recent years, alternative ratemaking mechanisms to recover costs for infrastructure improvements have become increasingly common as utilities seek to improve electric reliability, implement particular public policy goals, and increase efficiency in recovering capital spending. For example, in 2013, the Public Service Commission of Maryland approved of an “Electric Reliability Investment” initiative by Baltimore Gas & Electric (“BGE”) in order to “accelerate reliability improvements to BGE’s electric distribution system,” aimed at improving reliability associated with the utility’s “poorest performing feeders . . . due to vegetation, wildlife, and conductor and equipment failure,”<sup>124</sup> replacing various distribution lines, selective undergrounding of failing overhead lines, and various substation reliability performance improvements.<sup>125</sup> Like the proposed ECRM, it operated as “a separate charge from base rates, enabling the Company to receive a portion of cost recovery on a contemporaneous basis.”<sup>126</sup> BGE proposed the mechanism “in order to realize reliability benefits for customers in a shorter timeframe than would have been attained otherwise.”<sup>127</sup>

49. In sum, “[c]ircumstances in the industry today and modern regulatory practice . . . have led to a proliferation of risk reducing mechanisms being in place for utilities throughout the United States.”<sup>128</sup> What was “traditional” decades ago has changed due to reductions in customer growth and energy consumption. This has reduced utility revenues, forcing utilities and regulators to evolve from traditional ratemaking practices to cost recovery systems that are more flexible and responsive to utility needs while still ensuring utilities operate prudently and

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<sup>124</sup> *In the Matter of the Application of Baltimore Gas & Elec. Co. for Adjustments to Its Elec. & Gas Base Rates*, Case No. 9326, Order No. 86060, at 114 (Md. Pub. Serv. Comm’n Dec. 13, 2013).

<sup>125</sup> *Id.* at 111-112.

<sup>126</sup> *Id.* at 112.

<sup>127</sup> *Id.* at 112-13.

<sup>128</sup> *In re PSE and NW Energy Coalition For an Order Authorizing PSE To Implement Electric and Natural Gas Decoupling Mechanisms and To Record Accounting Entries Associated With the Mechanisms*, Dockets UE-121697 & UG-130137, Order 15 ¶ 155 (June 29, 2015).



efficiently.<sup>129</sup> The Commission has authority to approve the ECRM if it determines that the ERP and ECRM will benefit customers and are in the public interest.

**D. The ERP and ECRM Will Provide Significant Customer Benefits**

**1. Addressing the HMW Cable and WPCs Will Provide Significant and Immediate Reliability Benefits to Customers**

50. PSE's mission is to provide a safe, dependable and reliable service to all PSE customers.<sup>130</sup> The ERP and ECRM will provide significant benefits to customers by allowing PSE to accelerate its spending on HMW cables and WPCs. For a minimal increase to rates, the ERP and ECRM will conclusively eliminate the HMW cable failure problems that have been worsening exponentially for decades and can fully address WPC reliability problems that have been difficult for PSE to adequately resolve.<sup>131</sup> Importantly, the ERP and ECRM do not require more funds than if PSE proceeded at historical levels; rather, PSE is simply asking for accelerated recovery so that it can complete the HMW cable replacement sooner and focus concentrated resources directly on the WPCs.

51. Because cable failure rates exceed PSE's historical replacement rate, the only way PSE can protect customers from failing HMW cable is through a proactive and aggressive replacement policy.<sup>132</sup> Through the ERP and ECRM, PSE will accelerate PSE's spending on replacing the failing cable so that instead of replacing only 50-70 cable miles per year, PSE will nearly double cable replacement to approximately 160-195 cable miles per year.<sup>133</sup> This will allow PSE to complete the remaining 1,800 miles of failing cable in 10 years instead of 25-30 years.<sup>134</sup> PSE will eliminate approximately 195,000 customer interruptions based on actual historical performance, and Ms. Koch provides the cost estimates for this work.<sup>135</sup> By

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<sup>129</sup> See, e.g., *WUTC v. Puget Sound Energy*, Dockets UE-151871 & UG-151872, Order 06 ¶¶ 20-23 (Nov. 16, 2016).

<sup>130</sup> Koch, Exh. CAK-3C at 7.

<sup>131</sup> Koch, Exh. CAK-1CT at 12:20-13:16; Koch, Tr. at 209:3-10.

<sup>132</sup> Koch, Exh. CAK-4T at 2:18-20.

<sup>133</sup> Koch, Exh. CAK-1CT at 13:23-14:2; Koch, Exh. CAK-3C at 5.

<sup>134</sup> Koch, Exh. CAK-3C at 5-6.

<sup>135</sup> Koch, Exh. CAK-1CT at 17:22-18:1; Koch, Exh. CAK-3C at 6.

accelerating the rate of cable replacement, it will effectively eliminate HMW non-injected cable-related outages to zero over 10 years, significantly increasing PSE's electric reliability.<sup>136</sup>

52. The direct benefits for customers are substantial. The new cable system will be more resilient to deterioration and dig-ins, which improves reliability for customers, results in fewer long outages, less disruption due to power outages, and enhances public safety.<sup>137</sup> The benefits of replacing cable will result in immediate improvements to reliability. In 2017, PSE has estimated that the total customer minute interruptions will be approximately 2.7 million stemming from 86,000 customer interruptions due to failed cable.<sup>138</sup> By 2018, after implementing the ERP, the historical failure impacts from the replaced cable will be reduced by 22,000 customer interruptions, totaling 0.77 million customer interruption minutes.<sup>139</sup> Over the next two years, replacing the failing cable at an accelerated paced will reduce PSE's SAIDI minutes by an average of 1.5 minutes per year.<sup>140</sup>

53. Under the ERP and ECRM, PSE will replace both failed cables and failure prone cables simultaneously, thus improving its efficiency, controlling costs, and minimizing construction related services outages, traffic, and construction inconveniences.<sup>141</sup> Overall, customers will experience shorter outages as customers are generally impacted more by underground cable failures than overhead equipment failures because underground failures result in a 57 percent longer outage period than an overhead equipment failure.<sup>142</sup> The accelerated cable replacement will also reduce the number of future outages caused by failing cable or the potential for greater frequency of outages as cables age that would be avoided.<sup>143</sup> In sum, within ten years, through the ERP and ECRM, PSE can completely eradicate system failures associated with HMW cable, which will provide customers with numerous system benefits for decades.

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<sup>136</sup> Koch, Exh. CAK-3C at 6; Koch, Exh. CAK-1CT at 13:23-26.

<sup>137</sup> Koch, Exh. CAK-3C at 7-8.

<sup>138</sup> *Id.* at 8.

<sup>139</sup> *Id.*

<sup>140</sup> Koch, Exh. CAK-1CT at 17:19-22.

<sup>141</sup> *Id.* at 18:6-12.

<sup>142</sup> *Id.* at 18:13-17.

<sup>143</sup> *Id.* at 18:1-5.

54. For the WPCs, the benefits to customers are also substantial. In 2015, the WPCs accounted for 53 non-major event SAIDI minutes.<sup>144</sup> Under the ERP and ECRM, PSE will be able to directly address the reliability problems associated with the WPCs without competing demands from other reliability needs. The ERP would address the various reliability issues with the 135 WPCs which would improve reliability by approximately 50 percent and would target approximately 40 circuits annually as it incrementally works to improve the reliability of each WPC.<sup>145</sup> Overall, PSE estimates that an average of 29,000 customer interruptions will be saved annually.<sup>146</sup> This will improve reliability for impacted customers, which will result in shorter and fewer outages and will improve system measurements of SAIDI, SAIFI, and CEMI.<sup>147</sup> For example, PSE estimates that over the next two years, addressing these circuits will reduce PSE's non-major event SAIDI by an average of five minutes per year.<sup>148</sup> By hardening the WPCs, neighborhoods will experience fewer disruptions by PSE repair crews, and over time, PSE will see a reduction in overhead repair costs, which benefits are passed on to customers.<sup>149</sup> PSE intends to spend a significant amount from 2017-21 to address the WPCs.<sup>150</sup>

## 2. The ERP and ECRM Will Increase Reliability on a System-Wide Basis

55. In addition to the specific benefits tied to the HMW cable and the WPCs, the ERP and ECRM will improve the efficiencies associated with completing various HMW and WPC projects because having predictable funds allocated for specific projects will expedite the processes needed to holistically complete planning, engineering, permitting, construction, and coordination with governmental authorities.<sup>151</sup> Instead of repairing failed HMW cable or WPCs on a piecemeal basis requiring overhead costs and disruption each time, projects can be more

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<sup>144</sup> *Id.* at 18:18-20; Koch, Exh. CAK-3C at 13.

<sup>145</sup> Koch, Exh. CAK-1CT at 15:8-21.

<sup>146</sup> *Id.* at 18:21-22.

<sup>147</sup> Koch, Exh. CAK-3C at 13.

<sup>148</sup> *Id.*

<sup>149</sup> *Id.*

<sup>150</sup> Koch, Exh. CAK-1CT at 16:10-16.

<sup>151</sup> *Id.* at 19:4-8.

efficiently grouped and sequenced to minimize crew mobilization and demobilization efforts as well as minimizing potential construction activity disruption for customers.<sup>152</sup> The ability to recover investments in a timely manner following the installation year removes uncertainty associated with traditional ratemaking and allows PSE to plan for and commit to reliability improvement plans that are more than one year out, which will make it possible for PSE to coordinate the completion of more significant projects simultaneously and more quickly.<sup>153</sup>

56. The overall reliability benefits in resolving the issues associated with the HMW cable and the WPCs will also be significant. Improved reliability by fewer long outages and less disruption due to power outages is important to customers.<sup>154</sup> Customers depend on reliable, resilient, safe, and secure power systems to ensure vital necessities are available, including operating cellular networks, running fuel pumps, providing business and consumer access to banking systems, in providing lighting and security systems, and for many other purposes.<sup>155</sup> Replacing aging infrastructure with more robust assets also enhances public safety and security,<sup>156</sup> policies that are consistent with federal energy policy and Washington Governor Inslee's Resilient Washington, which aims at strengthening utility services during a catastrophic event.<sup>157</sup>

57. PSE customers expect reliable and resilient power, and PSE takes its responsibility to provide reliable power to its customers seriously.<sup>158</sup> PSE hears from customers throughout the year regarding how important reliability is to them and how power outages negatively impact their lives.<sup>159</sup> This is especially true for customers on a WPC.<sup>160</sup> Empirical research demonstrates that electric reliability is critically important to customers, and when customers perceive that a

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<sup>152</sup> *Id.* at 19:8-10.

