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*)**

REPLY BRIEF OF PUGET SOUND ENERGY

OCTOBER 27, 2017

PUGET SOUND ENERGY

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I. INTRODUCTION

1. Puget Sound Energy ("PSE") filed an Initial Brief that summarizes and supports PSE's requests for (i) approval of the Multiparty Settlement Stipulation and Agreement ("Settlement Agreement") and rejection of Public Counsel's proposed changes to the Settlement Agreement; (ii) approval of PSE's electric cost recovery mechanism ("ECRM") and electric reliability plan ("ERP"); (iii) continuation of electric and natural gas decoupling mechanisms with minor adjustments proposed by PSE; and (iv) approval of PSE's electric and natural gas cost of service, rate spread, and rate design for those issues not included in the Settlement Agreement. Many of the arguments raised by other parties in their initial briefs have already been addressed by PSE in its Initial Brief. As such, PSE will not repeat all those arguments in this Reply Brief. However, when viewed in the context of other parties' proposals, PSE's litigated case, combined with the Settlement Agreement, appropriately balances the interests of customers and PSE. PSE's case avoids intergenerational inequity and it responds to customers' requests to improve reliability through targeted actions and to move towards a reduced carbon footprint. PSE's case is consistent with the public interest and should be approved.

II. CONCERNS RAISED REGARDING THE ECRM ARE OVERSTATED AND DO NOT ACCOUNT FOR THE SIGNIFICANT BENEFITS THE ECRM WILL PROVIDE

A. The Obligation to Provide Safe and Reliable Services Does Not Preclude the Use of an Alternative Recovery Mechanism

2. Some parties opposing the ECRM have suggested that because PSE has an obligation to provide safe and reliable service that it should not be able to seek recovery through an alternative mechanism.[1] This position is unwarranted and is unsupported by any legal authority. While PSE has an obligation to provide reliable service to customers, it also has a corresponding right to reasonable recovery for providing such services.[2] The Commission has a duty to facilitate that

[1] *See, e.g.*, Commission Staff Initial Brief at ¶ 98.
[2] *People's Org. for Wash. Energy Res. v. WUTC*, 104 Wn.2d 798, 808 (1985) (en banc) ("*POWER*"); *Puget Sound Traction Light & Power Co. v. Pub. Serv. Comm'n*, 100 Wn. 329, 334 (1918) (en banc); RCW 80.28.010(1).

process through reasonable rate recovery, including when targeted areas of reliability concern are identified.[3] And there are circumstances where traditional ratemaking simply does not provide adequate and timely recovery, including where a utility needs to make a significant long capital investments, as set forth in this case.[4] In these instances, alternative mechanisms have been permitted, such as the Gas Cost Recovery Mechanism ("Gas CRM"). PSE has provided extensive evidence regarding the high cost of fully resolving reliability issues with the high molecular weight ("HMW") direct bury cable and the worst performing circuits ("WPCs") and that, without an alternative mechanism, PSE will be unable to aggressively fund these projects given its other substantial reliability obligations.[5] PSE's ERP and ECRM are a fulfillment of PSE's duty and desire to increase reliability to its customers.

3. Likewise, Public Counsel and Commission Staff have an obligation to take into consideration customer desire for increased reliability and be creative in looking for solutions that are also workable for PSE. In this case, however, both appear more intent on ignoring the acute need to proactively address the HMW cables and the WPCs when PSE has provided significant evidence that the most effective way to adequately address these reliability issues is through an alternative mechanism. Remarkably, many parties, including Staff, question whether there is even a need to address the HMW cables and WPCs in an aggressive manner despite the overwhelming evidence PSE has provided otherwise.[6] If the parties are truly interested in improving reliability and wanting to see better SAIDI results, for example,[7] then they should be open to alternative mechanisms that will unquestionably improve reliability for customers. Instead, the parties challenge and question PSE's prioritization methodology and allocation of capital spending on reliability projects without any evidence that PSE has somehow been

[3] RCW 80.28.010(1).
[4] *See* PSE Initial Brief at ¶¶ 42-46.
[5] *Id.* ¶¶ 42-43.
[6] *See, e.g.*, Commission Staff Initial Brief at ¶ 97; ICNU Initial Brief at ¶ 24.
[7] *See* Koch, Exh. CAK-3C at 7-8, 13-14 (discussing the extensive benefits that the ERP and ECRM will provide, including improvement in SAIDI and SAIFI performance).

imprudent on either front.[8] In actuality, the opposite is true. PSE has provided substantial evidence demonstrating that its allocation of available capital is appropriate[9] and that PSE's optimization process is aimed at maximizing resources to provide the greatest reliability benefits to the most customers.[10] For example, there is no evidence that PSE is failing to meet its current reliability obligations or is inadequately investing in capital spending. The ERP and ECRM would simply make it possible for PSE to accelerate the replacement of the failing HMW cable and invest more resources in addressing WPCs to prevent future reliability problems from these segments of PSE's distribution system, both of which would unquestionably benefit customers.

B. The Gas CRM Provides An Appropriate Model For the ECRM

4. The use of alternative cost recovery mechanisms has increased by regulatory commissions across the country, including the Commission. As explained by Staff, "[c]ost recovery mechanisms and trackers are a common tool in the Commission's regulatory toolbox"[11] and Commission Staff notes the numerous circumstances "in recent years" where the Commission has approved various cost recovery mechanisms, including the Gas CRM.[12] Likewise, PSE has cited numerous examples where commissions across the county have authorized various alternative mechanisms to fund capital investment in electric infrastructure repair and/or replacement.[13]

5. However, some parties have suggested that the Gas CRM is not an appropriate point of comparison because the purpose of the Gas CRM was to replace "vulnerable natural gas pipelines," the Gas CRM "was preceded by numerous meetings with natural gas companies and Commission-sponsored workshops," the risks "were known by both utilities and the Commission," and were prompted by natural gas pipeline explosions.[14] But these factors in no

[8] *See* Commission Staff Initial Brief at ¶¶ 98-100; ICNU Initial Brief at ¶¶ 25-29.
[9] Doyle, Exh. DAD-7T at 26:1-21; Doyle, Tr. 180:9 – 183:4.
[10] *See* PSE Initial Brief at ¶¶ 39-41.
[11] Commission Staff Initial Brief at ¶ 87.
[12] *Id.*
[13] *See* PSE Initial Brief at ¶¶ 47-49.
[14] *Id*. ¶ 37.

way demonstrate that a comparable mechanism cannot be implemented to address significant reliability problems with PSE's electric system. By comparison to the justifications for the Gas CRM, it is undisputed that the HMW cable and WPCs also have significant reliability issues that need immediate attention,[15] that there is a strong customer demand to address these issues,[16] that the impacts of electric system failure can be significant,[17] and that the cost to fully address the HMW cable and WPCs is monumental and will likely even exceed the amount spent on the Gas CRM.[18] In addition, the HMW cable and WPCs issues are known and well understood by the Commission and have been documented for decades.[19]

6. Moreover, any suggestion that an alternative mechanism is only appropriate where there is a public safety concern is simply not credible.[20] There is no Commission requirement that a safety concern precede an alternative mechanism; indeed, most alternative mechanisms do not have such a concern. In fact, as Commission Staff concedes, even the Gas CRM was not implemented because of an imminent safety risk as "Washington state's gas infrastructure is relatively modern and regulated gas utilities had very little of the highest risk and dangerous pipe in service."[21] Rather, the Gas CRM was implemented to proactively replace aging pipelines, not dangerous ones.[22] As explained by Ms. Koch, "PSE addresses dangerous or unsafe pipelines immediately, and they are not part of the Gas CRM process. The Gas CRM allows for the proactive replacement of failing pipelines to prevent the occurrence of leaks and their impact. Similarly, the ECRM proactively addresses HMW direct bury cable that are failing to prevent outages and subsequent impact. Doing this ensures the electric system is reliable and minimizes safety and other concerns resulting from outages such as street lights, traffic signals, climate

[15] *Id.* ¶¶ 33-41.
[16] Koch, Exh. CAK-4T at 15:1 – 16:14.
[17] Koch. Exh. CAK-1CT at 19:12-21; Koch. Exh. CAK-4T at 12:1-13, Koch, Exh. CAK-3C at 10-11.
[18] *See* Doyle, Exh. DAD-7T at 24:15-18 (noting for 2017 spending on the ERP will exceed what it spends on the Gas CRM); Koch, Exh. CAK-4T at 4-15; Koch, Exh. CAK-3C at 6, 11.
[19] *See* Koch, Exh. CAK-3C at 1-4, 8-10.
[20] *See* Commission Staff Initial Brief at ¶ 95.
[21] *Id.* ¶ 91.
[22] Koch, Exh. CAK-4T at 12:2-13.

control, security systems, and other frustrations associated with power outages."[23] The purpose of the Gas CRM was to provide PSE with the ability to efficiently recover its capital expenditures to proactively improve its pipeline system. Similarly, in this case, the purpose of the ECRM is so PSE can expend the capital resources needed to expeditiously replace the failing HMW cable and adequately address the WPCs in the aggressive time period set forth in the ERP.

