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Filed Via Web Portal

Ms. Amanda Maxwell, Executive Director and Secretary
Washington Utilities and Transportation Commission
621 Woodland Square Loop SE
Lacey, WA 98503

Re: Relating to the Commission's proceeding to develop a policy statement addressing alternatives to traditional cost of service rate making, Docket U-210590

Dear Ms. Maxwell:

Puget Sound Energy ("PSE") appreciates the opportunity to provide comments to the Washington Utilities and Transportation Commission ("Commission") in Phase 1 of Docket U-210590 in response to the April 7, 2022 Notice of Virtual Workshop ("Notice") regarding the requirements of Section 1 of Engrossed Substitute Senate Bill 5295 ("S.B. 5295"), to conduct a proceeding to develop a policy statement addressing alternatives to traditional cost of service rate making, including performance-based measures or goals, targets, performance incentives, and penalty mechanisms. Specifically, the Notice provided the opportunity to submit written comments in addition to oral comments provided during the workshop held on this matter on April 19, 2022.

PSE provides the following written responses, in addition to our comments during the workshop, to the questions in the Notice.

1. What goals and outcomes should be pursued through regulation in Washington?

The goals and outcomes pursued through regulation in Washington should generally reflect the goals and desired outcomes that Washington utility customers have for their utilities and utility service. State policies that reflect the public good are also applied to utility regulation such as clean energy and diversity, equity and inclusion goals. Many of these goals are outlined directly in legislative language in Section 1 of S.B. 5295.

In establishing goals and outcomes, it is also important to consider the financial health of the utility. Utilities must be able to recover the costs of meeting the goals set through this process, while having a fair chance to earn Commission-authorized rates of return.

It is challenging but necessary not only to identify goals and objectives, but also to establish their relative priority across utilities and service territories to enable informed decision making. At times, the pursuit of some goals may be in direct conflict with other goals – for example, investments in reliability or clean energy may often have a direct impact on cost, especially in the short term. Establishing a clear prioritization of goals will be essential to a well-functioning performance-based ratemaking ("PBR") approach.

In embarking on a process to determine the goals and outcomes that apply broadly to regulated utilities, it is also critical to keep in mind that customers and customer perspectives vary within utility territories. Further, utility service territories are unique, with distinct challenges and opportunities depending upon the characteristics of those areas.

2. What are the current regulatory mechanisms, approaches, or processes that are currently influencing or incentivizing utility performance? What behaviors or achievements are currently incentivized?

The performance of Washington gas and electric investor-owned utilities is influenced and incentivized through state policy directives and Commission ratemaking. Influential state policies are outlined in statute, such as the Energy Independence Act ("EIA")[1] and the Clean

[1] RCW 19.285.

Energy Transformation Act ("CETA").[2] Ratemaking practices that affect performance include periodic rate cases, integrated resource planning, PBR approaches, and others.

PSE engaged an expert witness to help develop a PBR proposal in its rate case filed with the Commission at the beginning of this year under Dockets UE-220066 and UG-220067 ("2022 GRC"). PSE's expert, Dr. Mark Lowry, discusses four general approaches to PBR in his report filed in the current rate case.[3] These approaches are revenue decoupling, multiyear rate plans ("MYRPs"), targeted performance incentive mechanisms ("PIMs"), and targeted incentives for underused practices. These four approaches can and often are used jointly by regulators.

PSE's regulatory system currently includes revenue decoupling and PIMs for reliability, customer service quality, safety, and demand side management ("DSM"). MYRPs, which the Regulatory Assistance Project calls "the most important tool of PBR" in their report to the Commission in this proceeding,[4] have been used to regulate the Company's gas and electric services on two prior occasions[5] and are now required to be proposed by Washington utilities in each rate case.[6]

Targeted incentives for underused practices encompass pilot programs that encourage these practices[7], trackers for costs of these practices, capitalization of operation and maintenance expenses that such practices entail (e.g., the "totex" approach to utility cost accounting used in Britain), rate of return premiums on capitalized costs of such practices, and management fees. Several of these approaches have been used in Washington or are permitted by state law. For example, costs of utility DSM programs are tracked, and pilot programs have occasionally been approved.

The relative impacts on utility performance of state laws, rate cases, PBR, and integrated resource planning are difficult to disentangle. For example, financial disincentives for utility

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[2] RCW 19.405.
[3] Second Exhibit to the Prefiled Direct Testimony of Mark Newton Lowry in Dockets UE-220066 and UG-220067 (220066-67-PSE-Exh-MNL-3-1-31-22.pdf)
[4] Elaine Prause and Jessica Shipley, *Performance-Based Regulation: Considerations for the Washington Utilities and Transportation Commission*, Regulatory Assistance Project, 2022.
[5] Dockets UE-951270 and UE-960195, and Dockets UE-121697 and UG-121705 (consolidated).
[6] RCW 80.28.425(1).
[7] Provisions for pilot programs in ratemaking are sometimes called a "regulatory sandbox". See for example https://www.unsgsa.org/sites/default/files/resources-files/2020-09/Fintech_Briefing_Paper_Regulatory_Sandboxes.pdf.