<sup>153</sup> Koch, Exh. CAK-4T at 10:5-15.

<sup>154</sup> Koch, Exh. CAK-1CT at 19:12-14.

<sup>155</sup> *Id.* at 19:15-20.

<sup>156</sup> *Id.* at 19:20-21.

<sup>157</sup> *Id.* at 8:15-9:3.

<sup>158</sup> Koch, Tr. at 207:3-8.

<sup>159</sup> Koch, Exh. CAK-4T at 15:3-6.

<sup>160</sup> *Id.* at 15:1-13.

rate increase is being driven by investments in infrastructure, reliability, and power supply, customer satisfaction increases.<sup>161</sup> Statistics show that PSE customers are willing to pay more for more reliable service, which PSE is attempting to provide through the ERP and the ECRM. And, customers prefer to pay smaller, more incremental increases in rates, than less frequent larger increases in rates, which is precisely how the ECRM is structured.<sup>162</sup>

58. In sum, the ERP and ECRM provide a concrete solution to fully addressing two segments of PSE's electric reliability system that need direct, immediate, and aggressive attention that cannot be adequately addressed through traditional ratemaking and in conjunction with the other reliability demands on PSE's system. The ECRM is patterned after the Gas CRM which has been an overwhelming success in addressing reliability demands on PSE's gas system and would unquestionably provide benefits to PSE's customers. PSE urges the Commission to authorize the ECRM so PSE can fully engage in addressing the HMW cable and the WPCs.

**V. PSE'S PROPOSED REVISIONS TO THE DECOUPLING MECHANISM ARE REASONABLE AND SHOULD BE APPROVED**

59. This case presents the Commission's first opportunity to comprehensively review PSE's decoupling mechanisms. In 2013, the Commission determined that PSE's decoupling mechanisms were warranted, consistent with the State's energy policy and with the Commission's decoupling policy statement:

The decoupling mechanisms we approve mean that PSE's recovery of the fixed costs it incurs for infrastructure and operations necessary to deliver power and natural gas will no longer depend on the amounts of electricity and natural gas the company sells. This removes the so-called throughput incentive, thus promoting PSE's more aggressive pursuit of cost-effective conservation to which it commits as part of the decoupling mechanisms. With the throughput incentive eliminated, the company will be indifferent to sales lost as a result of the success of its conservation efforts. The full decoupling approved here is the first utility - supported mechanism that is both generally consistent with, and truly targeted to

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<sup>161</sup> *Id.* at 15:14-16:14.

<sup>162</sup> Doyle, Tr. at 178:6-179:13.

achieve, this key objective embodied in the Commission's 2010 Decoupling Policy Statement.<sup>163</sup>

60. The evidence in this case demonstrates that the decoupling mechanisms are generally operating as intended. A third-party evaluation of PSE's decoupling mechanisms conducted by Gil Peach and Associates ("Gil Peach Report") confirmed the success of the decoupling mechanisms and specifically found that PSE is calculating decoupling deferrals and rates in accordance with Commission orders; rate impacts have been small for electric customers and most gas customers, including low-income customers; conservation program performance has been stable during the evaluation period; and removing the throughput incentive has been a positive step in removing barriers to energy efficiency performance.<sup>164</sup>

61. PSE's proposed revisions to the decoupling mechanisms are designed to improve the already strong mechanisms and address some unintended consequences that have arisen in the first four years since the decoupling mechanisms were approved. PSE requests the Commission approve the continuation of the decoupling mechanisms with the proposed revisions.

**A. There Are Several Aspects of PSE's Proposal that Are Not Contested**

62. The parties agree on several aspects of PSE's decoupling proposal in this case. PSE proposes a change to the methodology for calculating "actual revenue" for gas non-residential customers, which will provide more accurate results. Currently, PSE uses a blended average margin rate to determine the actual revenues upon which it calculates its decoupling deferrals for these customers. PSE is proposing to use the actual margin revenue for non-residential gas customers.<sup>165</sup> Additionally, PSE committed to accelerate its conservation achievement five percent above the levels approved by the Commission for PSE's biennial conservation target and submit to penalties equivalent to those outlined in RCW 19.285 for failure to achieve these

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<sup>163</sup> *In re PSE and NW Energy Coalition*, Dockets UE-121697 & UG-130137, Order 07, Synopsis at ii (June 25, 2013).

<sup>164</sup> *See* Piliaris, Exh. JAP-29 at 14-27.

<sup>165</sup> *See* Piliaris, JAP-1T at 139:20-140:10. This would be accomplished by multiplying the actual base rates for both volumetric and demand charges by the appropriate billing determinants. *See id.*

incremental savings.<sup>166</sup> PSE also committed to increase its funding for low-income weatherization by \$500,000 per year,<sup>167</sup> and in the Settlement Agreement committed to a one-time contribution up to \$2 million through June 30, 2019, and a continuation of the \$100,000 annual shareholder contribution, until the next general rate case.<sup>168</sup>

**B. PSE’s Decoupling Mechanisms Should Continue and the Commission Should Discourage Repetitive Relitigation of Decoupling in Future Cases**

63. The Commission should reject recommendations by ICNU and FEA to discontinue PSE’s decoupling mechanism. These are the only parties to argue that the decoupling mechanisms should be discontinued, and they rely on arguments that the Commission rejected when it authorized PSE’s decoupling mechanisms just four years ago. Additionally, their arguments against the electric decoupling mechanism are refuted by the independent analysis provided in the Gil Peach Report, which concludes that there is no evidence that the decoupling mechanism created a disincentive for PSE’s customers to conserve, that it does not have an adverse impact on PSE’s service quality, and only leads to minor rate adjustments, particularly excluding the effects of the associated “K-factor” increases.<sup>169</sup>

64. Moreover, because the decoupling mechanisms have now been litigated in two consecutive cases, and a third-party evaluation of the mechanisms was undertaken covering the period of July 2013 through June 2016, the Commission should reject Commission Staff’s proposal that PSE file within four years to renew its decoupling mechanisms. PSE should not be required to relitigate the same issues that have been litigated in this case and the 2013 decoupling petition proceeding. The Commission should make a more definitive statement that decoupling is its preferred policy direction, at least for the time being, so that parties can focus on the many other important and complicated issues facing the utility industry in this state.<sup>170</sup>

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<sup>166</sup> *Id.* at 144:17-21.

<sup>167</sup> *Id.* at 146:1-5.

<sup>168</sup> *See* Settlement Agreement at ¶¶ 108-110.

<sup>169</sup> Piliaris, Exh. JAP-29 at 130, Tables VII.5 and VII.6.

<sup>170</sup> Piliaris, Exh. JAP-46T at 6:9-12.

**C. PSE’s Proposal To Readjust Decoupling Customer Groupings Mitigates Cross Subsidies Among Customers Within a Group and Should Be Approved**

65. As a further enhancement to PSE’s decoupling mechanisms, PSE has proposed changes to non-residential customer groups within the mechanisms. PSE’s proposals walk a fine line. If decoupling groups are too big there may be cross subsidies of the customers within the decoupling group. If decoupling groups are too small, there may be rate volatility within the group. The Commission should approve PSE’s proposals that appropriately balance the competing objectives of minimizing cross subsidies while also mitigating rate volatility.

**1. PSE’s Proposed Changes to Electric Non-Residential Groups Appropriately Place Customers with Similar Usage Together**

66. Currently, there are three non-residential electric rate groups: (i) customers served under Schedules 12 and 26, (ii) customers served under Schedules 10 and 31, and (iii) the remaining non-residential rate schedules.<sup>171</sup> PSE proposes to separate the third group into three groups as set forth below, for the following reasons:

- Customers served under Schedules 8 and 24: These customers have smaller use per customer and are so great in number and aggregate load that they tend to dominate the overall results for the existing non-residential group.<sup>172</sup>
- Customers served under Schedules 40, 46 and 49: These customers have significantly different load and service characteristics from the other customers in the existing non-residential group.<sup>173</sup>
- All remaining non-residential rate schedules that are currently in the third existing rate group.

**2. PSE’s Proposed Change to Gas Non-Residential Group**

67. Currently all non-residential natural gas customers included in the decoupling mechanisms are in one group.<sup>174</sup> PSE proposes to break them into two groups: (i) a separate non-residential decoupling rate group composed of customers served under Schedules 31 and 31T,

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<sup>171</sup> See Piliaris JAP-1T at 130:1-6.

<sup>172</sup> See *id.* at 130:12-15.

<sup>173</sup> *Id.* at 130:9-12.

<sup>174</sup> *Id.* at 108:13-15. This includes Schedules 31, 31T, 41, 41T, 86 and 86T.



and (ii) all remaining non-residential gas customers that are currently in the decoupling mechanism. The large number of small commercial customers served under Schedules 31 and 31T tend to dominate the results for the rest of their existing decoupling rate group, and the remaining customers in the non-residential decoupling rate group have a use and revenue per customer more similar to one another than to customers served under Schedules 31 and 31T.<sup>175</sup>

**D. Removing Customers from Decoupling, as Parties Propose, Revives the Throughput Incentive that Decoupling Is Designed To Eliminate**

**1. Proposals to Exclude Customers from the Electric Decoupling Mechanism Should be Rejected**

68. The Commission should reject proposals by Commission Staff, ICNU and FEA to exclude large electric customers from PSE's electric decoupling mechanism, an approach that is inconsistent with the Commission's Decoupling Policy Statement.<sup>176</sup> The removal undermines PSE's decoupling mechanisms by reintroducing the throughput incentive for these customers. Specifically, the parties have proposed the following:

- ICNU proposes to exclude Schedules 40, 46 and 49 from decoupling.<sup>177</sup>
- FEA proposes to exclude "large customers" from decoupling.<sup>178</sup>
- Commission Staff proposes three rate groups for decoupling: one for residential, one for small commercial (Schedules 8 and 24), and one for medium commercial (Schedules 7A, 11, and 25). All other electric rate schedules would be excluded from decoupling under Staff's proposal.<sup>179</sup>

69. The customers ICNU and FEA propose to exclude from the electric decoupling mechanism have among the largest declines in use per customer. To remove them from the decoupling mechanism would amplify PSE's throughput incentive, contrary to the state energy

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<sup>175</sup> See Piliaris, Exh. JAP-1T at 132:2-14.