7. Commission Staff diminishes the importance of maintaining a reliable electric distribution system and suggests that unless "widespread failure" is imminent, an alternative mechanism is unnecessary.[24] The notion that failure must occur before action is nonsensical and harms customers. Additionally, Commission Staff discounts the importance of aggressively replacing the failing HMW cable and states that it "does not understand how the last 40 percent of bad cable could be a safety issue that merits alternative ratemaking when the first 60 percent did not."[25] It has taken PSE nearly three decades to replace 2,500 miles of HMW cable and PSE has provided clear evidence that the failure rate of HMW cable is increasing exponentially and is occurring faster than the rate of replacement. Without replacement, significant failures could in fact occur.[26] Without the ECRM, given the other reliability demands on PSE's system, it will take PSE at least 25 years to replace this cable.[27] Apparently, Commission Staff would prefer that total failure to occur before replacement. PSE has demonstrated that customers desire reliable service and are willing to pay for it.[28] The better approach for HMW cable, as demonstrated by the Gas CRM, is anticipatory replacement before catastrophic failure does in fact occur.[29] The same holds true for the WPCs where the risk of failure is significant and where PSE has received numerous requests by PSE customers that more be done to address the reliability problems.[30] PSE is surprised that both Commission Staff and Public Counsel have

[23] *Id.* at 12:7-13.
[24] *See* Commission Staff Initial Brief at ¶¶ 95-97.
[25] *Id.* ¶ 97.
[26] PSE Initial Brief at ¶¶ 33-37, 50-51.
[27] PSE Initial Brief at ¶¶ 35-37.
[28] Koch, Exh. CAK-4T at 15:14 – 16:14.
[29] PSE Initial Brief at ¶ 40; Koch, Exh. CAK-3C at 5, 10-11.
[30] Koch, Exh. CAK-4T at 15:14 – 16:14.

taken such a disinterested position in addressing these well-documented reliability issues. Staff's position harms PSE's customers and ignores customers' interests.

8. Finally, no party has denied that the Gas CRM has been an overwhelming success.[31] PSE has been able to replace the pipelines as planned and has been able to recover its costs without even a whisper of concern by the other parties.[32] The Gas CRM has been successful because the mechanism is targeted and straightforward, which has allowed PSE to work diligently to accomplish the purposes of the Gas CRM and efficiently recover its costs. The ECRM would provide a nearly identical process that would allow PSE to aggressively replace the failing HMW cable and WPCs in a far more accelerated manner than otherwise possible. The Gas CRM provides a proven framework to efficiently implement a plan to replace failing infrastructure. There is simply no reason to not implement the ECRM when it would mean replacement of failing distribution systems, better reliability, and all much sooner than otherwise possible. As explained by Ms. Koch, "[t]he ECRM mechanism would leverage the extensive roadmap established by the Gas CRM process, but does not need to be reinvented through lengthy proceedings."[33] The framework is already in place and there is no good reason not to utilize it.

C. The Suggestion That PSE Is Attempting to Capitalize Off the ECRM Is False

9. Public Counsel misconstrues PSE's testimony by suggesting that PSE is intentionally delaying replacement of the HMW cable and addressing the WPCs by diverting capital resources elsewhere in an attempt to effectively game the system.[34] PSE takes seriously its duty to provide reliable service to customers and PSE is constantly searching for ways to improve reliability both by responding to reliability issues as they occur and by anticipating reliability issues that could arise in the future.[35] The ERP and ECRM are a manifestation of PSE's desire to fully address

[31] *Id.* at 11:10-21.
[32] *Id.* at 8:16 – 9:12.
[33] *Id.* at 11:19-21.
[34] Public Counsel Initial Brief at ¶¶ 25-26.
[35] PSE Initial Brief at ¶ 57; Koch, Exh. CAK-4T at 12:14 – 13:5, 13:18 – 17:15.

reliability concerns regarding two key areas of its system—not capitalize off it.[36] Public Counsel's accusation that PSE is proposing the ERP and ECRM to "earn higher future returns by limiting spending on discretionary capital"[37] and that PSE is trading earnings for service quality is totally false and not supported by any evidence in the record. As PSE has shown repeatedly in this case, it has spent millions in addressing HMW cables and the WPCs for decades[38] and is only proposing the ERP and ECRM because it will be better for customers if both of these issues are resolved sooner.[39] Moreover, Public Counsel's suggestion that PSE can deduct accelerated and bonus tax depreciation[40] as a mechanism to finance the ERP reflects a fundamental misunderstanding of PSE's proposed revenue requirement regarding the ECRM which expressly factors in the impacts of bonus depreciation which benefits are already being passed on to customers[41]—in other words, the ECRM is already doing what Public Counsel proposes.

D. The Policy Surrounding Single Issue Ratemaking Does Not Preclude the ECRM

10. Some parties have suggested that the ECRM is improper because it constitutes single-issue ratemaking.[42] First, the ECRM is not single-issue ratemaking because as explained by Commission Staff, single-issue ratemaking cannot occur in the context of a general rate case where as in this case, "[t]he Commission is faced with dozens of issues to consider."[43] Second, the parties mistake the Commission's general policy for a binding rule. As explained in PSE's Initial Brief, the Commission has the discretion to implement alternative ratemaking mechanisms when it determines that doing so is in the public interest and that resulting rates are just, reasonable, and compensatory.[44] The Commission has repeatedly emphasized that its general

[36] PSE Initial Brief at ¶¶ 41, 43, 58; Koch, Exh. CAK-1T at 2:8 – 9:3, 12:6 – 19:21; *see generally* Koch, Exh. CAK-3C.
[37] Public Counsel Initial Brief at ¶¶ 25-26.
[38] PSE Initial Brief at ¶¶ 34, 37-38, 40.
[39] *Id.* ¶¶ 50-58.
[40] Public Counsel Initial Brief at ¶ 26.
[41] *See* Barnard, Exh. KJB-9.
[42] Public Counsel Initial Brief at ¶ 25.
[43] Commission Staff Initial Brief at ¶ 81.
[44] PSE Initial Brief at ¶¶ 47-49.

policy against single-issue ratemaking is general only, and a matter of policy not law, and thus has deviated from this policy many times.[45] "The ultimate determination to be made by the Commission in a rate proceeding is whether the proposed rates and charges are fair, just, reasonable, and sufficient."[46] As outlined in PSE's Initial Brief, the Commission has approved of numerous alternative ratemaking mechanisms in a variety of scenarios, including as discussed above, the Gas CRM, in similar circumstances as presented here.[47]

E. The ECRM Process Does Not Amount to Pre-Approval of Rates That Are Not Known and Measurable

11. Some parties have also suggested incorrectly that the ECRM amounts to pre-approval of rates that are not known and measurable.[48] This is a distortion of the ECRM and ignores that the ECRM is expressly modelled after the Gas CRM which the Commission approved.

12. As part of the ECRM, PSE is not asking for pre-approval or for investments to be put into rates prior to being known and measurable nor would it eliminate the prudence test.[49] Rather, the ECRM requests the same process as the Gas CRM which provides for Commission approval of the annual plan and that the spending proposed by PSE is a reasonable and measured approach to improving reliability for customers and ensures engagement through the process.[50] But this process does not replace or supplant the prudence review that occurs at the next general rate case.[51] Following the Gas CRM process, every two years, PSE would submit a work plan to Commission Staff representing the two forward-looking years, containing the projects that PSE intends to complete during that time period.[52] These projects are determined by PSE and are

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[45] *See, e.g., Wash. State Attorney Gen.'s Office, et al. v. PacifiCorp d/b/a Pac. Power & Light Corp.*, UE-110070, Order 01 ¶ 42 (Apr. 27, 2011) (acknowledging that "it generally is a matter of policy, not law" but rejecting single issue ratemaking under the circumstances).
[46] *MCI Telecom. Corp., v. GTE Nw., Inc.*, Docket UT-970653, Second Supp. Order Dismissing Comp. (Oct. 22, 1997) (internal citation omitted).
[47] PSE Initial Brief at ¶¶ 47-49; Koch, Exh. CAK-4T at 5:3-18.
[48] Commission Staff Initial Brief at ¶¶ 86, 94; ICNU Initial Brief at ¶¶ 33-34.
[49] Koch, Exh. CAK-4T at 7:16 – 8:1.
[50] *Id.* at 7:3-6.
[51] *Id.* at 8:6-7.
[52] Koch, Exh. CAK-1CT at 6:1 – 12:3; Barnard, Exh. KJB-1T at 73:14 – 83:13; Koch, Tr. 195:15-20, 197:6-17; Koch, Exh. CAK-3C.

submitted to Commission Staff six months ahead of the date in which a ERP project would begin.[53] The Commission's role in reviewing the work plan is to determine whether the projects achieve the objectives and purposes of the ERP and ECRM.[54]

13. Through the ECRM, PSE and the Commission can review the progress, objectives, and expenditures of the ERP on an annual basis instead of waiting until the next GRC.[55] Just as the Gas CRM currently operates now, while PSE would still determine what projects it will complete under the ERP and ECRM, Commission Staff and other interested stakeholders would have the opportunity to engage with PSE in discussing PSE's project plans to ensure that the projects selected benefit customers.[56] This transparency benefits customers, PSE, and the Commission because it ensures the most efficient use of resources in addressing reliability.[57]

14. Nor would the Commission be acting as a super-manager to review and decide for PSE which projects it should pursue. Contrary to ICNU's overstated concern, PSE is not deferring "distribution infrastructure investment decisions to the Commission for final approval."[58] Under the ECRM, like the Gas CRM, PSE would still follow its internal process in determining which projects should be prioritized.[59] The Commission's role is simply to confirm from a high level that the objectives of the ERP and ECRM are being achieved which is the exact same role it assumes with the Gas CRM.[60] There is nothing new or novel about this process as the Commission and its Commission Staff are closely involved in numerous aspects of PSE's utility operations.

