BEFORE THE WASHINGTON
UTILITIES AND TRANSPORTATION COMMISSION

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

REPLY BRIEF
OF PUBLIC COUNSEL

October 27, 2017

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I. INTRODUCTION

1. The Public Counsel Unit of the Attorney General's Office respectfully files this Reply Brief, pursuant to the procedural schedule in the above-captioned matter. Public Counsel responds to several Puget Sound Energy (the Company or PSE) and Commission Staff arguments concerning Public Counsel's position regarding the Multiparty Settlement (Settlement) and the contested issues. Public Counsel reaffirms the arguments presented in our initial post-hearing brief, filed in this matter on October 18, 2017, and does not repeat them here for brevity. Silence regarding a party's argument does not indicate acceptance or agreement. Public Counsel continues to recommend that the Commission modify the Settlement and grant rates for PSE that are consistent with Public Counsel's recommendations discussed in Public Counsel's initial post-hearing brief, testimony, and exhibits.

II. ARGUMENT

A. Public Counsel's Recommendation Regarding Colstrip Depreciation Is Reasonable

2. It is a longstanding practice to adjust depreciation based on new information.[1] Similar to the Michigan Commission in the 1943 *Edison* case, the Commission in this case has the authority to adjust depreciation schedules based on new information and changing circumstances. In hindsight, the current depreciation schedule was too long. The current depreciation schedule was the result of a settlement in PSE's 2007 general rate case, and the parties to that case made the

[1] *Detroit Edison Co. v. C.I.R.*, 319 U.S. 98, 103 (1943) (holding, "The Commissioner was warranted in adjusting the depreciation base to represent the taxpayer's net investment").

best decisions given the information and knowledge at the time. In adopting the settlement in that case, the Commission said described the agreement as follows:

> Another significant feature of the overall settlement is the parties' agreement to accept the results of an updated depreciation study commissioned by PSE, with one adjustment, for purposes of resolving this case. The electric depreciation rates have been adjusted from the Company's rebuttal filing to reflect Staff's and Public Counsel's proposed Colstrip depreciable life of 60 years.[2]

3. New depreciation studies sometimes reveal new information that alters the depreciation schedules of a utility's assets. That is the case with PSE's Colstrip generation plant. PSE's proposal to increase the depreciation expense collected from current ratepayers due to the reserve deficiency related to the earlier-than-expected retirement of Colstrip Units 1 and 2 is not fair to the ratepayers because the overall balance for PSE's Steam Production Plant account is a surplus. Using the overall surplus from the Steam Production Plant account to offset the reserve deficiency caused by the retirement of Units 1 and 2 assists with the inter-generational issues resulting from the deficiency.

4. With respect to Colstrip Units 3 and 4, accelerating the depreciation expense using a retirement year that is on the lower end of the range, when there is no certainty of the actual retirement date for those units, is also unfair to the ratepayers. Accelerating the depreciation expense places more of the burden of the unknown future retirement date on the current ratepayer. PSE is only one owner of Colstrip Units 3 and 4 and is not able to make decisions unilaterally about its future.

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[2] *WUTC v. Puget Sound Energy*, Dockets UE-072300 and UG-072301, Order 12, Final Order Approving and Adopting Settlement Stipulations ¶ 57 (Oct. 8, 2008).

5. Public Counsel agrees that the Commission should shorten the depreciation schedules for Colstrip Units 1 through 4. However, the schedules should align with the useful lives of the assets. The useful lives is determined by depreciation studies, not speculation regarding what might or might not occur in the future.[3] In this case, Public Counsel bases its recommendation on its review of PSE's depreciation study and uses reasonable techniques to mitigate the impact on ratepayers.

B. Expedited Rate Filing

6. PSE claims Public Counsel is reversing course from our 2013 position where we, "opposed PSE's multi-year rate plan and proposed multiple ERFs as an alternative."[4] PSE fails to recognize the different facts, evidence, and circumstances existing currently that were not present in 2013. Public Counsel's position is responding to a different situation than existed in 2013, when PSE was proposing a multi-year rate plan. In this case, PSE is not proposing a multi-year rate plan. Nor has PSE provided a showing of future financial need that would justify an expedited rate filing. PSE states that, "there is nothing the Commission rules that would prohibit an ERF" as if that alone demonstrates future financial need for an ERF.[5] It does not, and Public Counsel opposes PSE's ERF proposal in this case based on PSE's current facts, evidence, and circumstances.