<sup>176</sup> *Report and Policy Statement on Regulatory Mechanisms, Including Decoupling, to Encourage Utilities to Meet or Exceed their Conservation Targets*, Docket UE-100522, ¶ 28 (Nov. 4, 2010).

<sup>177</sup> Gorman, Exh. MPG-1T at 31:8-10.

<sup>178</sup> Al Jabir, Exh. AZA-1T at 12:6-7.

<sup>179</sup> Liu, Exh. JL-1CT at 30:16-20, 31:3-6.

policy.<sup>180</sup> Additionally, the proposals by ICNU and FEA lack detail, specifically with regard to how the significant remaining deferral balance would be handled.<sup>181</sup>

70. Further, these proposals undermine the PCA settlement agreement (“PCA Settlement Agreement”), which allowed fixed production costs to be moved from the PCA with the understanding that if decoupling continues, these fixed production costs would be included in the decoupling mechanism.<sup>182</sup> Excluding customer groups from PSE’s electric decoupling mechanism effectively moves the recovery of approximately 20 percent of fixed production costs out of the decoupling mechanism, contrary to the PCA Settlement Agreement.<sup>183</sup>

## **2. Commission Staff’s Proposals to Exclude Customers from the Gas Decoupling Mechanism Should be Rejected**

71. Similarly, Commission Staff’s proposal to exclude Schedules 86 and 86T from PSE’s gas decoupling mechanism fails to address the throughput incentive that will be reintroduced. Additionally, it fails to address how the existing substantial deferrals would be handled if these customers are removed from decoupling. The Commission should reject Commission Staff’s proposal as inconsistent with prior Commission orders and the Commission’s policy statement.

## **E. Proposed Alternatives to Decoupling Are Insufficient and Flawed**

### **1. Rate Design Alternatives**

72. Although Commission Staff is the only party that attempts to address the throughput incentive for the customers it proposes to exclude from the electric decoupling mechanism, it has not presented an adequate alternative. Commission Staff’s proposed solution is to increase the demand charges of customers served under Schedules 46 and 49. However, increasing the

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<sup>180</sup> Piliaris, Exh. JAP-46CT at 20:12-18.

<sup>181</sup> To try to correct this, ICNU filed a cross exam exhibit where it belatedly provided additional detail through its own data request response attempting to flesh out issues that it had failed to address in its filed case. The Commission allowed this to be used for illustrative purposes only. *See* Tr. 305:6-306:2. The response was inadequate, however, and does not change the fact that ICNU’s filed case fails to address this important issue.

<sup>182</sup> *See WUTC v. Puget Sound Energy*, Docket UE-130617, Order 11 ¶ 7 (August 7, 2015) (“While Fixed Production Costs are removed from the PCA and added to the decoupling mechanism, the Settlement provides that PSE may still update Fixed Production Costs through a PCORC.”).

<sup>183</sup> Staff’s proposal would remove \$115.8 million of the total \$579.7 million of fixed production costs from decoupling.

demand charge will not address the recovery of fixed costs or the throughput incentive. As Mr. Piliaris testified:

Staff is confusing the recovery of demand-related costs with the recovery of fixed costs. These are different concepts. Demand-related costs have to do with costs related to meeting peaking needs, and fixed costs have to do with how much these costs are likely to change over a period of time. It is the recovery of fixed costs through charges that are directly or indirectly tied to energy consumption that drive a utility's throughput incentive.<sup>184</sup>

73. Mr. Piliaris further illustrated this distinction using the peak credit methodology, which differentiates demand-related versus energy-related costs and has been approved for use in this case.<sup>185</sup> Under the peak credit methodology, 75 percent of production costs are energy related and 25 percent are demand related. In contrast, production costs that are viewed as “fixed” in nature constitute approximately 43 percent of the total power costs. “Therefore, even if demand-related charges are set to recover 100 percent of demand-related costs, approximately 42 percent of the \$544 million of production costs considered to be fixed in PSE’s PCA mechanism would be subject to a throughput incentive.”<sup>186</sup> Accordingly, Commission Staff’s proposal to increase demand related charges for Schedule 46 and 49, and remove these customers from decoupling, would reintroduce a throughput incentive<sup>187</sup> and should be rejected.

## **2. Other Proposed Forms of Decoupling Are Flawed and Previously Have Been Rejected by the Commission**

### **a. Public Counsel’s “Complete” Decoupling Should be Rejected**

74. Public Counsel’s proposal to move from revenue per customer decoupling to what Public Counsel terms a “complete” form of decoupling is draconian in nature and would deny PSE an opportunity to earn its authorized rate of return. As a compromise, PSE has agreed in the

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<sup>184</sup> Piliaris, Exh. JAP-46CT at 18:18-19:4.

<sup>185</sup> *See In the Matter of the Petition of Puget Sound Energy To Update Methodology Used to Allocated Electric Cost of Service and for Electric Rate Design Purposes*, Docket UE-141368, Order 03 ¶ 17 (Jan. 29, 2015).

<sup>186</sup> Piliaris, Exh. JAP-46CT at 19:17-20:2 (calculated by subtracting 25 percent from 43 percent and dividing the difference by 43 percent). For transmission-related costs, more than 75 percent of fixed transmission costs would be subject to a throughput incentive, even if all demand-related transmission costs were recovered through demand charges. *See id.* at 19:3-8.

<sup>187</sup> *Id.* at 22:5-7; Piliaris, Tr. 299:13-300:23.

Settlement Agreement to set the total Allowed Revenue for fixed production costs recovery per decoupled group at the level the Commission authorizes in this general rate proceeding, with the understanding this will be updated in future general rate cases and PCORCs, and with the understanding that the production factor is set to zero. However, what Public Counsel advocates for in this proceeding is that all costs, including fixed delivery costs, be set at the amount set by the Commission in this proceeding, rather than use the revenue per customer approach that the Commission authorized in 2013. The evidence demonstrates that PSE's delivery cost growth has exceeded customer growth by 1.2 percent per year.<sup>188</sup> Accordingly, to freeze PSE's delivery costs at the amount in this case, with no opportunity for increased revenue tied to customer growth, would deprive PSE of a reasonable opportunity to earn its authorized rate of return.

**b. FEA's Proposal to Focus Only on Conservation Has Previously Been Rejected by the Commission**

75. FEA proposed alternative to PSE's revenue per customer decoupling runs contrary to the Commission's policy statement and is essentially the same proposal that was expressly rejected by the Commission in PSE's last general rate case. In that case, PSE proposed a Conservation Savings Adjustment ("CSA") that was intended to compensate the utility only for the lost margin associated with PSE's energy efficiency programs. The Commission rejected this form of "limited decoupling" as inconsistent with its policy statement and because it relied on "engineering estimates of conservation savings that are ill-suited to development of a revenue requirement."<sup>189</sup> FEA's proposal should likewise be rejected.

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<sup>188</sup> See Barnard, Exh. KJB-1T at 6:10-11.

<sup>189</sup> See *WUTC v. Puget Sound Energy*, Dockets UE-111048 & UG-111049, Order 08 at p. ii (May 7, 2012).

**F. PSE’s Proposed Adjustments To the Rate Test on Decoupling Deferrals Are Reasonable and Should Be Approved**

**1. PSE’s Two Proposed Adjustments to the Rate Test are Reasonable and Should be Approved**

76. PSE’s two proposed adjustments to the Rate Test are reasonable and should be approved.

The Rate Test was included as part of the decoupling mechanisms to limit the percent increase customers will experience each year as a result of the decoupling mechanism.<sup>190</sup> PSE proposes to (i) revise the method by which the rate test is calculated, and (ii) increase the Rate Test cap for electric and gas residential customers.

77. First, no party has contested PSE’s proposed method of calculating the Rate Test. PSE proposes to use a baseline where “current” revenue (i.e., the basis for determining the percentage change in rates) is calculated as the product of current rates and the weather-normalized billing determinants in the prior calendar year. PSE’s proposed change will make the Rate Test more transparent and easier to calculate.<sup>191</sup>

78. Second, in response to concerns about growing deferral balances expressed by the Commission at annual Schedule 142 filings, PSE has proposed to increase the Rate Test from the current three percent cap to a five percent cap for electric and gas residential customers. Commission Staff supports this change for all customers subject to the decoupling mechanisms. PSE’s proposal to increase the current three percent rate caps to five percent for the electric and gas residential customers will continue to provide a reasonable limit to the rate increases customers will potentially experience but will serve two important purposes.

79. For PSE’s gas residential customers, the substantial deferred decoupling balances that have been accrued will be amortized on a more timely basis. Setting a higher cap will better align cost causation and cost recovery, and improve intergenerational equity.

The longer the deferred balances remain on the balance sheet, the less likely the customers who benefited from the deferred recovery of costs will be the customers that pay for those costs. In addition it is reasonable to believe that, the

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<sup>190</sup> See Piliaris, Exh. JAP-1T at 109:9-11.

<sup>191</sup> See *id.* at 134:14-135:2.

longer the period between cost causation and cost recovery, the more likely it will create customer confusion and dissatisfaction regarding why rates continue to be elevated for costs incurred in the past.<sup>192</sup>

PSE's proposal is also supported by the recommendations in the Gil Peach Report<sup>193</sup> and analysis PSE has performed showing that the decoupling-related gas residential deferrals would have cleared if a five percent cap on rate increases had been in place in the 2015 and 2016 annual filings, rather than the three percent cap.<sup>194</sup>

80. For PSE's electric residential customers, the higher Rate Test will reflect the fact that a greater amount of electric revenues are now subject to decoupling under the terms of the Settlement Agreement, which provides that fixed production costs will be included in PSE's electric decoupling mechanism.<sup>195</sup> A five percent rate cap is on the upper bounds of the impacts that would have been experienced over the past several years, if the K-factor had been removed and fixed production costs were included in the electric decoupling mechanism, as would be the case beginning in 2018.<sup>196</sup> Using the higher Rate Test means that customers who incurred the costs are more likely to be the customers who pay for those costs.

## **2. The Hard Caps Proposed by FEA are Unreasonable**

81. PSE's Rate Test is sometimes referred to as a "soft cap" because it caps the rate increase to customers in a given year but allows PSE to defer amounts above the cap and recover them in future years, subject to the Rate Test or "soft cap." The Commission should reject FEA's proposal to replace PSE's soft cap with a hard cap. A hard cap would "materially dilute the efficacy of PSE's decoupling mechanisms, effectively reinstating a throughput incentive if or when the cap is reached."<sup>197</sup> Additionally, it would undermine the concept of "allowed revenue"

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<sup>192</sup> *Id.* at 135:7-13.