15. Finally, Commission Staff's suggestion that it lacks the expertise to review PSE's plans under the ERP is simply not credible.[61] The ERP review process is a question of whether the

[53] Koch, Tr. 197:20 – 198:3.
[54] Koch, Tr. 196:2-11.
[55] Koch, Exh. CAK-4T at 4:15-18.
[56] *Id.* at 4:18 – 5:1.
[57] Koch, Exh. CAK-1CT at 7:16-22.
[58] ICNU Initial Brief at ¶ 32.
[59] Koch, Tr. 199:1 – 200:10.
[60] Koch, Tr. 200:11-25.
[61] Commission Staff Initial Brief at ¶¶ 92-94.

plans are reasonable and does not require a detailed engineering study requiring expert analysis. Again, that is PSE's role. Moreover, Commission Staff routinely undertakes prudence reviews of new electric plant in service in general rate cases. Commission Staff is already engaged in reviewing electric reliability plans associated with the econometric reliability benchmark study per WUTC Docket U-151958 and the IRP rulemaking per WUTC Docket U-161024.[62] Commission Staff also collaborates with PSE on its SAIDI and SAIFI standards in litigated proceedings as well as informally.[63] Commission Staff's role would not exceed the expertise it already utilizes in working with utilities generally, a role it has performed countless times before.

F. Concerns Raised by ICNU Relating to Capital Expenditures, Regulatory Lag, and Attrition Are Inaccurate and Misguided

16. ICNU raises a variety of arguments against the ECRM relating to capital expenditures, attrition, and regulatory lag, all of which are red herrings. First, ICNU makes the unfounded assertion that PSE was required to first demonstrate "that dividends to its owners have been or would be compromised in order to fund distribution infrastructure" before seeking an alternative mechanism.[64] Then ICNU appears to be suggesting that to the extent there are dividends, that PSE should avoid passing along any costs to customers by paying less dividends.[65] The problem with ICNU's proposal is where would it stop; there are numerous scenarios where a utility could theoretically stop compensating investors and instead finance utility expense. ICNU's proposal is simply bad policy—shareholders should receive appropriate dividends if a company is doing well. Moreover, no party has claimed that PSE is inappropriately making dividends nor has ICNU provided any authority to support its proposition. And there is no evidence that PSE or Puget Holdings have disregarded their commitment to make delivery infrastructure a "high priority" as ICNU implies. In fact, Public Counsel's expert even concedes that PSE has

[62] Koch, Exh. CAK-4T at 9:13-18.
[63] *See, e.g., WUTC v. Puget Sound Energy*, Dockets UE-072300 & UG-072301, Order 29 (June 17, 2016) (approving updated SAIDI metrics in settlement supported by Commission Staff).
[64] ICNU Initial Brief at ¶¶ 27-28.
[65] *Id.* ¶¶ 27-29.

"prudently invested in needed electric utility reliability investments in prior years."[66] The ECRM is actually a manifestation of PSE's commitment to infrastructure and to the recognition that in order to adequately address these reliability issues, more aggressive spending is necessary. PSE's request to accelerate this work and to receive more timely rate recovery is not inconsistent with the 2008 merger order or any other obligations.

17. Second, ICNU squanders several paragraphs in its initial brief discussing how "PSE presents no attrition study to support its claims,"[67] which is correct. The ECRM is not an attrition adjustment and the Commission has never stated that a showing of attrition is a prerequisite to an alternative cost recovery mechanism. For example, a showing of attrition was not required by the Commission involving the Gas CRM. ICNU also ignores the substantial evidence demonstrating that PSE would not have earned its authorized rate of return in 2015 or 2016 absent the combined effect of the K-factor and the ERF. Mr. Doyle provides an analysis in his rebuttal testimony[68] and concludes that "[w]ithout the benefit of the 2013 ERF and the ensuing K-factor increases, PSE would have substantially under-earned against its allowed rate of return and return on equity on both an actual and normalized basis for both electric and gas operations. It is important to note that neither the expedited rate filing nor the K-factor increases would have been sufficient *on their own* to close the return gap created by regulatory lag and attrition." [69]

18. ICNU also tries to diminish the adverse effects of regulatory lag by arguing that the statutory framework under RCW 80.04.130 that creates the suspension period expressly mandates regulatory lag.[70] But ICNU has flipped the purpose of RCW 80.04.130 on its head. The statute simply provides that "the commission may suspend the operation of such rate, charge, rental, or toll for a period not exceeding ten months."[71] The law does not prescribe that a

[66] Brosch, Exh. MLB-1T at 59:13-18.
[67] ICNU Initial Brief at ¶¶ 13-18.
[68] *See* Doyle, Exh. DAD-7T at 9:6 – 10:9.
[69] *Id.* at 10:4-9.
[70] ICNU Initial Brief at ¶ 20.
[71] RCW 80.04.130(1).

case must take ten months, and the Commission certainly has discretion to take less. This statute actually protects utilities from prolonged regulatory litigation. Notably, ICNU concedes that "regulatory lag should [not] be allowed to unconstitutionally impair the earnings of the Company,"[72] but then ignores that PSE has shown how it will be adversely impacted by regulatory lag in this case, to a tune of at least $20 million per year.[73]

19. Finally, ICNU also argues that assuming that the ERF and decoupling are permitted to continue, the Commission should wait to approve the ECRM to see if the ERF and decoupling are sufficient to address the work on the HMW and WPCs. However, as discussed above, without the K-factor and ERF, PSE would not have earned its authorized return.[74] Now it is proposing to significantly accelerate reliability work in addition to losing the K-factor. There is no need to wait to see if the ERF and decoupling are sufficient to address the work proposed under the ERP because as Mr. Doyle's testimony makes clear, they are not.

G. ECRM Conclusion

20. Reliability is of critical importance to PSE and the Commission. Indeed, unlike other utilities, PSE is subject to significant penalties for failure to meet its reliability obligations. In this case, PSE has identified two targeted areas of its electric distribution system that need large capital investments in order to resolve their reliability issues. To address those issues, PSE has proposed the ECRM which mirrors a proven mechanism recently authorized by the Commission. By implementing the ECRM and corresponding ERP, PSE will significantly improve the reliability and stability of PSE's electric distribution system at a rate much faster than otherwise possible, which will benefit customers. PSE requests that the Commission authorize the ECRM.

[72] ICNU Initial Brief at ¶ 21.
[73] Koch, Exh. CAK-4T at 15-18; Barnard, Exh. KJB-17T at 100:19 – 101:2.
[74] *See* Doyle, Exh. DAD-7T at 9:6 – 10:9.

II. RESPONSES TO DECOUPLING CONCERNS RAISED BY PARTIES

A. The Evidence Does Not Support Public Counsel's Concerns of Found Margin

21. The revenue per customer approach to decoupling approved by the Commission in 2013 has not resulted in "found margin" as Public Counsel asserts. "Margin" requires an evaluation of incremental revenue and incremental cost. As recognized by the Commission in the Decoupling Policy Statement, "revenue associated with new customers is offset by the costs to serve those customers."[75] PSE has demonstrated in this case that the cost for serving new customers exceeds the revenue generated from the new customers by 1.2 percent per year; therefore there is no found margin.[76]

22. In claiming that new customers constitute "found margin," Public Counsel and The Energy Project consider only the incremental revenue and ignore the incremental costs associated with new customers.[77] It is ironic that Public Counsel and The Energy Project disregard the incremental cost for serving new customers at the same time they are attempting to prevent some of these new costs—such as transformers—from being recovered in basic charges. Moreover, Public Counsel's claim that most "fixed costs do not vary with the number of customers served"[78] is incorrect, as PSE has demonstrated.[79] Commission Staff's analysis likewise provides evidence that new customers produce new costs.[80]

23. The Commission rejected similar arguments of found margin by Public Counsel and ICNU in the 2013 PSE decoupling case. The Commission stated that although there was "a potential for PSE to capture found margin from new customers that will more than offset the cost

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[75] *In the Matter of the Washington Utilities and Transportation Commission's Investigation into Energy Conservation Incentives*, Docket U-100522, Report and Policy Statement on Regulatory Mechanisms, Including Decoupling, to Encourage Utilities to Meet or Exceed Their Conservation Targets n.44 (Nov. 4, 2010) ("Decoupling Policy Statement").
[76] *See* Barnard, Exh. KJB-1T at 6:10-11; Piliaris, Exh. JAP-46CT at 23:9-14.
[77] *See, e.g.*, Brosch, Exh. MLB-1T at 30:14-17 (referencing only the sales and revenue growth from new customers without consideration of the costs to serve the new customers); s*ee also* The Energy Project Initial Brief ¶ 31 (citing Brosch testimony).
[78] Public Counsel Initial Brief at ¶ 14.
[79] *See* Piliaris, Exh. JAP-46CT at 44:8 – 49:3 (line transformer costs), 50:10 – 51:13 (overhead administrative costs).
[80] *See* Liu, Exh. JL-1CT at 49:15 – 50:2.

of servicing those customers" it was "equally plausible that PSE's cost per customer will continue to increase and outstrip increased revenue from new customers"[81] and the evidence in that case demonstrated that PSE's costs per customer had indeed outstripped customer growth.[82] Therefore, the Commission concluded there was no found margin. Moreover, the Commission pointed to the earnings sharing mechanism as a means to "keep any excess earnings that may be attributable in part to customer growth from becoming a windfall for PSE."[83]

24. In its Initial Brief, Public Counsel claims there is a misunderstanding with respect to Public Counsel's recommendation on decoupling. For the first time, Public Counsel asserts that "[u]nder Public Counsel's proposal, PSE's expenses would not be factored down, but rather would be determined at the appropriate level and allowed under the decoupling mechanism."[84] PSE welcomes Public Counsel's new assertion, on brief, that the production factor would not be applied to PSE's expenses. However, PSE is unable to glean this from Public Counsel's testimony, nor does Public Counsel's brief cite to evidence supporting this characterization of its approach.