7. PSE dismisses Public Counsel's position on the ERF by stating Public Counsel "confuses attrition and the ERF."[6] Public Counsel is not confused. One way to show financial need would

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[3] *Puget Sound Power & Light Co. v. Strong*, 59 Wash. App. 430, 439 (1991) (holding, "useful life of the [asset] must be based on the depreciation schedule").

[4] PSE Initial Brief ¶ 21.

[5] *Id.*

[6] *Id.* ¶ 24.

be to show earnings attrition. PSE admitted they did not study or quantify any earnings attrition (see Exhibit MLB-5) and has made no showing of financial need for higher future revenues beyond what the pending rate cases will award. In absence of any financial need for higher revenues through an ERF, the Company should not be granted an ERF through which to file for higher revenues. PSE must demonstrate some future financial need for higher revenues before expedited rate relief is assumed to be needed, particularly when the expedited nature of an ERF will ultimately dampen the ability of other parties to conduct a full review of the Company's proposal.

C. Public Counsel's Proposal on Decoupling Should Be Adopted

8. PSE has acknowledged through the Multi-Party Settlement that it should not be granted revenue per customer decoupling and the resulting growing revenue stream for its fixed production costs. The same approach, providing constant rather than growing distribution revenues through decoupling in the form advocated by Public Counsel, is appropriate for the Company's delivery costs. PSE has not demonstrated that its future delivery service costs will grow proportionately with customer growth or that the Company has any financial need for higher future delivery service revenues arising from customer growth. PSE claims that its "delivery cost growth has exceeded customer growth by 1.2 percent per year."[7] This is a backward looking review of expense trends, and past trends do not prove that future costs will continue in the same manner.

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[7] PSE Initial Brief ¶ 74.

9. The Company's claim in its brief that, "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,"[8] is based on a misinterpretation of Public Counsel's recommendation. Even so, PSE has not demonstrated that it faces any future earnings attrition risk that would justify collecting revenue growth through decoupling. Indeed, PSE's reported earnings have actually exceeded authorized return levels in 2015 and 2016. This is due, in part, because decoupling revenue growth from customer additions was excessive in relation to PSE expense levels, demonstrating that revenue per customer decoupling is harmful to ratepayers.[9]

D. Public Counsel's Modification to Storm Damage Amortization Is Reasonable

10. The Commission used a 10-year period in a previous PSE case for catastrophic storm expense.[10] For this reason, Public Counsel's expert witness, Roxie M. McCullar, used a depreciation methodology that adopts a 10-year amortization period. Public Counsel recommends the Commission adopt Ms. McCullar's reasonable 10-year proposal.

E. Public Counsel's Recommendation with Respect to Pension Expense Should Be Adopted

11. PSE will over-recover its pension costs if the Commission uses PSE's backward-looking, four-year average.[11] The amount PSE requested is higher than the amount for the current year or the next projected years, which includes the rate effective period. The over-recovery of current

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[8] *Id.*

[9] Response Testimony of Michael L. Brosch, Exh. MLB-1T at 18.

[10] See Order 12, dated October 8, 2008 from Dockets UE-072300 and UG-072301, in which the Commission adopted a settlement between PSE and the intervenors in that proceeding.

[11] Response Testimony of Ralph C. Smith, Exh. RCS-1CT at 57–59.

year and projected pension expense exists under both a FAS 87 (accrual approach) and under a cash funding basis approach. The Commission should not use PSE's backward-looking, four-year period because the evidence is compelling that this would over-recover pension cost in each and every year of the rate effective period.[12] Instead, the Commission should use Public Counsel's recommendation of a pension expense allowance of $18.4 million per year. This is based on a four-year average of net periodic pension cost for years 2013 through 2016, and includes the Company's projections.

F. Environmental Remediation

12. PSE's environmental remediation efforts are required by law.[13] However, the law does not mandate the amounts PSE is required to spend on environmental remediation even though it has an obligation to demonstrate how it intends to allocate insurance funds.[14] To that end, the Settling Parties have determined they, "will commence a process to determine a methodology for assigning insurance recoveries." In short, the Settlement does not require PSE to do anything the law does not already require them to do, i.e. conduct environmental remediation and assign insurance recoveries.