<sup>193</sup> See Piliaris, Exh. JAP-29 at 132 ("We recommend that the Rate Test be adjusted from a 3% soft cap to a 5% soft cap to clear balances in most years while still providing a level of protection to the customer against extreme rate changes. As discussed earlier in this section, the benefit of raising the soft cap from 3% to 5% on rate increases includes better temporal alignment between incurred cost of service and the actual payment for service. This benefits both the customer class and PSE.").

<sup>194</sup> See Piliaris, Exh. JAP-1T at 135:13-17.

<sup>195</sup> See Settlement Agreement at ¶ 113.

<sup>196</sup> See Piliaris, Exh. JAP-46CT at 13:10-11.

<sup>197</sup> *Id.* at 14:5-7.

as PSE would not clearly understand what revenue it would be allowed to recognize for reporting purposes until the end of the year. This would negatively affect PSE's ability to budget, plan and operate efficiently, as the revenue stability afforded by the decoupling mechanism is weakened.<sup>198</sup> Moreover, as discussed in more detail below, the Commission has rejected "hard caps" because artificial caps on earnings diminish the incentive for efficient management.<sup>199</sup>

**3. The Coalition's Opposition to PSE's Proposal to Adjust the Rate Test Lacks Coherent Reasoning**

82. The Coalition proposes to use a five percent rate cap for gas residential customers for this case until PSE's next rate case, when improvements to weather forecasting can be implemented, but PSE does not use a forecast of weather. In its decoupling mechanisms PSE defers

the difference between allowed revenue, which is based on actual customer counts and allowed revenue per customer determined on historic test year information, to actual revenue, which is based on actual load and rates developed using historic test year information. The deferred amounts are surcharged or credited to customers in the year, or years, that follow. Nowhere in PSE's proposed mechanisms is a forecast of weather required.<sup>200</sup>

**G. The Changes to the Earnings Sharing Mechanism Proposed by PSE Are Reasonable**

83. PSE has proposed two reasonable adjustments to the earnings sharing mechanism associated with the decoupling mechanisms. First, PSE proposes to include a 25 basis point deadband before sharing earnings above its authorized rate of return.<sup>201</sup> Second, PSE proposes that the earnings sharing mechanism be based on actual, rather than normalized, earnings.<sup>202</sup> It is reasonable to adjust the earnings sharing mechanism in this case for the following reasons:

(i) PSE has agreed to decrease its ROE by 30 basis points and no longer has an ROE at the high

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<sup>198</sup> *Id.* at 14:8-12.

<sup>199</sup> *See In re PSE and NW Energy Coalition*, Dockets UE-121697 & UG-130137, Order 07 ¶ 162 (citing *WUTC v. Avista Corp.*, Dockets UE-120436 & UG-120437, Order 09 ¶ 79 (Dec. 26, 2012)).

<sup>200</sup> Exh. JAP-46CT at 14:20-15:5. Even if the Coalition meant "temperature normalization of loads" rather than "weather forecasting," differences in temperature normalization methodology as presented in this case would be immaterial in the context of setting the appropriate level of rate caps. *Id.* at 15:12-17.

<sup>201</sup> *See Doyle*, Exh. DAD-7T at 53-60.

<sup>202</sup> *Id.* at 48-53.

end of the range of reasonableness as was the case in 2013, (ii) PSE is not requesting a multi-year rate plan with built in rate increases as it did in 2013, (iii) four years of actual practice with the earnings sharing mechanism demonstrate that using normalized earnings does not accurately reflect PSE's actual earnings and should not be the basis for sharing of earnings.

**1. Circumstances Today Differ From Circumstances When the Earnings Sharing Mechanism Was Approved**

84. PSE's earnings sharing mechanism was first approved by the Commission in 2013, as part of the multi-year rate plan that accompanied PSE's amended decoupling proposal. With the rate plan and decoupling, PSE received annual rate increases of three percent applied to electric delivery costs and 2.2 percent applied to natural gas delivery costs.<sup>203</sup> Additionally, during the multi-year rate plan that began in 2013 and lasts through 2017, PSE's ROE remained at 9.80 percent, which the Commission had authorized in May 2012, and which the Commission found to reside at the higher end of the range of reasonable ROEs in 2013.<sup>204</sup>

85. In the 2013 decoupling case, PSE had proposed an earnings sharing mechanism that provided for 50-50 sharing of excess earnings with customers if PSE exceeded its authorized rate of return by 25 basis points.<sup>205</sup> This was consistent with the Commission's philosophy to apply earnings sharing mechanisms in a manner that maintains a company's incentive to cut costs. When the Commission approved PSE's "earnings test" it set the 50-50 sharing at the authorized rate of return, rather than at 25 basis points above the authorized rate of return, as PSE had proposed. The Commission expressed concern about doing so because "one of the purposes of a multi-year rate plan is to provide incentives to the company to cut costs, and allowing the company the potential to earn in excess of its authorized rate of return creates just such an incentive."<sup>206</sup> The Commission explained its general philosophy to not craft earnings sharing mechanisms in a way that removes incentives to cut costs and manage efficiently. The

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<sup>203</sup> *In re PSE and NW Energy Coalition*, Dockets UE-121697 & UG-130137, Order 07 ¶ 137.

<sup>204</sup> *Id.* ¶ 58.

<sup>205</sup> *Id.* ¶ 159.

<sup>206</sup> *Id.* ¶ 161.



Commission pointed to a recent Avista case in which it had rejected a hard cap in Avista’s earnings sharing mechanism:

We are mindful of our rejection in Avista’s most recent general rate case of a “hard cap” on earnings that Avista offered in settling the case. In its Final Order in the proceeding, the Commission explained:

In the course of consideration of the Settlement, Avista proposed a cap on its earnings at the 9.8 percent ROE level. We decline to accept that offer. It would send the wrong signal to the Company. Under ratemaking theory applied by this and other state commissions for decades, companies should have every incentive to manage the company efficiently in order to earn more for the company shareholders. We should not set an artificial cap on earnings that could diminish the incentive for efficient management. Further, if Avista were to “overearn” through savings efforts, those savings would become the new norm in the next rate case which would serve to benefit ratepayers in the future. Indeed, the Company’s efforts to save money through efficiency are a key element to earning its allowed rate of return.<sup>207</sup>

86. The Commission found this reasoning “equally cogent” in PSE’s case.<sup>208</sup> However, because the Commission determined that PSE’s then currently authorized 9.8 percent ROE—which was in the middle of the range of reasonableness when set in PSE’s last rate case—had moved to the higher end of that range, the Commission authorized an earnings sharing mechanism that required immediate, equal sharing of earnings between PSE and customers, when PSE exceeded its authorized rate of return.<sup>209</sup>

87. As shown above, the current earnings sharing mechanism, with its 50-50 sharing of any earnings in excess of PSE’s authorized rate of return, was crafted by the Commission to meet a specific situation that is no longer present in this case. It was approved by the Commission at a time when the Commission (i) had not reset PSE’s authorized rate of return for a year and was not planning to reset it during the course of the estimated three year rate plan, (ii) perceived that the existing ROE was at the high end of the range of reasonable returns, and (iii) had authorized

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<sup>207</sup> *Id.* ¶ 162 (citing *Avista Corp.*, Dockets UE-120436 & UG-120437, Order 09 ¶ 79).

<sup>208</sup> *In re PSE and NW Energy Coalition*, Dockets UE-121697 & UG-130137, Order 07 ¶ 163.

<sup>209</sup> *Id.* ¶¶ 164-165.

a multi-year rate plan with annual rate increases. None of these factor are present in this case. The Settling Parties have agreed on a reasonable ROE that is a 30 basis point reduction from PSE's current ROE and is in line with other utilities. Further, PSE will no longer have a multi-year rate plan with automatic annual rate increases. Given the changed circumstances from 2013, it is appropriate to revisit the earnings sharing mechanism. The Commission should apply the sound policy, expressed above, and set PSE's earnings sharing at 25 basis points above PSE's authorized rate of return. Doing so will create additional incentives for PSE to institute cost cutting measures that will result in savings to customers.

**2. The Commission Should Base the Earnings Sharing on Actual Earnings And Not Normalized Earnings that PSE Has Not Earned**

88. PSE should not be required to share excess earnings that it has not actually earned. That is the situation under the existing earnings sharing mechanism. As Mr. Doyle testified, the current mechanism “calculates rate of return as PSE’s normalized operating income divided by its average-of-monthly-averages rate base. To arrive at normalized operating income, actual operating income is adjusted for numerous Commission-accepted adjustments as reflected in PSE’s annual Commission Basis Report.”<sup>210</sup> Some of these adjustments are normalizing adjustments that restate the test year for “normal” conditions and normalize certain test year expenses. Normalization adjustments, while appropriate for Commission Basis Reporting, are not appropriate for determining when a utility has actually earned in excess of its authorized rate of return. Normalization adjustments can skew, and have skewed, the measurement of financial performance for excess earnings sharing purposes.<sup>211</sup> For example, it makes no sense for PSE to share earnings it did not actually earn, based on normalized wind and hydro conditions, when under the actual wind and hydro conditions PSE did not earn in excess of its authorized rate of return. If normalizing adjustments had been removed, in 2015 PSE would not have shared

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<sup>210</sup> Doyle, Exh. DAD-1T 15:9-13.

<sup>211</sup> *See id.* at 20:12-15.

\$4.6 million of pre-tax excess earnings that it did not actually earn, as it was required to do under the current earnings sharing methodology.<sup>212</sup>

89. The reverse situation can also occur to the disadvantage of customers. For example, it would be nonsensical to assume PSE did not earn in excess of its authorized rate of return based on normal wind and hydro conditions, when in fact it actually did earn above its authorized rate of return based on actual favorable wind and hydro conditions. Whether favoring the customer or PSE, these inequities have occurred and will continue to occur if the earnings sharing mechanism considers earnings based on normalized conditions rather than actual earnings.