B. PSE's Adjustments to the Earnings Sharing Mechanism Are Reasonable

25. Public Counsel posits arguments regarding the earnings sharing mechanism that are irrelevant and contradictory. As discussed in more detail below, the Commission should reject these arguments and approve the two adjustments PSE proposes to its earnings sharing mechanism.

[81] *In the Matter of the Petition of Puget Sound Energy and Northwest 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 ¶ 116 (June 25, 2013) ("2013 Decoupling Order").
[82] *See id.*
[83] *See id.*
[84] Public Counsel Initial Brief at ¶ 17.

1. PSE Has Not Proposed to Remove the Earnings Sharing Mechanism

26. Public Counsel argues that "[r]emoving the Earnings Test would expose ratepayers to risk they do not currently bear and have no control over."[85] This argument is irrelevant since PSE has not proposed to remove the earnings sharing mechanism. Rather, PSE has proposed a 25 basis point deadband before customer share in earnings above PSE's authorized ROE. Additionally, it is not clear how customers "bear risk" with an earnings sharing mechanism that allows them to share in earnings that exceed PSE's authorized rate of return by 25 basis points. Customers have the opportunity to share in a benefit. They are not placed at risk by sharing in PSE's earnings that exceed the authorized rate of return.

2. Normalization Adjustments are Appropriate for Rate Cases and the CBR but Should Not Be Considered for Purposes of the Earnings Sharing Mechanism

27. Public Counsel's opposition to PSE's proposal to remove normalization adjustments from the earnings sharing calculation is fraught with contradictions. Public Counsel acknowledges that the earnings sharing mechanism provides a significant incentive for PSE to control its costs, but Public Counsel inconsistently argues that factors over which PSE has no control, such as weather and power supply, should be normalized in the earnings sharing mechanism.[86] When these results are normalized they can skew PSE's actual results, mask the effects of PSE's efforts to control costs,[87] and produce unexpected and irrational results.[88]

28. It is important to note that PSE is *not* proposing to remove the normalizing adjustments from the Commission Basis Reports.[89] While it is appropriate to use normalizing adjustments when setting base rates and for periodic review of PSE's performance against specified standards, the analysis changes when the Commission is taking the extraordinary step of

[85] *Id.* ¶ 22.
[86] *Id.* ¶ 23.
[87] *See* Doyle, Exh. DAD-1T at 20:13-15 ("Normalization adjustments can skew, and have skewed, the measurement of financial performance for excess earnings sharing purposes.").
[88] *See id.* at 19:1-3.
[89] *See* Barnard, Exh. KJB-17T at 64:5-19 (normalization adjustments are appropriate for ratemaking and Commission Basis Report purposes but are inappropriate for earnings sharing purposes where these adjustments distort PSE's actual earnings by pretending normal conditions occurred).

requiring a utility to share its earnings with customers. An earnings sharing mechanism is not a part of the traditional rate making paradigm.[90] Under those special circumstances in which earnings sharing is allowed, the sharing should be required only when the utility actually earns at the prescribed level above its authorized rate of return. The utility should not be required to share hypothetical earnings based upon normalized circumstances that did not occur. Under the current earnings sharing mechanism, PSE has shared phantom earnings that were not actually earned.[91]

3. A 25 Basis Point Deadband is Appropriate Given the Elimination of the Rate Plan, Annual Escalations and the Adjustment of PSE's ROE

29. PSE's Initial Brief addressed the reasons for adjusting the earnings sharing mechanism to include a 25 basis point deadband before customers begin sharing in earnings that exceed the authorized rate of return. Public Counsel completely misses the mark by suggesting the asymmetry that characterizes the earnings sharing mechanism was put into place to "reflect the control over costs and the ability of utility management to determine when to request rate relief."[92] Utilities have been expected to control costs and also have been able to determine when to request rate relief for several decades without the imposition of an earnings sharing mechanism. Rather, the earnings sharing mechanism was proposed by PSE in 2013 in conjunction with its (i) proposal for a multi-year rate plan with annual increases in delivery revenue and decoupling mechanisms and (ii) ROE remaining at the 9.80 level approved in 2012.

30. The facts before the Commission are different today than they were in 2013. With the removal of the multi-year rate plan and its annual increases in revenue, as well as the 30 basis point decrease to PSE's ROE in this case, there arguably is no longer a reason to include an earnings sharing mechanism. However, PSE is proposing a middle ground. The earnings sharing mechanism should have a 25 basis point deadband and should be based on actual earnings. This

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[90] *See, e.g., Petition of Commonwealth Edison Company for approval of an Alternative Rate Regulation Plan,* Docket 10-0527, 2011 WL 2115070, at *6 (Ill.C.C. May 24, 2011) (citing Illinois statute listing alternatives to rate of return regulation, including but not limited to earnings sharing, rate moratoria, price caps or flexible rate options).
[91] *See* Doyle, Exh. DAD-1T at 19:4 – 20:2.
[92] Public Counsel Initial Brief at ¶ 24.

is not an unreasonable change given the cessation of the annual rate increases under the multi-year rate plan. In this regard, it is important to note that the Commission's discussion of the earnings sharing mechanism in the 2013 Decoupling Order falls under the discussion of the "multi-year rate plan" and does not fall under the discussion of decoupling. In other words, the Commission considered whether the earnings sharing mechanism adequately protected customers in the context of its discussion of the multi-year rate plan, not in its discussion of decoupling, which was a separate section of the 2013 Decoupling Order.[93]

31. Commission Staff attempts to rewrite history by suggesting that the Commission "summarily reject[ed]" PSE's proposal for a 25 basis point deadband in the earnings sharing mechanism in 2013.[94] If one reads beyond the introductory paragraph of the 2013 Decoupling Order, cited in Commission Staff's brief, to the substantive discussion of the earnings sharing mechanism, it is clear that the Commission did not summarily reject PSE's proposal. To the contrary, in 2013, the Commission reiterated its general view that companies should be incentivized to operate efficiently and it generally *avoided* artificially capping earnings because this could diminish the incentive for efficient management.[95] Despite this general philosophy against artificial caps, the Commission ultimately decided that under the circumstances that existed in the 2013 case— a multi-year rate plan with an ROE that remained unchanged from 2012 and was determined to be at the high end of the range of reasonableness—it would vary from its general philosophy and allow 50-50 sharing of earnings that exceeded PSE's authorized rate of return.[96]

32. As discussed in detail in PSE's Initial Brief, the circumstances are much different today. The Commission has substantial evidence before it to determine that PSE's ROE of 9.50 is within the range of reasonableness. The ROE agreed to by the ten Settling Parties decreases

[93] *See* 2013 Decoupling Order at ¶¶ 137-173 (discussing rate plan). In contrast, the Commission's discussion of decoupling can be found in paragraphs 81 through 136.
[94] Commission Staff Initial Brief at ¶ 84 (citing ¶ 26 of the 2013 Decoupling Order).
[95] 2013 Decoupling Order at ¶ 162.
[96] *See id.* ¶ 164.

PSE's current ROE by 30 basis points. Moreover, PSE no longer will receive annual increases in delivery revenue as it did during the multi-year rate plan. For these reasons, it is appropriate to take a second look at the earnings sharing mechanism and adjust it to comport with the Commission's philosophy and the facts presented in this case.

C. ICNU's Arguments Against Decoupling Lack Merit

1. ICNU's Claim that Decoupling is Illegal is Not Supported by the Law

33. In its initial brief, ICNU employs a new tact in its perennial battle against decoupling—decoupling is illegal. ICNU argues that the decoupling mechanisms violate Washington statutes and case law because, according to ICNU, customers are charged for a service never rendered. In support of its novel argument, ICNU purports to rely on RCW 80.28.010 and three Washington cases. However, none of the law cited by ICNU supports the proposition that decoupling is outside the Commission's statutory authority.