13. As of September 30, 2016, the Company received proceeds from insurance carriers and third parties totaling $5.344 million for environmental remediation sites related to electric operations and

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[12] *Id.*

[13] *See, Comprehensive Environmental Response, Compensation, and Liability Act (CERCLA) and Federal Facilities,* U.S. Environmental Protection Agency, https://www.epa.gov/enforcement/comprehensive-environmental-response-compensation-and-liability-act-cercla-and-federal (last updated on Feb. 16, 2017). *See also*, RCW 70.105D, Hazardous Waste Cleanup-Model Toxics Control Act.

[14] *See Puget Sound Energy v. Alba Gen. Ins. Co.*, 109 Wash. App. 683, 695, 10 P.3d 445, 452 (2000) *review granted in part, cause remanded*, 143 Wash. 2d 1008, 21 P.3d 281 (2001) *and amended*, 36 P.3d 1072 (Wash. Ct. App. 2001) *and aff'd and remanded*, 149 Wash. 2d 135, 68 P.3d 1061 (2003) (holding "PSE must demonstrate how it intends to or has allocated the funds it has received from the settling insurers").

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$50.268 million for environmental remediation sites related to gas operations, for total recoveries of $55.612 million. Under the Settlement, the parties do not disclose how much PSE will allocate or when. Public Counsel recommends the Commission use 100 percent of the proceeds recovered from insurance carriers and third parties that is known and measureable to offset environmental remediation as of September 30, 2016.[15] Public Counsel's position on this issue is reasonable and consistent with positions taken by Commission Staff, ICNU, and NWIGU prior to the Settlement.[16]

G. Public Counsel's Approach to Depreciation (Other than Colstrip) Is Reasonable

14. The amount of future inflation to be reflected in the cost of removal/negative net salvage estimates is a legitimate subject of debate. However, rebalancing depreciation reserve excesses and deficiencies merely using a different amount is not "an unconventional depreciation methodology."[17] PSE's argument should not convince the Commission that only PSE's depreciation methodology is "conventional."[18]

15. Public Counsel's proposal to reallocate the depreciation reserve is fair to current and future customers. As discussed in Ms. McCullar's testimony the reserve surplus has been collected from ratepayers over the last decade.[19] The reserve surplus indicates that PSE

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[15] PSE will receive unknown, additional insurance recoveries in the future.

[16] Response Testimony of Bradley G. Mullins, BGM-1CTr at 47; and Testimony of Elizabeth C. O'Connell, Exh. ECO-1CT at 16.

[17] See *US West Commc'ns v. WUTC*, 134 Wash.2d 48 (1997), (where the Washington Supreme Court held, "[the statute] governing Washington Utilities and Transportation Commission (WUTC) power over public service company depreciation and retirement accounts allows broad discretion to Commission to set depreciation rates and methods").

[18] PSE Initial Brief ¶ 14.

[19] Testimony in Response to Proposed Settlement of Roxie M. McCullar, Exh. RMM-12T at 3-6.

over-collected depreciation rates from ratepayers. PSE's proposal delays the return of this surplus at the expense of current customers.

16. Public Counsel's proposal to offset the depreciation reserve deficiency due to the earlier than expected retirement of Colstrip Units 1 and 2 with the depreciation reserve surplus is fair to both the company, who will have the opportunity to recover its investment and estimated future costs, and the ratepayers, who contributed to the depreciation reserve surplus. PSE would have the Commission believe that Ms. McCullar's testimony "is erroneous," "is defective," "is unconventional," "is inconsistent," "is unfocused," "argues unconvincingly," "ignores key facts," "fails to understand compromise," "creates generational inequities," and "creates under-recoveries."[20] PSE repeats this theme throughout its brief.[21] These claims are categorically false.

17. Ms. McCullar uses the exact same theoretical reserves as Mr. Spanos in his depreciation study.[22] Additionally, Ms. McCullar's depreciation methodologies are nothing but conventional and accepted by the National Association of Regulatory Utility Commissioners (NARUC).[23] Wolf & Fitch, the text relied upon by PSE witnesses, recognizes that depreciation experts may use different procedures for estimating salvage values.[24] While Ms. McCullar uses a procedure

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[20] PSE Initial Brief ¶¶ 14 – 16.
[21] PSE Initial Brief generally.
[22] McCullar, RMM-12T at 4:15-17 and 5:3-7.
[23] Exh. RMM-13X at 4-5 (NARUC Manual at 157 – 158), which states:

When estimating future net salvage, every effort should be made to ensure that the estimate is as accurate as possible. Normally, the process should start by analyzing past salvage and cost of removal data and by using the results of this analysis to project future gross salvage and cost of removal.