**VI. PSE'S ELECTRIC COST OF SERVICE ANALYSIS IS CONSISTENT WITH THE PRIOR SETTLEMENT AGREEMENT AND SUPPORTED BY THE MAJORITY OF THE INTERESTED PARTIES**

90. PSE conducted a cost of service study to identify the costs incurred to serve each individual customer class.<sup>213</sup> PSE's electric cost of service analysis is generally consistent with the study performed in PSE's last general rate case and with the spirit and intent of the 2014 Electric Cost of Service and Rate Design Collaborative Settlement in Docket UE-141368 ("Rate Design Settlement"), which resulted from a collaborative following PSE's 2013 PCORC. In general, the parties accept PSE's analysis, with the exception of Public Counsel. For the reasons discussed below, the Commission should accept PSE's electric cost of service analysis, with updates to the results of the peak credit methodology to reflect more up to date information.

**A. PSE Used the 4-CP Allocation Factor Consistent With the Rate Design Settlement**

91. Mr. Piliaris testifies to the methodology and the changes made to cost of service analysis since PSE's 2011 general rate case.<sup>214</sup> One change involves the way in which PSE allocates demand-related production and transmission costs. As agreed to in the Rate Design Settlement, these costs were allocated on the basis of each class's contribution to coincident system peaks ("CP") in the months of November and December 2015 and January and February 2016. This is

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<sup>212</sup> See *id.* at 19:19-20:8.

<sup>213</sup> See Piliaris, Exh. JAP-1T at 18:10-14.

<sup>214</sup> *Id.* at 18:10-35:4.

referred to as the “4-CP” allocation factor. This is a change from PSE’s 2011 case.<sup>215</sup> No party objects to this change, which applies to this case only pursuant to the Rate Design Settlement.<sup>216</sup>

**B. PSE Used the Peak Credit Methodology Updated For Current Information**

92. PSE used the peak credit methodology to divide production costs into demand and energy components.<sup>217</sup> This methodology is important for classifying and allocating power costs in this case, and is also used for several of PSE’s adjusting price schedules that are traditionally tied directly to the results of the peak credit methodology from the most recent general rate case.<sup>218</sup>

93. The use of the peak credit methodology was agreed to in the 2014 Rate Design Settlement, and consistent with that settlement, PSE classified 25 percent of production costs as demand and 75 percent as energy in this rate case. However, because the peak credit analysis in the Rate Design Settlement was conducted in 2014, it did not incorporate more up to date information such as the underlying assumptions being used in the development of PSE’s 2017 IRP.<sup>219</sup> Using more current data to update the calculations from the peak credit study in the Rate Design Settlement, the percent of production cost classified as demand would be 18 percent, with 82 percent classified as energy.<sup>220</sup> While PSE is willing to stand by the 25 percent demand and 75 percent energy classification from the Rate Design Settlement, Mr. Piliaris testified that the updated results are more in line with the spirit of the Rate Design Settlement:

[I]t would be more appropriate to update the peak credit analysis for purposes of this rate case to reflect more current information than was used in [the Rate Design Settlement]. Doing so would be consistent with sound ratemaking practices, which are supportive of more current and accurate electric price signals. It would also be consistent with the intent behind this portion of the Rate

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<sup>215</sup> *Id.* at 24:11-17, 30:13-31:2.

<sup>216</sup> *Id.* at 30:19-31:2.

<sup>217</sup> *Id.* at 26:7-10.

<sup>218</sup> *See* Piliaris, Exh. JAP-46CT at 29:18-30:9. These include Schedule 95 (Power cost Adjustment clause), Schedule 95A (Federal Incentive Tracker), Schedule 120 (Electric Conservation Service Rider) and, indirectly, Schedule 140 (Property Tax tracker).

<sup>219</sup> *See* Piliaris, Exh. JAP-1T at 26:15-27:7.

<sup>220</sup> *Id.* at 28:18-29:5.

Design Settlement, which was to update the data used to perform PSE's peak credit analysis to a period more current than was used in PSE's 2011 GRC.<sup>221</sup>

94. Commission Staff accepts PSE's proposal to update the calculations.<sup>222</sup> Kroger, FEA and ICNU accept the Rate Design Settlement result that classifies power costs 75 percent energy and 25 percent demand as a compromise package.<sup>223</sup> Only Public Counsel proposes changes to the methodology. Public Counsel's proposal to carve out fuel costs for different treatment and treat these as 100 percent energy-related costs violates the Rate Design Settlement, to which Public Counsel was a signatory. PSE has a long history of including fuel costs among the power costs subject to the peak credit allocation factors, and to remove these now is inconsistent with the parties' intention in the Rate Design Settlement<sup>224</sup> and contrary to the peak credit methodology:

[T]he peak credit methodology compares the levelized cost of a peaking unit to that of a baseload unit to derive a relationship that is meant to be reflective of the proportion of overall production costs that would be considered demand-related. The levelized costs of the generic units compared include fuel expense. Therefore, fuel costs should be included among those to which the peak credit results would apply and separating those costs for unique treatment is inconsistent with the application of the methodology.<sup>225</sup>

### C. Public Counsel's Other Areas of Dispute Lack Merit

95. Public Counsel takes issue with two other aspects of PSE's cost of service study: (i) the allocation of income taxes, state excise taxes, and WUTC fees; and (ii) the allocation of certain transmission expenses. For the most part, Public Counsel's analysis is flawed. With respect to the allocation of taxes and fees, Public Counsel proposes to tie these revenue-dependent costs to actual revenues, rather than on a cost basis, as PSE proposes. While the results are seemingly immaterial, Public Counsel's approach creates a problem of circularity, where rates that are set based on actual rate revenue produce revenue-dependent costs. Allocating revenue-dependent

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<sup>221</sup> *Id.* at 28:11-17.

<sup>222</sup> *See* Ball, Exh. JLB-1T at 8:1-7.

<sup>223</sup> *See* Higgins, Exh. KCH-1T at 8:5-9:7; Al-Jabir, Exh. AZA-1T at 25:7-26:12; Gorman, MPG-1T at 27:10-23.

<sup>224</sup> *See* Piliaris, Exh. JAP-46CT at 28:15-29:6.

<sup>225</sup> *Id.* at 29:9-15.

expenses on a cost of service basis, and then independently deciding from that point how much, and in what direction to potentially deviate rates from this cost basis avoids this circularity.<sup>226</sup>

96. Public Counsel identifies several transmission costs that Public Counsel believes should be allocated partially to the Retail Wheeling class. However, Retail Wheeling customers do not use generation integration facilities to wheel power to their points of delivery and therefore PSE properly allocated costs related to generation integration using the PC4 allocation factor in PSE's cost of service, which excludes the Retail Wheeling class. PSE's approach is consistent with the FERC Open Access Transmission Tariff ("OATT") under which the Retail Wheeling customers are charged for their transmission, which similarly excludes these costs from tariffed rates.<sup>227</sup>

## VII. ELECTRIC RATE SPREAD AND RATE DESIGN

97. Several issues regarding non-residential electric rate spread and rate design are addressed in the Settlement Agreement. The below sections address the rate spread and rate design issues that are included in the Settlement Agreement, as well as the remaining contested rate spread and rate design issues. Attachment A, hereto, updates pages 13 and 14 of JAP-15 and summarizes: (i) PSE's position on contested rate spread and rate design issues, (ii) non-contested rate spread and rate design issues that are not expressly addressed in the Settlement Agreement, and (iii) settled rate spread and rate design issues included in the Settlement Agreement.

### A. Electric Rate Spread

#### 1. Issues Addressed in the Settlement Agreement

98. The Settlement Agreement sets forth the allocation of revenue deficiency for most non-residential schedules.<sup>228</sup> Public Counsel testifies that the electric rate spread in the Settlement Agreement is "inadequate" because (i) it does not precisely explain the methodology that would

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<sup>226</sup> *Id.* at 32:9-33:2.

<sup>227</sup> *Id.* at 33:3-35:9. While PSE agrees with Public Counsel that a few transmission related costs are allocable to Retail Wheeling customers such as transmission costs related to the Energy Imbalance Market ("EIM") found in Intangible Transmission Plant, Accumulated Deferred Income Taxes, and ARO Transmission Wood Poles, there is no impact to the rates for Schedule 449 for this reallocation, since transmission costs are recovered from these customers under PSE's OATT. *See id.* at 35:10-36:5.

<sup>228</sup> *See* Settlement Agreement at ¶ 94.

be used to allocate the electric increase of \$20.160 million, (ii) the revenue impact on the largest rate classes is not addressed, and (iii) it is at odds with the Commission's prior rate spread policies and practices. With respect to the first two issues raised by Public Counsel, it is true that not all issues have been settled, and the remaining contested matters must be decided by the Commission as part of the litigated case, as occurs whenever a settlement has not been reached on electric rate spread issues.

99. PSE disagrees with Public Counsel's claim that the electric rate spread methodology is at odds with prior Commission policy. First, there is very little recent guidance from the Commission on rate spread issues, since this issue has been settled in most, if not all, PSE cases for the past few decades. Moreover, the Settlement Agreement compromises on the manner in which the electric revenue deficiency will be spread for the non-residential customers set forth in paragraph 95 of the Settlement Agreement, all of which have parity levels at or above 108 percent based on PSE's cost of service study, meaning that they are paying more than their allocated costs. In their litigated positions, the Settling Parties had proposed a wide range of rate treatment for these customer groups: PSE proposed to increase these customer groups' rates by 75 percent of the adjusted average rate increase,<sup>229</sup> Kroger proposed a 35 percent increase for secondary and high voltage customers,<sup>230</sup> while ICNU and FEA testified that no increase would be appropriate for secondary and high voltage customers, including Schedule 46 and 49.<sup>231</sup> The proposal in the Settlement Agreement to increase the designated schedules by 65 percent is reasonable and should be accepted by the Commission.

## **2. Issues Not Addressed in the Settlement Agreement**

100. PSE proposed a five percent deadband in which retail schedules within five percent of full parity, plus or minus, would receive the adjusted average rate increase. While PSE disagrees with the results of Public Counsel's cost of service study on which its parity ratios are set, PSE

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<sup>229</sup> See Piliaris, Exh. JAP-1T at 53:9-5.

<sup>230</sup> See Higgins, Exh. KJH-1T at 10:7-11:11.

<sup>231</sup> See Gorman, Exh. MPG-6; Al Jabir, Exh. AZA-1T at 3:17-33.

does not object to the use of a ten percent deadband as proposed by Public Counsel, which would result in most schedules, that are still contested, receiving an adjusted average rate increase.<sup>232</sup> Additionally, PSE can agree to Public Counsel's proposal to give Schedule 35 a rate increase that is 150 percent of the average, as Schedule 35 has a parity ratio well below 1.0 using PSE's cost of service study.<sup>233</sup> All other schedules not included in the Settlement Agreement should receive the adjusted average rate increase.