34. The Commission has authority to determine the ratemaking methodology to use in conjunction with the rendering of electric and natural gas service. Setting a revenue per customer rate through the use of revenue decoupling is wholly within the Commission's authority, and has been widely accepted by state commissions.[97] The revenue per customer decoupling mechanisms charge customers for electricity and gas service and for services to be rendered in connection therewith, as authorized by RCW 80.28.010 and 80.28.020. PSE's revenue decoupling mechanisms do not violate these statutes, as ICNU erroneously claims.

35. ICNU's claim that decoupling charges customers for nothing received is incorrect. Capacity costs are almost exclusively recovered through the allowed fixed production delivery revenue in decoupling.[98] Customers receive additional and avoided capacity from what ICNU

[97] Piliaris, Exh. JAP-46CT at 24:4-8.
[98] *See* Piliaris, Exh. JAP-1T at 91:14-17 (discussing linkage between capacity and delivery costs), 107:4-18 (referencing recovery of delivery costs in decoupling).

refers to as "negawatts."[99] Accordingly, there can be no doubt that the charges customers incur under PSE's decoupling mechanisms are for electricity and natural gas services.

36. The *POWER* case[100] cited by ICNU actually supports the broad power of the Commission to set rates under RCW 80.28.010 and .020, rather than limiting it. It does not prohibit revenue decoupling as ICNU claims. In *POWER*, the Washington Supreme Court affirmed the Commission's authority to allow Puget Sound Power & Light Company ("Puget") to include in rates as an operating expense the prudently incurred costs for the planning and designing of the subsequently canceled nuclear generating project at Pebble Springs.[101] Noting that the power of the Commission to set and regulate rates that utilities charge is broad, the Washington Supreme Court refused to read into the rate setting statutes, RCW 80.28.010 and .020, a used and useful requirement as exists in the rate base statute, RCW 80.04.250.[102] Instead the Court relied on the plain meaning of the language "rendered in connection with electricity service" and upheld the Commission's authority to allow the utility to charge for expenses related to nuclear power plants that had never been put into service because the charges were "rendered in connection with electricity service."[103] ICNU ignores the ultimate holding in the case and stretches language in the *POWER* decision, claiming the Court ruled that the Commission could not permit a utility to charge for services not rendered. To the contrary, the Washington Supreme Court upheld the Commission's determination that Puget could include in rates the expenses associated with a power plant that was never built, never served customers, and never met the used and useful standard.[104]

37. A second case cited by ICNU, *Jewell*,[105] differs from the facts of this case. In *Jewell*, parties challenged a charge to customers to recover contributions made to private charities by

[99] *See* ICNU Initial Brief at ¶ 45.
[100] *POWER*, 104 Wn.2d 798.
[101] *Id.* at 805-26.
[102] *Id.* at 815-16.
[103] *Id.* at 825.
[104] *Id.* at 825-26.
[105] *Jewell v. State Utils. & Transp. Comm'n*, 90 Wn.2d 775 (1978).

telephone companies. The Washington Supreme Court concluded that this practice was not authorized or supported by RCW 80.36.080. Telephone users were not receiving any more prompt or expeditious service because of the charitable contributions, and the statute did not direct that a telephone company be a "good corporate neighbor."[106] The Court disapproved of the fact that these contributions were being assessed against ratepayers and subscribers, calling the assessment an "involuntary contribution[ ]".[107] Unlike the charge to customers for charitable contributions, revenue per customer decoupling is tied directly to the provision of electricity and natural gas service. It is a method for recovering costs for those services that is intended to eliminate the throughput incentive companies otherwise face. Comparing a charge for charitable contributions to charges for the delivery of electricity and natural gas service compares apples to oranges.

38. Similarly, the *TRACER*[108] case cited by ICNU differs from the facts and law currently before the Commission. *TRACER* did not involve a challenge to rates set by the utility, but a challenge to a tax set by the Commission. In *TRACER*, the court struck down a Commission rule that essentially required larger local exchange carriers ("LEC"), such as US West and AT&T, to pay into a fund that would subsidize smaller LECs. The Community Calling Fund ("CCF") was intended to "cushion the local rate effect" of a new law on customers of smaller LECs and to provide revenue support for smaller LEC."[109] The court distinguished *TRACER* from *POWER* and *Jewell*, noting that *TRACER* involved a tax by the Commission requiring larger carriers to pay smaller carriers, whereas in both *Jewell* and *POWER* the challenge was to a charge that the utility sought to impose on customers. The court ruled that there is no statutory authority for enacting the CCF.[110] The charge proposed was unrelated to the service provided by the company

[106] *Id.* at 777.
[107] *Id.* at 778.
[108] *Wash. Indep. Tel. Ass'n v. Telecomms. Ratepayers Ass'n for Cost-Based & Equitable Rates (TRACER)*, 75 Wn. App. 356 (1994).
[109] *Id.* at 361.
[110] *Id.* at 365.

on which the tax was imposed and did not relate to the revenue requirement of the company against which the charge was ostensibly assessed.[111] In sum, no statutory authority was identified that permitted the Commission to set up a fund, such as the CCF, to which all LECs are required to contribute, but from which not all LECs can draw.[112] In contrast to the facts at issue in *TRACER*, the decoupling mechanisms are not a tax set by the Commission by which certain larger utilities fund smaller utilities. Rather, decoupling is a rate mechanism for recovering the costs for electricity and natural gas services.

2. Large Customers Should Remain in the Decoupling Mechanisms

39. Although it is true that the Commission approved a settlement stipulation for Avista that omitted large industrial and commercial customers from its decoupling mechanism, that settlement is not dispositive in this case. The settlement stipulation itself states that it is not appropriate for resolving any issue in any other proceeding.[113] Moreover, PSE's relationship with its large customers differs from Avista and PacifiCorp. One significant difference, admitted by ICNU in its brief, is that PSE offers Schedule 258, which allows PSE's large customers to self-direct conservation measures. Neither Avista nor PacifiCorp offers such a tariff. If these large customers are removed from decoupling and the throughput incentive is reinstated, PSE may need to return to a compliance mode in terms of conservation programs, and innovative ideas such as Schedule 258 may no longer be available to these customers.

3. ICNU's Arguments with Respect to Conservation Have Been Rejected

40. ICNU adopts an argument on brief similar to FEA—that decoupling should be tied to conservation—and complains because "decoupling makes no attempt to align rate recovery with kilowatt hour sales impacted by customer conservation."[114] In 2011, the Commission rejected PSE's Conservation Savings Adjustment proposal that was tied to conservation expressing

[111] *Id.* at 367.
[112] *Id.* at 368.
[113] *See WUTC v. Avista Corp.*, Dockets UE-140188, *et al.*, Order 05, Attachment A, ¶ 25 (Nov. 25, 2014).
[114] *See* ICNU Initial Brief at ¶¶ 40-41.

discomfort over the use of engineering estimates of conservation in the development of a revenue requirement.[115]

41. Moreover, ICNU is wrong in claiming that decoupling removes the incentive for conservation for larger commercial customers.[116] These customers will realize the benefit in lower bills and lower future costs through the avoidance or delay of new capacity, as discussed above. With decoupling, they receive these benefits. Without decoupling, they reap windfall benefits in the form of avoiding their share of existing capacity costs.

42. ICNU acknowledges that large customers have the opportunity for self-directed conservation through Schedule 258, with little PSE involvement and oversight.[117] This is an opportunity not available to other customers. However, this does not justify removing these large customers from decoupling. To the contrary, it provides all the more reason why PSE (and its other customers) should be shielded from risks that they cannot control and for which they may not otherwise be adequately compensated.

D. The General Rate Case Rule Does Not Apply To Decoupling Deferrals

43. The Energy Project argues, incorrectly, that the general rate case rule, WAC 480-07-505(1), applies to the decoupling deferrals and cites this rule in opposition to PSE's proposal to increase the decoupling rate cap to five percent for residential customers. While that rule may have had some applicability to the K-factor rate increases under the multi-year rate plan, as claimed by The Energy Project,[118] it does not apply to the decoupling deferrals. Under decoupling, PSE is allowed to recover a set amount of revenue per customer. Multiplying this amount per customer by the number of customers served in each month produces the revenues that PSE is allowed to book in each month. From an accounting perspective this revenue is booked in two places, as the cash received through existing rate revenues and as the deferred

[115] *See WUTC v. Puget Sound Energy*, Dockets UE-111048 & UG-111049, Order 08 at p. ii, ¶ 473 (May 7, 2012).
[116] ICNU Initial Brief at ¶¶ 53-59.
[117] ICNU Initial Brief at ¶¶ 61-62.
[118] The Energy Project Initial Brief at ¶ 27.

revenue to be trued up the following year. When PSE files to true up the deferred revenue in the following year, it produces no increase to PSE's revenue. The true up only provides the cash recovery of the revenues already recognized in the previous year. Therefore, since the true up filing produces no increased revenues, the rate limitations under WAC 480-07-505 do not apply.

III. ELECTRIC COST OF SERVICE RATE SPREAD AND RATE DESIGN

A. PSE's Proposal for the Electric Basic Charge Is Reasonable

44. The increase PSE proposed to its basic charge is reasonable, follows the principles of gradualism, and is consistent with PSE's cost of service study in past cases. The 2014 *PacifiCorp* case, as well as other cases cited by NWEC, Public Counsel, and The Energy Project are distinguishable.