[24] Exh. KJB-56X at 19 (Wolf & Fitch, Depreciation Systems at 267), which states:

different than PSE for estimating the salvage for mass property accounts, that does not make her procedures "unconventional." Public Counsel implores the Commission to discount rhetoric meant simply to undermining its witnesses' intellect, reasonableness, and discretion when evaluating their testimony and the significant thoughtfulness they exercised in their recommendations, but rather focus on the merits of the recommendations brought forth by each witness.[25] With respect to PSE's depreciation, Ms. McCullar's recommendation results in PSE recovering the estimated costs in a manner that is fair to the ratepayers that contributed to the reserve surplus.

H. Public Counsel's Residential Rate Design Proposal Does Not Violate the Rate Design Settlement

18. Public Counsel recommends that fuel costs be treated as 100 percent of energy-related costs.[26] PSE argues that this treatment violates the Rate Design Settlement.[27] The Rate Design Settlement required parties to use the Peak Credit methodology. Public Counsel used the Peak Credit methodology and complied with the Rate Design Settlement.

I. Public Counsel's Proposal Regarding Schedule 449 Rate Allocation Is within the Commission's Jurisdiction

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> In practice, the procedure for estimating salvage varies widely. The depreciation professional's judgement of whether a procedure is reasonable is based on several variables. These include the magnitude of the salvage ratio, the available data, and the importance of the depreciable group. It is not unusual for a mass property account of a utility to exhibit large negative salvage. In such cases, the depreciation accrual rate may be more sensitive to the salvage estimate than to the life estimate.

[25] The Settling Parties had the opportunity to question and/or impeach Public Counsel's witnesses at both the August 30 contested hearing and the September 29 settlement hearing, but chose not to. The Settling Parties would not have waited until briefing to attack Public Counsel's witnesses if they truly believed their testimonies were deficient. The Commission should not be persuaded by the Settling Parties' attempts to convince the Commission that Public Counsel's witnesses do not understand the salient facts, key issues, and relevant authority the Commission needs to decide this case.

[26] Response Testimony of Glenn A. Watkins, Exh. No. GAW-1T at 20:12 – 21:5.

[27] PSE Initial Brief ¶¶ 93-94.

19. Customers taking service under PSE's Schedule 449 are retail wheeling customers and thus are transmission customers. The Federal Energy Regulatory Commission (FERC) sets rates for wholesale transmission rates. While some states treat retail wheeling as being controlled under the FERC wholesale wheeling jurisdiction, Washington has not done this. Retail wheeling is tariffed under UTC jurisdiction, requiring Commission approval. Moreover, retail wheeling tariffs are subject to RCW 80.28.020, which requires the Commission to set just, reasonable, and sufficient rates.

20. The Commission historically has allocated costs informed by the Peak Credit method, but FERC rates are not necessarily based on the Peak Credit method. Public Counsel witness, Mr. Glenn Watkins recommends allocating certain transmission costs to Schedule 449.[28] PSE criticizes Public Counsel's recommendation, stating that the rates are subject to FERC jurisdiction.[29] Public Counsel's recommendation is correct because failure to allocate the appropriate costs to Schedule 449 customers results in the rate schedule not achieving parity. Adopting PSE's recommendation creates a situation in which Schedule 449 may never achieve parity. The Commission has the ability to determine rates for Schedule 449 and should do so in this case.

III. CONCLUSION

21. Public Counsel respectfully requests the Commission adopt its recommendations in this case. Highly qualified witnesses evaluated and analyzed PSE's filing, and Public Counsel has

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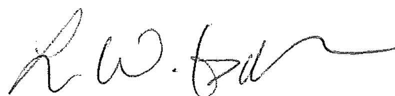
[28] Watkins, Exh. No. GAW-1T at 18:18 – 19:9.
[29] PSE Initial Brief ¶ 101.

presented a case that is balanced and thoughtful. The Company is a healthy utility, and our recommendations ensure their fiscal vitality will continue unabated. For these reasons, the Commission should modify the proposed Settlement and set rates for PSE in accordance with Public Counsel's recommendations.

22. DATED this 27th day of October, 2017.

ROBERT FERGUSON
Attorney General



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