101. The Commission should reject Public Counsel's proposal to give Schedule 449 customers a rate increase equal to 150 percent of the average. The vast majority of the revenues associated with Schedule 449 are not subject to the jurisdiction of the Commission, but are subject to FERC jurisdiction, pursuant to PSE's OATT. Public Counsel's proposal would effectively subject an otherwise FERC jurisdictional customer to Commission based rates.<sup>234</sup>

## **B. Contested Residential Electric Rate Design Issues**

### **1. Residential Basic Charge and Minimum Charge**

102. PSE proposes to increase the basic charge for single-phase electric service to \$9.00 per month. This is a \$1.51 per month increase over the current basic charge as reflected in base rates, but the net impact is \$1.13, since approximately \$0.38 per month of the proposed basic charge increase is already being paid by residential customers through Schedule 141 (Expedited Rate Filing).<sup>235</sup> This is consistent with the Commission's standard in past cases endorsing gradualism in the increase to the basic charge.<sup>236</sup> The proposed increase reflects the current level of costs traditionally recovered through PSE's residential electric basic charges, including customer service, customer accounting, meter reading, billing and line transformation.<sup>237</sup>

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<sup>232</sup> Piliaris, Exh. JAP-46CT at 37:12-38:1.

<sup>233</sup> *Id.* at 38:1-3.

<sup>234</sup> *Id.* at 38:6-39:2.

<sup>235</sup> See Piliaris, Exh. JAP-1T at 65:15-21. The rates within Schedule 141 will be set to zero coincident with the new base rates going into effect at the end of this rate case.

<sup>236</sup> See, e.g., *WUTC v. PacifiCorp d/b/a Pac. Power & Light Co.*, Docket UE-111190, Order 07 ¶ 39 (Mar. 20, 2012) (“[W]hen establishing an appropriate rate spread and rate design we consider not only the cost burden a customer class imposes on a utility but also the principles of rate stability and gradualism.”).

<sup>237</sup> See Piliaris, Exh. JAP-1T at 65:9-12.



103. PSE's proposed increase is reasonable when viewed in the context of the multi-year rate plan that has been in place since July 1, 2013. The current basic charge was set in PSE's last rate case, effective in May 2012, and the additional \$0.38 of basic charge currently being paid through Schedule 141 was based on a test year ending June 30, 2012. Thus, there has not been an increase to the basic charge for several years. In contrast, the multi-year rate plan provided for three percent annual increases to allowed delivery revenue per customer for electric service, and PSE has recovered 100 percent of these annual revenue increases through volumetric charges. If a portion of the three percent increases had been applied to monthly basic charges, there would currently be a \$9.12 monthly basic charge in effect.<sup>238</sup>

104. PSE's proposed basic charge is below the average basic charge for utilities across the country and within Washington. The 107 basic charges of the national electric utilities surveyed average \$9.17 per month. The average basic charge for all 44 of the utilities surveyed in Washington State is \$17.76, or almost double the basic charge proposed by PSE.<sup>239</sup>

105. In contrast to PSE's reasonable proposal, the other parties' proposals are likely to cause confusion and are not well-grounded. Commission Staff's proposal will increase customer charges to \$10.88, but will do so through the use of two separate charges. Commission Staff proposes to retain the existing basic charge of \$7.87, but add a minimum charge of \$3.01, which Commission Staff testifies will recover all customer costs including transformers. PSE estimates the additional \$300,000 in revenue that is likely to result from the minimum bill, over and above what PSE would have recovered from the same customers without a minimum bill through volumetric rates, does not outweigh the confusion customers are likely to experience or the cost that PSE would incur in adding a minimum bill component into its residential rate structure.<sup>240</sup>

106. Coalition witness Amanda Levin disputes PSE's inclusion of transformer costs in the calculation of the residential basic charge, but her testimony demonstrates several

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<sup>238</sup> See *id.* at 66:7-15.

<sup>239</sup> See *id.* at 67:2-9; Exh. JAP-17.

<sup>240</sup> See Piliaris, Exh. JAP-46CT at 42:1-44-7.

misunderstandings about the allocation of line transformer costs. Contrary to Ms. Levin's testimony, the manner in which line transformer costs are classified (demand versus customer related) does not make a difference in how they are allocated in PSE's cost of service study. The transformers are not shared by customers taking service under different schedules, nor does PSE allocate the full pool of transformer costs among various schedules. Rather, transformer costs are assigned to the various classes of customers; therefore, whether they are demand related or customer related is irrelevant to the subsequent allocation.<sup>241</sup> Moreover, Ms. Levin's suggestion that PSE is proposing to recover all transformer costs through the basic charge is incorrect. PSE has proposed to recover through its basic charge \$1 per month of the approximately \$3 per month in transformer costs.<sup>242</sup> Ms. Levin's testimony also relies on incorrect assumptions about PSE's construction standards<sup>243</sup> and she fails to recognize that transformer costs can be driven in part to serve customers and in part to meet a peak load requirement.<sup>244</sup>

107. The Coalition's recommendation for a study of cost differences for residential customers lacks clarity, would likely be an enormous undertaking, and should be rejected by the Commission. The proposal would require collection of load profile data that does not yet exist at the level required for the recommended study.<sup>245</sup>

108. Public Counsel's proposal to reduce PSE's existing customer charge to \$7.50 is not reasonable. Public Counsel improperly excludes transformer costs and overhead administrative costs in the basic charge calculation. As previously discussed, it is appropriate to include a portion of transformer costs as customer-related in the basic charge, as PSE has done. And it cannot be denied that a portion of overhead costs are driven by the number of customers.<sup>246</sup>

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<sup>241</sup> See *id.* at 44:8-45:13.

<sup>242</sup> See *id.* at 45:14-46:5.

<sup>243</sup> See *id.* at 46:6-47:6.

<sup>244</sup> See *id.* at 47:7-17.

<sup>245</sup> See *id.* at 49:4-49:20.

<sup>246</sup> See *id.* at 50:1-51:8.

## 2. Seasonal Energy Rates

109. Commission Staff's seasonal rate proposal is a well-intentioned attempt to reflect cost-causation, but it would cause negative unintended consequences. First, the proposal would be difficult to implement and would be unlikely to elicit a significant change in overall customer usage patterns. Also, the proposal is likely to disproportionately impact low-income customers who tend to rely disproportionately on electric heating. Finally, the proposal may hinder efforts to decarbonize by pushing customers to natural gas usage, for which there is limited ability to decarbonize. For these reasons, the Commission should reject Staff's proposal at this time.<sup>247</sup>

## 3. Three-Block Rates

110. All interested parties, other than the Coalition, have agreed that three-block rates should not be instituted in this case. Although the parties to the Rate Design Settlement in Docket UE-141368 agreed that PSE would propose a three-block rate structure in this case, that agreement was based on an assumption that the rates for the third block would be higher than the rates for the first and second blocks. When PSE calculated the third-block rates in preparation for filing this general rate case, the third-block rate was lower than the rate for the first and second block. Because such a rate structure would not have sent the desired price signals to customers, PSE provided the three-block rate in its filing but did not propose to change the design of its electric residential rate design to incorporate the three-block rates.<sup>248</sup> After reviewing PSE's direct filing all parties to the Rate Design Settlement either agreed that the parties should not move forward with a three-block rate proposal or did not oppose this approach, and a joint motion was filed seeking to amend the Rate Design Settlement and Order approving the Rate Design Settlement to remove this requirement.<sup>249</sup> The Commission issued a notice concerning the interplay between

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<sup>247</sup> *Id.* at 53:10-54:13. If the Commission does accept Staff's proposal for seasonal rates, it should require that the definitions of the summer and winter seasons align with those currently used for other rate schedules that have seasonal rates. (Summer: April 1 through September 30; Winter: October 1 through March 30.). *Id.* at 54, n. 98.

<sup>248</sup> See Piliaris, Exh. JAP-1T at 57:14-58:8.

<sup>249</sup> See *WUTC v. Puget Sound Energy*, Docket UE-141368, Joint Motion to Amend Order 03 and Settlement Agreement ¶¶ 5-6 (June 29, 2017).

the Rate Design Settlement and this case and has taken official notice of the record in the Rate Design Settlement, including the Joint Motion, but has not ruled on the Joint Motion.<sup>250</sup>

111. The Coalition is the only party proposing a third-block rate in this case. However, the Coalition's proposal to recalculate the third-block residential rate, accounting for the expected cost of carbon emissions, relies on speculative and dated forecasts of carbon costs in the future. The Commission has previously rejected proposals by PSE which rely on similar "engineering estimates" that were deemed to be unsuitable for ratemaking by the Commission.<sup>251</sup> Moreover, it is not clear why the Coalition cannot achieve its objective with a two-block rate with a greater differential. The proposal is likely to cause billing and customer perception issues and it may result in fuel switching, which potentially conflicts with goals to decarbonize energy use.<sup>252</sup>

112. Additionally, the Coalition's vague proposal to incorporate load factor considerations into the calculation of PSE's tail block rate lacks the necessary detail to implement the proposal. The Coalition points to a study conducted over 40 years ago that has not been located. Though there could be some merit to the concept, it is not fleshed out enough to be implemented in this case.<sup>253</sup>

### **C. Schedule 40 Proposals**

113. The Settlement Agreement provides that Schedule 40 will be discontinued by the tariff effective date of PSE's next general rate case, and Schedule 40 will be closed to new customers effective with this Settlement Agreement.<sup>254</sup> Additionally, PSE proposed to grandfather locations already served under Schedule 40 from losing their eligibility when these locations would have otherwise qualified for service under Schedule 40 but for the fact that electric service at this

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<sup>250</sup> See *WUTC v. Puget Sound Energy*, Docket UE-141368, Notice Concerning Interplay Between Pending Proceedings in Puget Sound Energy, Dockets UE-141368 & UE-170033 (July 17, 2017) (Taking Official Notice of Respective Records Concerning Common Issue As of July 14, 2017).

<sup>251</sup> See Piliaris, Exh. JAP-46CT at 55:20-56:5.

<sup>252</sup> See *id.* at 55:9-20.

<sup>253</sup> See Piliaris, Exh. JAP-46CT at 56:8-19.