45. Public Counsel proposes to decrease PSE's basic charge proposal by $1.50. In support of its position, Public Counsel cites to a prior Commission decision rejecting PacifiCorp's proposal to increase its residential basic charge by 81 percent, from $7.75 per month to $14.00 per month.[119] The *PacifiCorp* case differs from the current case, in which PSE proposes to increase its basic charge from $7.87 per month to $9.00 per month, which is less than a 15 percent increase in its basic charge following a four-year period with no increase to the basic charge.[120] Another difference is that PacifiCorp proposed to include all distribution system fixed costs (line transformers, poles, and wires) in its basic charge.[121] In contrast, PSE proposes to include approximately one-third of its transformer costs in the basic charge.[122] Finally, it should be noted that in the *PacifiCorp* case, the Commission did not rule out the possibility that transformers could be included in basic charges in the future. The Commission's decision is clearly stated in the context of an 81 percent increase to the basic charge:

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[119] *See WUTC v. PacifiCorp d/b/a Pac. Power & Light Co.*, Dockets UE-140762, *et al.*, Order 08 ¶ 203 (Mar. 25, 2015).
[120] Piliaris, Exh. JAP-1T at 66:7-15.
[121] *See WUTC v. PacifiCorp d/b/a Pac. Power & Light Co.*, Dockets UE-140762, *et al.*, Order 08 ¶ 203.
[122] *See* Piliaris, Exh. JAP-46CT at 45:14 – 46:5 (relying on NWEC calculations).

> *We reject the Company's and Staff's proposals to increase significantly the basic charge to residential customers*. The Commission is not prepared to move away from the long-accepted principle that basic charges should reflect only "direct customer costs" such as meter reading and billing. Including distribution costs in the basic charge *and increasing it 81 percent*, as the Company proposes in this case, does not promote, and may be antithetical to, the realization of conservation goals.[123]

The modest increase PSE proposes in this case includes only a portion of the cost of transformers[124] and allows PSE's basic charge to almost keeps pace with the volumetric rate changes that have occurred during the multi-year rate plan.[125]

46. The Energy Project similarly uses an inapposite comparison to argue against PSE's proposed increase to its basic charge. The Energy Project cites to a Maryland decision in which the utility proposed to increase its basic charge by 62 percent,[126] a significantly higher increase than PSE is requesting. As stated above, PSE's proposed basic charge increase is reasonable and follows the principles of gradualism endorsed by the Commission. It should be approved.

47. The Energy Project purports to rely on a RAP publication where it states that "[i]n most states, the customer charge is set to recover customer-specific costs such as metering, meter reading and payment processing."[127] But one must weigh this statement against the evidence of actual basic charges for utilities across the country that demonstrates PSE's basic charges lag behind utilities in other states as well as utilities in Washington.[128] If these other utilities are truly only recovering metering, meter reading, and payment processing costs, as The Energy Project postulates, one must question why PSE's basic charges are so much lower than these other utilities.

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[123] *WUTC v. PacifiCorp d/b/a Pac. Power & Light Co.*, Dockets UE-140762, *et al.*, Order 08 ¶ 216 (emphasis added).
[124] *See* Piliaris, Exh. JAP-46CT at 45:18 – 46:5.
[125] *See* Piliaris, Exh. JAP-1T at 66:7-15.
[126] The Energy Project Initial Brief at n. 10.
[127] *Id.* ¶ 12.
[128] *See* Piliaris, Exh. JAP-17.

48. The Energy Project repeatedly warns of the danger of "high" basic or customer charge,[129] and NWEC expresses concerns, largely unsupported, that PSE's basic charge proposal will harm low-income customers.[130] But PSE is not proposing a "high" customer charge as can be seen in Exhibit JAP-17. Even with PSE's proposed increase to the basic charge, PSE is well below the average basic charge in Washington and below the average basic charge for investor owned utilities across the country.

49. PSE and Commission Staff have provided significant testimony demonstrating that it is appropriate to include transformer charges in the basic charge, contrary to NWEC's statement in its Initial Brief.[131] Line transformer sizes are standardized, they are installed and sized specifically to serve a particular customer or group of customers, and they are rarely re-sized for a particular customer or a group of customers.[132] PSE developed its line transformer costs by using its GIS and CIS to associate each line transformer with the customers using the transformer. This results in allocating approximately 330,550 transformers to PSE's different customer classes by type and size. The majority of line transformers are used by a single class and thus are directly assigned. The remaining transformers are allocated to each class based upon the class's relative contribution to the transformer's load.[133] PSE included line transformers as customer-related costs in its last four general rate cases.[134] Based on the evidence in this case and the modest increase in the basic charge proposed by PSE, it is appropriate for the Commission to approve PSE's basic charge.

50. NWEC's reference to the 1989 case in which the Commission rejected a "minimum system approach" for cost of service studies[135] is irrelevant as PSE did not propose or perform a

[129] *See* The Energy Project Initial Brief at ¶¶ 5, 6, 7 ("High customer charges impose unfair costs . . . .").
[130] *Id.* ¶ 33
[131] *See* Ball, Exh. JLB-1T at 26:10 – 28:10; Piliaris, Exh. JAP-1T at 33:1-16.
[132] *See* Piliaris, Exh. JAP-1T at 33:3-9.
[133] *See id.* at 33:10-16.
[134] *See id.* at 33:1-2.
[135] *See* NWEC Initial Brief at ¶¶ 26, 31 (quoting *WUTC v. Puget Sound Power & Light Co.*, Dockets U-89-2688-T & U-89-2955-T, Third Supp. Order at 71 (Jan. 17, 1990)). Minimum system analyses attempt to estimate the cost of a "minimally-sized" system and ascribe those costs to serving customers. Capacity built in excess of that amount is ascribed to meeting demands.

minimum system analysis. Further, NWEC creates confusion by quoting the 2014 *PacifiCorp* case involving an 81 percent proposed increase to the basic charge in a manner that implies this was a PSE case.[136] It was not. As compared to the cited PacifiCorp case, PSE's percentage increase is much lower—15 percent as compared to 81 percent for PacifiCorp, and the basic charge amount PSE proposes is also much less—$9.00 per month as compared to PacifiCorp's proposal for a $14.00 basic charge.

B. Commission Staff's Minimum Bill Charge and Seasonal Rate Should Be Rejected

51. Commission Staff's proposal to add a minimum bill charge and seasonal rate reflects a lack of understanding of PSE's billing systems and customer relations efforts. Commission Staff would impose a major change to PSE's billing system that would result in a little more than $300,000 in minimum bill revenue above what PSE would have recovered from the same customers without a minimum bill, through volumetric rates.[137] PSE, which has extensive experience addressing customers' concerns and complaints, testified that the confusion likely to result from Commission Staff's minimum bill charge outweighs the additional $300,000 in revenue that will result from this major shift in PSE's billing approach.[138] Commission Staff dismisses this concern, stating that PSE must embrace and not shy away from interacting with customers.[139] This comment shows a lack of understanding of PSE's work directly with customers on a daily basis, through its approximately 200 call center employees,[140] its customer preference surveys[141] and many other customer interactions. As such, PSE has unique expertise on the issues that are likely to create stumbling blocks with its customers, increase customer complaints, and sow discord and misunderstanding. The minimum bill and seasonal rate as

[136] *See* NWEC Initial Brief at ¶ 26 ("More recently, the Commission again 'reject[ed] the Company's and Staff's proposals to increase significantly the basic charge to residential customers.'").
[137] *See* Piliaris, Exh. JAP-46CT at 43:17 – 44:7.
[138] *See id.* at 43:22 – 44:7.
[139] Commission Staff Initial Brief at ¶ 40.
[140] *See* Zeller, Exh. GJZ-3T at 13:4-5.
[141] *See* Zeller, Exh. GJZ-1T at 20:16 – 21:5.

designed by Commission Staff are likely to create obstacles to maintaining smooth customer relationships. Accordingly, they should be rejected by the Commission.

C. A Collaborative on Third-Block Rates Is Not Necessary

52. NWEC's request for a collaborative to discuss a third-block rate is unnecessary and duplicative of the rate design collaborative from 2014 in which a third-block rate for residential customers was discussed. NWEC did not participate in that proceeding, but now seeks to have the Commission duplicate the recent proceeding. In the 2014 collaborative and settlement, the parties agreed that PSE would propose pricing for such a rate structure, and PSE did so in this case. Ultimately, all parties who participated in the collaborative either agreed in this case not to pursue the third-block rate structure or did not oppose this decision.[142] It is not necessary to order another collaborative on this same topic, as NWEC proposes. There has been no evidence in this case on the need for a third block nor has there been testimony on whether the block levels were appropriately set.

53. The Energy Project discussed the hardship that a third-block rate potentially creates for low-income customers in its Initial Brief.[143] NWEC, which opposes an increase to the basic charge due to concerns about the impacts to low-income customers, apparently has no qualms about the impacts of a third-block rate on low-income customers. The Commission has previously recognized that a third-block rate may adversely affect low-income customers.[144] There is not a pressing need to study or implement a third-block rate at this time.

IV. NATURAL GAS COST OF SERVICE, RATE SPREAD AND RATE DESIGN

54. Commission Staff's interpretation and proposed treatment of the Special Contract[145] would eviscerate the purpose of the special contract rule by essentially charging the Special Contract customer the same rate that would otherwise be paid under tariffed services, despite the

[142] *See* Piliaris, Exh. JAP-46CT at 57:1-10.
[143] The Energy Project Initial Brief at ¶¶ 20-21.
[144] *WUTC v. PacifiCorp d/b/a Pac. Power & Light Co.*, Dockets UE-140762, *et al*., Order 08 ¶¶ 218-19.
[145] *See* Piliaris, Exh. JAP-66HCX.

threat of a bypass that justifies the use of a special contract. WAC 480-80-143 provides that a special contract can be entered into between a gas company and a customer, and approved by the Commission, "if the basis for using the special contract is the availability of an alternate service provider,"[146] or in other words, if there is a threat of bypass by the special contract customer. The special contract may "state charges or conditions that do not conform to the company's existing tariff."[147] The special contract must be for a stated time period[148] and the duration of the contract is an essential term of the special contract.[149] The special contract must "[d]emonstrate, at a minimum, that the contract charges recover all costs resulting from providing the service during its term, and, in addition, provide a contribution to the gas, electric, or water company's fixed costs."[150]

55. The Special Contract at issue in this case was approved for renewal in 2009. Although Commission Staff did not question the Special Contract at that time, or in the 2009 general rate case, or in the 2011 general rate case, Commission Staff now interprets the language of the Special Contract in a manner that ignores the purpose of the special contract rule and asks the Commission to take unprecedented steps that would revise the terms of the Special Contract in the middle of its term or, alternatively, would penalize PSE for complying with the terms of the Special Contract. The Commission should decline Commission Staff's invitation to revise this previously-approved Special Contract.

56. The "price floor" that Commission Staff cites to in the Special Contract[151] must be read in the context of WAC 480-80-143(5)(c) that allows the Special Contract customer to contribute "all costs resulting from providing the service during its term, and, in addition, provide a contribution to the gas . . . company's fixed costs." Thus, the Special Contract customer must

[146] WAC 480-80-143(5)(e).
[147] WAC 480-80-143(1)(a).
[148] WAC 480-80-143(6).
[149] WAC 480-80-143(7)(c).
[150] WAC 480-80-143(5)(c).
[151] *See* Commission Staff Initial Brief at ¶ 17 (citing Piliaris, Exh. JAP-66HCX at 14-15).

pay *incremental* fixed costs associated with the service, including the return of and a portion of the return on the *incremental* investment required to serve the contract load. PSE testified that the amount received from the Special Contract customer is well in excess of the return of and on the incremental costs to serve the contract load,[152] consistent with the intent of WAC 480-80-143(5)(c). Staff's interpretation of the "floor provision" of the Special Contract focuses on the fully embedded cost of service allocated to the Special Contract customer, rather than the *incremental* fixed costs. Staff's interpretation would completely gut the purpose of the Special Contract by requiring the Special Contract customer to pay a return of and a return on the fully allocated cost of service, which would render the Special Contract meaningless. The Special Contract was negotiated between PSE and the Special Contract customer to avoid a bypass threat and with the understanding that PSE's remaining customers are better off with the Special Contract customer on the system than if the Special Contract customer bypassed the system.[153] To interpret the language of the Special Contract in the manner proposed by Commission Staff, would render valueless the consideration received by the Special Contract customer for staying on PSE's system.

57. Further, there are a wide range of results from the various cost of service studies performed by parties to this case. As Mr. Piliaris testified, the results from these cost of service studies are too unstable to make recommendations with the level of precision of Commission Staff's proposal.[154] NWIGU has addressed the Special Contract issue in depth in its initial brief. PSE agrees with NWIGU's analysis. The Commission should not penalize PSE for implementing the terms of the Special Contract as approved by the Commission.

[152] *See* Piliaris, Tr. 280:16 – 282:3, 286:10-25.
[153] *See* Piliaris, Exh. JAP-54T at 11:8 – 12:2.
[154] *See id.* at 8:11-17.

V. PUBLIC COUNSEL'S OBJECTIONS TO THE SETTLEMENT AGREEMENT ARE UNWARRANTED AND SHOULD BE REJECTED

A. The Return on Equity Should Not Be Lowered Based on Decoupling

58. Public Counsel seeks to resurrect an argument that was put to rest by the Commission in 2015. Public Counsel argues that the Commission should adjust PSE's ROE downward to reflect the reduced "risk of volatility of revenue based on customer usage"[155] associated with PSE's decoupling mechanisms.[156] The Commission considered the issue, based on a full record, in the PSE decoupling remand case. Ultimately, the Commission determined that the ROE should not be adjusted downward for decoupling.

> The Commission has never tried to account separately in its ROE determinations for specific risks or risk mitigating factors, nor should it. Circumstances in the industry today and modern regulatory practice that have led to a proliferation of risk reducing mechanisms being in place for utilities throughout the United States make it particularly inappropriate and unnecessary to consider such an undertaking. The effects of these risk mitigating factors was by 2013, and is today, built into the data experts draw from the samples of companies they select as proxies.[157]

PSE's Initial Brief provided further discussion of the appropriateness of the 9.50 ROE.

B. The Depreciation Set Forth in the Settlement Is Reasonable

59. Public Counsel argues that the depreciation for Colstrip Units 1 and 2, agreed to by the ten Settling Parties, should be undone by the Commission and replaced with Public Counsel's unconventional approach to depreciation. As Sierra Club notes, a change to this fundamental aspect of the Settlement Agreement would risk jeopardizing the entire Settlement Agreement.[158] Public Counsel's approach, which involves transferring a portion of the book reserve from the Colstrip Units 1 and 2 to other steam production plants, including PSE's combined cycle

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[155] Public Counsel Initial Brief at ¶ 43 (citing Decoupling Policy Statement).
[156] Although FEA joined in the Settlement Agreement, FEA also makes this argument with respect to the decoupling mechanisms. *See* FEA Initial Brief at 7-8. For the reasons discussed herein, the Commission should reject FEA's request.
[157] *In the Matter of the Petition of Puget Sound Energy and Northwest 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 & UE-130137, Order 15 at ¶ 155 (June 29, 2015).
[158] Sierra Club Initial Brief at 11.

facilities, would push recovery of depreciation expense for Colstrip Units 1 and 2 out another 25 years after the units close, either creating significant intergenerational inequities or other underrecoveries of PSE's combined cycle plants.[159] Although Public Counsel attempts to position its depreciation proposal as a more reasonable option, the manner in which Public Counsel's witness calculates the reserve balances—and specifically, the terminal salvage value for power plants that is a component of the reserve balance—does not conform to standard utility practice as discussed in detail in Mr. Spanos's rebuttal testimony.[160] Specifically:

> Public Counsel argues that terminal net salvage costs should be expressed in today's price levels, as opposed to escalated to reflect the best estimate of the actual cost that will be incurred by PSE upon retirement. However, Public Counsel's proposal is a deferral of costs to future customers, and it will not result in the full recovery of the costs associated with PSE's power plants through straight line depreciation rates. Her proposal therefore increases the risk of similar situations occurring in the future to the current situation for Colstrip Units 1 and 2, in which there are a higher level of unrecovered costs that need to be recovered over a relatively short period of time.[161]

Public Counsel's ill-advised calculation of reserve balances does not follow industry practice, burdens future customers, and is likely to unwind the entire Settlement Agreement if adopted.

60. Moreover, Public Counsel's justification of the need for its proposed methodology is nonsensical. Public Counsel argues that its methodology for calculating depreciation for the Colstrip Units 1 and 2 would avoid rate shock.[162] But there is no rate shock associated with the 0.9 percent increase in electric rates in the Settlement Agreement. It is not necessary to use Public Counsel's questionable approach to depreciation to avoid rate shock.

C. The Use of PTCs for Colstrip Funding Is Appropriate

61. It is not clear what Public Counsel intends by proposing that "[i]f the balance of PTCs is not sufficient, then shareholders should reimburse the Company with the amount of PTCs used

[159] *See* Spanos, Exh. JJS-4T at 12:18-23.
[160] *See id.* at 31:12-22.
[161] *See id.* at 32:1 – 38:20.
[162] *See* Public Counsel Initial Brief at ¶ 57.

for community planning."[163] How or why shareholders of PSE would reimburse PSE is puzzling. Moreover, the $5 million of PTC funding for Colstrip community transition is not likely to have a significant impact on the later availability of PTCs for plant recovery and decommissioning and remediation, considering there is approximately $280 million in PTCs available for these uses, in addition to the nearly $100 million of Treasury Grants that is being set aside for decommissioning and remediation of Colstrip Units 1 and 2.[164] The Commission should reject Public Counsel's ill-defined proposal.