<sup>254</sup> Settlement Agreement at ¶ 96.

location was subsequently provided from a different substation.<sup>255</sup> PSE applied this proposed change to one location in the current case. No party opposed this proposal.

114. Public Counsel’s proposal to remove the linkage between the rates of Schedules 40 and 49 would be difficult to implement. Rather than adopt Public Counsel’s proposal, the Commission should adopt PSE’s more refined approach for determining the parity ratios for Schedule 40, which has been used in this case.<sup>256</sup>

#### **D. Other Non-Residential Rate Design Proposals**

##### **1. ECRM Cost Allocation and Rate Design**

115. PSE proposes a two-step process to allocate ECRM costs. First, the overall revenue requirement will be allocated between overhead and underground investments based on the relative capital investment in these two cost categories. Next, the overhead and underground-related CRM revenue requirement are each allocated to electric customers based on the load-weighted line miles associated with each type of distribution feeder.<sup>257</sup> Mr. Piliaris provides more detail on the methodology and the rate impacts.<sup>258</sup> PSE supports Kroger’s proposal that the ECRM rates, if approved, be designed as a demand charge for demand-billed rate schedules.<sup>259</sup>

##### **2. Net Metering Proposals**

116. PSE supports one of Commission Staff’s proposals regarding net metering customers, but requests that the Commission deny the other requests. PSE is willing to perform a demand study for net metering customers suggested by Commission Staff and has already begun designing a program to collect the requested information for these customers. However, PSE cannot reprioritize the roll out of advanced metering infrastructure (“AMI”) as Commission Staff requests. This will occur over several years in a deliberate manner and reprioritizing the AMI

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<sup>255</sup> See Piliaris, Exh. JAP-1T at 70:6-71:12.

<sup>256</sup> *Id.* at 71:10-73:10.

<sup>257</sup> See *id.* at 148:1-8.

<sup>258</sup> See *id.* at 148:1-151:15; Piliaris, Exh. JAP-32.

<sup>259</sup> See Piliaris, Exh. JAP-46CT at 66:8-16. For Schedule 25, a portion of the costs should be recovered in its demand charge and another portion in the first block energy rates, based on the level of first block rates in excess of the tail block rate.

roll out would significantly increase the costs and delay the roll out. Finally, PSE believes it is premature to establish a separate rate schedule for net metering customers, but PSE will commit to compiling interval load data and responding to this proposal in its next general rate case.<sup>260</sup>

### **3. Electric Bill Presentation**

117. The Commission should reject Public Counsel’s proposal that PSE provide a summary sheet within its tariff that shows the all in price of electricity. This is unnecessary and duplicative of information already available to customers on their bills and on the PSE website.<sup>261</sup>

### **E. Settled and Uncontested Non-Residential Rate Design**

118. Paragraphs 95 through 99 of the Settlement Agreement addresses non-residential rate design issues that have been settled, including demand charges for Schedules 46 and 49. In addition, there are several rate design components that are not contested by the parties from PSE’s case as originally filed and for which PSE requests Commission approval.

119. One change proposed by PSE that has been accepted by Staff<sup>262</sup> addresses the manner in which lighting rates are determined. PSE proposes to: (i) expand the wattage range for each Light Emitting Diode (“LED”) rate, (ii) update overall lighting rates to better reflect cost causation with a more detailed and current cost analysis, and (iii) remove the “Wattage Including Driver” column in tariffs with LEDs. Mr. Piliaris provides extensive testimony on the change.<sup>263</sup>

120. Another change proposed by PSE relates to Schedule 449 basic charge rate design. PSE proposes to significantly simplify pricing for Power Supplier Choice and Retail Wheeling Service (Schedules 448 and 449) by setting the basic charge at its cost of service and eliminating the existing per kVA charges, which are not needed for PSE to recover its cost of serving customers under these schedules. Mr. Piliaris provides further detail of this proposed change.<sup>264</sup>

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<sup>260</sup> *Id.* at 67:2-68:3.

<sup>261</sup> *Id.* at 68:5-17.

<sup>262</sup> *See* Ball, Exh. JLB-1T at 53:12-19.

<sup>263</sup> *See* Piliaris, Exh. JAP-1T at 78:4-88:10.

<sup>264</sup> *See id.* at 74:1-75:18.

## VIII. NATURAL GAS COST OF SERVICE, RATE SPREAD AND RATE DESIGN

121. The natural gas cost of service, rate spread and rate design proposed by PSE in this case are reasonable and consistent with past cases and should be adopted by the Commission in this case. Commission Staff has convened a generic cost of service workshop that may affect cost of service issues in the future. PSE is participating in that process and looks forward to working with other parties to reach mutually agreeable solutions that will apply to cases in the future.

### A. PSE's Natural Gas Cost of Service Study Should Be Accepted By the Commission

122. PSE's natural gas cost of service study is reasonable. PSE updated its classification and allocation of gas costs for the first time in a decade, and no party has disputed this classification. The objections that parties have raised relate to allocation of gas distribution mains. However, as discussed below, PSE's approach is more balanced than the approaches proposed by Commission Staff and NWIGU. The Commission should accept PSE's natural gas cost of service study.

#### 1. PSE Updated the Classification of Gas Costs Used in PGA Filings

123. PSE reviewed and updated the classification and allocation factors used in its PGA filings for the first time in a decade because of significant changes in the resource mix.<sup>265</sup> PSE classified purchased gas costs into two components: demand and variable.<sup>266</sup> Mr. Piliaris's testimony details the costs that are included in each component<sup>267</sup> and how the costs are allocated to the customer classes.<sup>268</sup> No party has disputed the classification and allocation, and PSE requests that the Commission approve this methodology for use in future PGA filings.

#### 2. The Peak and Average Method for Classifying and Allocating Gas Distribution Mains is Reasonable

124. Following a long-standing practice, dating back to PSE's 2007 general rate case, PSE used the peak and average methodology for allocating gas distribution main costs. This

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<sup>265</sup> See *id.* at 49:9-50:4.

<sup>266</sup> See *id.* at 50:5-7.

<sup>267</sup> See Piliaris, Exh. JAP-1T at 50:8-20; Piliaris, Exh. JAP-12.

<sup>268</sup> See Piliaris, Exh. JAP-1T at 51:1-52:9; Piliaris, Exh. JAP-14.

methodology allocates gas demand costs based on a combination of peak demand and average demand (or average throughput).<sup>269</sup> Using this approach, PSE's demand-related gas distribution mains were allocated 33 percent on average demand and 67 percent on design day peak demand.<sup>270</sup> In support of this approach, Mr. Piliaris testified as follows:

The peak and average methodology's use of system load factor provides a reasonable basis for classifying and allocating these costs. This peak and average approach reflects a balance between the way the gas system is designed (to meet peak demand) and the way it is utilized on an annual basis (throughput based on gas usage that occurs during all conditions, not only peak conditions). It also acknowledges previous Commission guidance that some portion of gas demand costs should be allocated based on energy use.<sup>271</sup>

125. This balanced and transparent approach recognizes that all customers benefit from the gas distribution system of medium to large mains as a whole, not only from the stretch of main through which gas flows to reach the individual customer. PSE's gas distribution system is a network of pipes that provides benefits to customers in addition to providing the stretch of pipe through which molecules flow to reach the individual customer. PSE's approach avoids the practice of using a customer's physical location on the system to determine the costs assigned to that customer, which has been opposed in past cases. Further, it exempts large gas customers from the cost of the smallest diameter main (less than two inches), because the smallest main is in isolated locations on the system and is unlikely to benefit large commercial and industrial customers. And, it addresses concerns regarding cost responsibility for two-inch main by allocating a portion of it to all customers and excluding the largest interruptible customers from a portion of it.<sup>272</sup> PSE's approach was recently validated by a third-party consultant.<sup>273</sup>

126. In contrast to PSE's balanced approach, NWIGU proposes that distribution mains be allocated entirely on coincident demand. NWIGU's approach does not reflect the manner in

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<sup>269</sup> See Piliaris, Exh. JAP-1T at 43:5-15.

<sup>270</sup> See *id.* 43:17-20, 44:12-47:15.

<sup>271</sup> *Id.* at 44:3-9.

<sup>272</sup> See *id.* 47:18-48:13.

<sup>273</sup> See Piliaris, Exh. JAP-46CT at 74:24-75:13, citing final report by Brown, Williams, Moorehead & Quinn in Docket UG-151663.



which the system is used and is inconsistent with prior guidance from the Commission that gas main costs should be allocated in a manner that reflects both the way these costs are incurred and the way the system is used.<sup>274</sup> Additionally, there are rate design implications with NWIGU's approach. Currently distribution main costs are split between energy and demand under the peak and average methodology. Under NWIGU's proposal, these costs would be considered entirely demand-related, and demand charges would need to be set much higher to recover these costs, which NWIGU has not proposed to do. PSE estimates its current demand charge of \$1.14 per therm of peak or contract demand would need to be set in the range of \$2.89 to 3.74 per therm, depending on the schedules.<sup>275</sup> Accordingly, the Commission should reject NWIGU's proposal.

### **3. PSE Properly Used the Design Day Peak to Allocate Gas Mains Costs**

127. PSE used the system design day to develop its peak demand allocator.<sup>276</sup> In contrast, Commission Staff proposes that gas mains costs be allocated using the average class use in the highest five day period for each of the last three years. NWIGU supports a design day approach that appears to be more aligned with PSE's position. The Commission should reject the proposal offered by Commission Staff for the following reasons.

128. First, design day peak is a better indicator of gas cost causation than historical peak demands. PSE designs its gas system to meet a design day peak demand, which is based on cold weather conditions. Regardless of how often those design day conditions occur, PSE incurs the capacity costs associated with being able to provide natural gas service on a design day. PSE uses the design day standard in its gas capacity investment decisions and builds capacity to meet that standard. If PSE built its gas system based on an historical peak, the capacity might not be sufficient to serve customer needs in extreme weather. The gas design day standard was developed in PSE's IRP process and has been accepted by the Commission. An estimated peak

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<sup>274</sup> See *id.* at 73:17-18:5 (citing *WUTC v. Wash. Natural Gas Co.*, Docket UG-940034, Fifth Supp. Order (Apr. 11, 1995)).

<sup>275</sup> See *id.* at 75:16-26.

<sup>276</sup> *Id.* at 37:8-39:11.

based on historical weather conditions during a particular period, as Commission Staff and NWIGU propose, would not reflect PSE's costs associated with meeting its peak demand.<sup>277</sup>

129. Second, design day provides a more stable estimate of gas peak than historical peaks provide, and provides more stable gas cost of service results over time. Weather, gas volumes and peak gas demands change from year to year, yet the costs of designing and building PSE's gas system do not change.<sup>278</sup>

130. In summary, PSE's approach to allocating gas distribution mains is a balanced approach that (i) splits costs between demand and energy, (ii) allocates a portion of costs based on cost causation (design day peak) and a portion based on volumetric usage, and (iii) further splits energy-related costs between main sizes to provide a more refined allocation between rate classes. PSE's natural gas cost of service study, including the methodology for allocating distribution mains, should be accepted by the Commission in this case.

#### **B. Natural Gas Rate Spread**

131. PSE's proposed natural gas rate spread would (i) apply the system average increase to those classes with parity percentages between 90 percent and 110 percent (Schedules 23, 16, 53, 41, 41T, 85 and 85T); (ii) apply 50 percent of the average increase to those classes between 110 and 150 percent of parity (Schedules 86 and 86T); (iii) apply no increase to those above 150 percent of parity (Schedules 71, 72 and 74); and (iv) apply 150 percent of the average increase to those below 90 percent of parity (Schedules 31, 31T, 87 and 87T).<sup>279</sup>

132. NWIGU's proposal to move classes receiving decreases under NWIGU's proposed cost of service study to 25 percent of their cost of service is extreme and ignores the philosophy of gradualism that has been endorsed repeatedly by the Commission.<sup>280</sup> NWIGU's proposal would

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<sup>277</sup> See Piliaris, Exh. JAP-1T at 40:1-14.

<sup>278</sup> See *id.* 40:17-22.

<sup>279</sup> Piliaris, Exh. JAP-1T at 88:13-20.

<sup>280</sup> See, e.g., *WUTC v. PacifiCorp d/b/a Pac. Power & Light Co.*, Docket UE-111190, Order 07 ¶ 39 (Mar. 20, 2012) (“[W]hen establishing an appropriate rate spread and rate design we consider not only the cost burden a customer class imposes on a utility but also the principles of rate stability and gradualism.”).

increase rates to certain schedules by 19.38 percent and 25.73 percent, and would decrease rates to other schedules by 14.89 percent.<sup>281</sup> These aberrant results are due in large part to NWIGU's flawed cost of service study. NWIGU's compromise position of equal percentage increases, in light of the recently-commenced process to consider cost of service issues,<sup>282</sup> is more reasonable.

133. The Commission should reject both of Commission Staff's alternative proposals with respect to the natural gas special contract. Commission Staff recommends that the Commission either (i) impute revenue for PSE's natural gas Special Contract class sufficient to recover 100 percent of its allocated costs, including the authorized return on rate base allocated to serving these customers, and to allow any shortfall in revenue flow to shareholders; or (ii) order an increase in rates to the Special Contract class. Commission Staff misinterprets the Special Contract rule,<sup>283</sup> relies too heavily on one estimate of cost,<sup>284</sup> and ignores the evidence that the Special Contract is contributing to PSE's fixed gas distribution costs.<sup>285</sup> Additionally, from a policy standpoint, Commission Staff's recommendation is flawed. Commission Staff has had multiple opportunities in the past to raise this issue but has failed to do so.<sup>286</sup> Staff's proposal is contrary to the public interest and Commission rules,<sup>287</sup> and it would be an unprecedented step by the Commission to unravel a Special Contract that the Commission has approved, in the middle of the contract term.<sup>288</sup> Specifically, with respect to Commission Staff's alternative proposal to raise the Special Contract rates in this proceeding so that the rates reflect a two percent rate of return, there is no basis for this arbitrary increase in the Special Contract contribution to rate of return and it undercuts Commission Staff's alternate position. Moreover, the Special Contract is a contract and it cannot be unilaterally revised in this proceeding. The only way to increase the rate for this Special Contract, which is not suspended in this case,

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<sup>281</sup> See Piliaris, Exh. JAP-46CT at 78:13-79:5.

<sup>282</sup> See Collins, Exh. BCC-5T at 2:18-21, 8:20-9:4.

<sup>283</sup> See Piliaris, Exh. JAP-54T at 3:6-4:17.

<sup>284</sup> See *id.* at 7:15-8:17.

<sup>285</sup> See *id.* at 5:3-6:15.

<sup>286</sup> See *id.* at 9:4-10:16.

<sup>287</sup> See *id.* at 10:17-13:7.

<sup>288</sup> See *id.* at 13:8-16.

would be to dramatically increase rates to Schedules 87 and 87T simply to change rates for the Special Contract, which rate is based on Schedule 87 and 87T. Such an approach is arbitrary and unreasonable.<sup>289</sup>

## **C. Natural Gas Rate Design**

### **1. Residential Rate Design**

134. PSE proposes to increase the residential basic charge to \$11 per month from its current rate of \$10.34 per month.<sup>290</sup> The cost of providing this service is \$15.62.<sup>291</sup> PSE's proposal is a gradual move towards the cost of service, which Public Counsel accepts.<sup>292</sup> Commission Staff proposes a higher basic charge of \$12.04 per month,<sup>293</sup> and PSE approves of the greater alignment of customer costs and customer-related revenue presented in that proposal.

### **2. Non-Residential Rate Design Proposals**

135. Commission Staff supports PSE's proposal to move non-residential demand charges 25 percent towards their calculated cost of service.<sup>294</sup> No other party provided evidence on this issue. PSE's proposal should be accepted by the Commission.

136. PSE's proposed changes to procurement charges are uncontested and should be approved. The procurement charge is intended to recover the cost associated with procuring and managing gas supply for sales customers and to recover the cost associated with PSE's storage facilities used to manage gas supply for its sales customers.<sup>295</sup> This charge currently applies to non-residential gas customers served under gas Schedules 85, 86 and 87.<sup>296</sup>

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<sup>289</sup> See *id.* at 15:4-21.

<sup>290</sup> See Piliaris, Exh. JAP-1T at 91:1-93:22.

<sup>291</sup> See *id.* at 91:4-5.

<sup>292</sup> See Watkins, Exh. GAW-1T at 69:18-23.

<sup>293</sup> See Ball, Exh. JLB-1T at 22:1-2.

<sup>294</sup> See *id.* at 55:1-56:6.

<sup>295</sup> See Piliaris, Exh. JAP-1T at 96:10-13.

<sup>296</sup> See *id.* at 96:15-16. PSE proposes to (i) extend the application of this charge to non-residential customers served under Schedules 31 and 41, (ii) eliminate the Gas Procurement Credit for customers served under Schedule 31T and 41T, and (iii) update the Gas Procurement Charge to reflect current costs for each schedule to which it applies. See *id.* at 97:1-98:15

137. PSE requests the Commission approve three proposed changes to its base natural gas tariffs for non-residential gas customers. First, PSE proposes to implement annual maximum volume limitations on Schedules 41 and 41T, effectively requiring customers exceeding these volume limits to take service on Schedule 85 or 85T.<sup>297</sup> Second, PSE proposes to eliminate the existing annual minimum load charge on Schedules 85 and 85T.<sup>298</sup> Third, to ease the transition, PSE proposes to charge fully-firm customers on Schedules 85 and 85T based on their actual demands and to relieve gas sales customers receiving fully-firm service of the obligation to sign a separate customer agreement for service under these schedules.<sup>299</sup>

138. The Settlement Agreement provides that PSE, Staff, and other interested stakeholders will discuss the future of the water heater rental program in PSE's natural gas schedules.<sup>300</sup> Commission Staff had proposed, in its litigated case, that the water heater rental tariffs be eliminated and the lost revenue from this service be allocated to other customers through the rate spread process.<sup>301</sup> Given the terms of the Settlement Agreement, it is unnecessary to impute the loss of revenues from PSE's water heater rental program to other customers at this time.

DATED this 18th day of October, 2017.

**Respectfully submitted**

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<sup>297</sup> See Piliaris, Exh. JAP-1T at 101:1-104:1.

<sup>298</sup> See Piliaris, Exh. JAP-1T at 104:2-105:11

<sup>299</sup> See *id.* at 105:12-106:11.

<sup>300</sup> Settlement Agreement at ¶ 123.

<sup>301</sup> See Ball, Exh. JLB-1T at 13:8-22.

# **ATTACHMENT A**

**Puget Sound Energy**  
**Summary of Proposed Rate Design**  
**Docket No. UE-170033**

Line No.	Rate Schedule	Tariff	Percent of Uniform Increase	Basic Charge	Demand Charge	Reactive Power Charge	Energy Charge	Lamp Charge
1	Residential	7	100%	\$9	na	na	Remaining class average increase, 1st Block adjusted for residual	na
2	Sec Volt <= 50 kW Demand	8/24	75%	Class average increase	na	na	Class average increase, Winter Block adjusted for residual	na
3	Sec Volt 50 > kW Demand <=350	7A/11/25	65% *	Class average increase *	Remainin increase *	Remaining increase *	Block 1- Increase Demand portion Block 2- No increase *	na
4	Sec Volt > 350 kW Demand	12/26	65% *	Class average increase	Sch 31, adjusted for losses	Class average increase	Sch 31, adjusted for losses	na
5	Sec Volt, Irrigation	29	65% *	Class average increase	Class average increase	Class average increase	Class Average Increase, All Blocks	na
6	Pri Volt - Gen Svc	10/31	65% *	Class average increase	Class average increase	Class average increase	Class average increase, Adjusted for Residual	na
7	Pri Volt - Irrigation	35	150%	Same as Schedule 31	Class average increase	Class average increase	Residual	na
8	Pri Volt - Interruptible Schools	43	100%	Same as Schedule 31	Class average increase	Class average increase	Residual	na
9	Campus Rate	40	Cost Based *	Sch 25, 26 or 31	Sch 49, Adjusted for Power Factor and Line Losses Distribution Demand Adjusted \$250k for Ardmore Substation *	Sch 26 or 31	Sch 49, Adjust for Line Losses	na
10	High Volt - Interruptible	46	65% *	na	Increase 48% *	na	Same as Schedule 49	na
11	High Volt - Gen Service	49	65% *	na	Increase 48% *	na	Remaining increase, Adjusted for Residual *	na
12	Lighting	50-59	100%	na	na	na	na	See Testimony
13	Choice / Retail Wheeling	448/449	Cost Based	COS Basic Charge	na	na	na	na

\* - Included in Multi-Party Settlement Stipulation and Agreement