62. Further, PSE disagrees with Public Counsel's proposal that PSE assume the risk that PTCs will not be monetized and available to offset unrecovered plant for Colstrip Units 3 and 4. Because it is unknown when Units 3 and 4 may close, and because PSE may not unilaterally make a decision to close those units, PSE cannot accept that risk. This differs from the risk PSE has accepted in the Settlement Agreement with respect to Colstrip Units 1 and 2. PSE is able to assume the risk that sufficient PTCs would not be available to recover the unrecovered balance for Colstrip Units 1 and 2 because the closure of these units will occur no later than 2022 and PSE will have until December 31, 2029 to monetize sufficient PTCs to address the unrecovered balance.[165] PSE cannot similarly accept the risk that monetized PTCs will not be available for the unrecovered plant balance for Colstrip Units 3 and 4 by a set date, when the closure date for Colstrip Units 3 and 4 is not yet known.

D. The Water Heater Rental Program Is Addressed Reasonably in the Settlement

63. Public Counsel's concerns with the Settlement Agreement terms regarding the water heater rental program are unwarranted. Notably, it was Commission Staff who raised this concern in testimony, and as part of the Settlement Agreement, PSE and Commission Staff have agreed to enter into a collaborative to discuss the future of Schedules 71, 72, and 74. Public

[163] *Id.* ¶ 63.
[164] Piliaris, Exh. JAP-1T at 5:11 – 6:3.
[165] Settlement Agreement at ¶ 25.

Counsel provided no testimony or independent analysis on this issue. There are numerous reasons why PSE and Commission Staff agreed that a collaboration regarding the future of the program is warranted and why an abrupt closure of the program as now advocated by Public Counsel would be detrimental to PSE and its customers.

64. First, it is well known that PSE and its predecessor companies have offered various equipment rental services for more than half a century.[166] Despite numerous legal challenges over the years, the Commission and the Washington Supreme Court have repeatedly reaffirmed the authority of utilities to implement rental or leasing programs.[167] Indeed, the authority of utilities to implement equipment leasing programs was confirmed by the Commission just last year where PSE's existing rental program was expressly acknowledged and cited by the Commission as conclusive evidence of strong customer interest in such a program.[168]

65. Second, Public Counsel's apparent concerns with the program do not reflect the voice of its constituents as there are still approximately 30,000 customers that still participate in the program.[169] Customers choose to participate in the program because of the value it provides to them and they can end their participation any time.[170] An abrupt termination as proposed by Public Counsel would be harmful as many customers depend on and utilize PSE's rental program because of the important service it provides for them. As explained by Mr. Einstein:

> Customers participate in the program not merely because of the equipment itself. Rather, the rental program is a comprehensive service program whereby PSE provides the rental equipment, plus parts, repair, and replacement. If a customer experiences failing equipment, PSE will repair or replace the equipment at no additional cost to the customer. This provides a tremendous peace of mind for many customers. Some PSE customers have participated in the program for decades because they value the service provided and predictability of cost. Replacing a failed water heater can be expensive and inconvenient for customers. Ms. O'Connell's testimony totally fails to address this aspect of the rental program and the

[166] *See* Einstein, Exh. WTE-1T at 2:13 – 3:3.
[167] *Id*. at 3:9-17; *Cole v. WUTC*, 79 Wn.2d 302 (1971).
[168] *WUTC v. Puget Sound Energy*, Dockets UE-151871 & UG-151872, Order 06 ¶¶ 48-73, 84 (Nov. 16, 2016).
[169] Einstein, Exh. WTE-1T at 2:6-10, 3:4-8, 7:20 – 8:2.
[170] *Id.* at 5:10 – 6:5.

> value many customers find in the program. Automatically transferring ownership of the equipment ignores the fact that many customers do not want to own the equipment because they participate in the program for the service PSE provides.[171]

66. Staff's proposal, now apparently adopted by Public Counsel, to automatically transfer "fully accrued" equipment would arbitrarily end the service for these customers when they have chosen to participate in the program because of the services provided.[172] As explained further by Mr. Einstein, "The customer would then be required to bear the full burden of repair or replacement costs should the equipment fail, disallowing customers from availing themselves of the value of the service they invested in prior to such a forced transfer."[173] In particular, this could adversely affect low income or small business owners who do not have the resources to cover these costs.[174] Public Counsel's disregard of the impacts that immediate termination will have on some customers is surprising.

67. Third, the concerns regarding rate design and overearning are not a conclusive determination that immediate termination of the program is appropriate. Utility programs can underearn or overearn at varying degrees over time, and the purpose of a rate case is to periodically adjust these concerns.[175] Moreover, Public Counsel's suggestion that no adjustment could correct the policy reasons for maintaining the program is simply incorrect. PSE's program does promote the use of more efficient equipment as PSE has worked with its distribution and installation partners to ensure that rental equipment being replaced meets or exceeds current energy efficiency standards.[176]

68. Finally, the proposals for terminating the program, which Public Counsel has apparently adopted, would cause significant harm to customers and to PSE. For example, the suggestion to immediately replace a failing water heater and then gift the equipment to the customer before

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[171] *Id.*
[172] *Id.* at 6:8-16.
[173] *Id.* at 6:10-13.
[174] *Id.* at 6:13-16.
[175] *Id.* at 6:17 – 7:5.
[176] *Id.* at 9:3-12.

terminating service would deprive PSE of the ability to recover its costs. This could amount to a regulatory taking and might also provide an undue preference to these customers, not to mention harm the ratepayers who would bear the costs for this proposal.[177] Likewise, the proposal for how to account for loss of rental income was initially unworkable and would have significant detrimental revenue implications.[178]

69. Public Counsel's late decision to adopt Commission Staff's testimony does not address any of these problems. The more reasoned approach, as agreed to by PSE and Commission Staff, is a collaborative to fully evaluate the merits of the program, the ratemaking concerns expressed by the parties, and if closure of the program is deemed appropriate, the proper course for doing so that mitigates the harm to PSE and to customers. Public Counsel's proposal to simply cancel the program would do none of those things and should be rejected.

E. Service Quality Index and Related Issues

70. Public Counsel's concerns regarding SQI-5 are not credible and should be rejected for several reasons. First, as explained in PSE's Initial Brief, the standard agreed to by the parties is the same metric as recently approved by the Commission for Avista, to which Public Counsel agreed.[179] Thus, Public Counsel's statement that "the Settlement proposal would lead directly to 'a deterioration in quality of service'" expressly contradicts its position in the Avista matter.[180] Public Counsel has not articulated any reason why PSE's standard should be different from Avista's nor has it explained why it is now suddenly changing positions. The standard agreed to in the Settlement Agreement reflects a compromise.[181] The Settling Parties reasonably determined that the recently-approved Avista standard was the best compromise and had already been approved by the Commission.[182]

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[177] *Id.* at 9:13-20.
[178] *See* Piliaris, Exh. JAP-46CT at 81:16 – 83:12.
[179] *See* PSE Initial Brief at ¶ 18.
[180] Public Counsel Initial Brief at ¶ 72.
[181] Settlement Panel, Tr. 587:1 – 592:8.
[182] *Id.*

71. Second, as Public Counsel concedes, the SQI program is two decades old.[183] Change was needed because new technologies such as Integrated Voice Response ("IVR") now handle a significant portion of incoming calls, which has an effect on the types of calls received by the call-center.[184]

72. Finally, even in comparison to Avista, PSE faces a $1.5 million penalty for failing to comply with the SQI-5 standard.[185] No other utility in Washington is held to this standard. Public Counsel is looking for problems where none exist. Every other party is satisfied with the standard agreed to in the Settlement Agreement (including Public Counsel in a prior case) and the SQI-5 standard agreed to in the Settlement Agreement should be approved.

73. Likewise, Public Counsel's concerns with the Get-to-Zero initiatives ("GTZ") are equally unavailing. PSE has been moving, and will continue to move, forward with these initiatives as discussed in the testimony of David E. Mills,[186] but there are no pro forma adjustments or other requests for Commission action with respect to GTZ. As part of the Settlement Agreement, PSE has agreed to consult with "The Energy Project and Agencies jointly regarding any initiatives or modifications affecting operation or administration by the agencies of bill assistance or weatherization programs."[187] Public Counsel's request would have the Commission micromanage PSE's internal operations at a level of detail—the timing of a notification on the IVR system—that is not advisable. There is no need for Commission action with respect to GTZ.

F. The Procedure for the Expedited Rate Filing Is Reasonable

74. Public Counsel's primary concern with the Expedited Rate Filing ("ERF") agreed to by the parties in the Settlement Agreement is it complains that the 120-day process for processing an ERF is inadequate time for such a proceeding.[188] Given that the nine other parties to the

[183] Public Counsel Initial Brief at ¶ 71.
[184] Schooley, Tr. 606:9 – 608:11.
[185] *See* PSE Initial Brief at ¶ 18.
[186] Mills, Exh. DEM-4T at 5:13 – 8:16.
[187] Settlement Agreement at ¶ 106.
[188] Public Counsel Initial Brief at ¶ 66.

Settlement Agreement disagree with Public Counsel, its objection should not be entertained. Moreover, Public Counsel's concern "with the number of ERFs that may be anticipated between rate cases"[189] and its hypothetical scenarios regarding the filing of subsequent ERFs[190] is speculative. The parties have agreed to a reasonable time period and parameters surrounding the filing of an ERF, and PSE requests that the Commission approve this provision and the entirety of the Settlement Agreement.

DATED this 27th day of October, 2017.

Respectfully submitted

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[189] *Id.* ¶ 67.
[190] *Id.*