DSM programs are mitigated by the tracking of program cost. PSE's decoupling mechanism works to counter-act the traditional cost-of-service regulatory approach by weakening the direct link between usage and earnings.[8] PSE is also required to establish electric and natural gas energy efficiency targets and is subject to penalties for not exceeding those targets. The combination of incentive provisions and targets has worked reasonably well to encourage robust energy efficiency programs for PSE. But it is difficult to determine the effect of each policy individually.

To date, the balance of incentives rarely encourages exemplary performance by utilities in Washington. Budgets for promising new initiatives are often lean, and PIMs have customarily entailed penalties but not rewards. Some attempts by the Commission to provide positive incentives for non-rate base alternatives, such as additional earnings applied to energy efficiency savings, have been too weak to provide meaningful incentives.

Overreliance on "penalty" mechanisms, statutory compliance, and rules enforcement encourages a compliance mentality and contributes to an environment where doing the bare minimum is all that can be supported. Highly proscriptive rules and an associated compliance mentality can be a burdensome distraction to innovation and progress toward future desired outcomes.

The current regulatory approach maintains the traditional incentives for utilities to financially benefit from investing in capital to provide the essential services provided to their customers. While it is likely that this form of financial incentive may be necessary for the foreseeable future, particularly in light of the significant investments that will likely be required as the industry transitions to cleaner energy sources, complementary incentives may also be required to make this transition in the most efficient manner possible.

Exacerbating this compliance focus, a bias toward ensuring the lowest possible utility rates over all other factors (e.g., reliability, customer service quality, and innovation) is stifling the ability of utilities to move in more progressive directions as swiftly as customers and state policy makers would like us to. While affordability is clearly a key concern regarding utility

[8] Note that, under PSE's current decoupling system, automatic revenue adjustments do not cover all costs that impact its earnings and, moreover, not all customers' sales are subject to these mechanisms. Therefore, a modest linkage between utility sales and earnings continues to exist.

service, particularly for the most vulnerable customers, artificially depressing rates for all customers, including those for whom cost is not their primary concern, is no longer a viable solution. The state and the Commission must find more efficient and effective ways of addressing the concerns of affordability for those that are truly in need in more targeted ways that do not unnecessarily sacrifice the utility's ability to fund and achieve other important policy and customer goals.

Through this PBR initiative, the Commission should consider exploring and adopting incentive approaches that make a deliberate difference in how utilities are compensated for service. One avenue to explore may be looking to service industries to better understand the pricing of services in the absence of significant capital costs. Provisions for pilot programs in MYRPs merit consideration, an approach to ratemaking that is sometimes called a "regulatory sandbox".[9]

Additionally, recent laws authorize new incentive-based approaches that have yet to be executed at the Commission. For example, RCW 80.28.360(2) authorizes an incentive rate of return on utility investments in electric vehicle supply equipment. RCW 80.28.410(2) permits a return on power purchase agreements that are part of a utility's clean energy action plan. RCW 19.405.030(1)(b) permits recovery of the prudently-incurred undepreciated investment in fossil-fueled generating resources that have been retired from service.[10]

3. In what ways does the Commission's current regulatory framework (i.e., traditional cost of service regulation) measure utility performance? What additional performance measures should the Commission be tracking?

The Commission's current regulatory framework has resulted in a proliferation of reporting requirements. In the case of PSE, extensive information is gathered on cost in rate cases and planning proceedings. Additionally, PSE routinely submits reports on its service

[9] See for example https://www.unsgsa.org/sites/default/files/resources-files/2020-09/Fintech_Briefing_Paper_Regulatory_Sandboxes.pdf.

[10] This encourages retirement of such plant.

quality, transportation electrification, demand-side management, and many other dimensions of its operations. Under the provisions of CETA, PSE will now periodically report on its clean energy plans. Utilities file many reports and documents to the Commission, but the continuing use and value of these submissions is sometimes unclear.[11]

Changing business conditions and societal concerns create a need for new performance metrics. Areas of mounting concern at present, as indicated by stakeholder engagement prior to filing PSE's 2022 GRC, include peak load management, electric vehicles, new metering technologies, and equity. These stakeholder discussions led to PSE's rate case proposal for performance metrics in the following areas:

- System average interruption frequency index ("SAIFI") for highly impacted communities ("HIC") and vulnerable populations ("VP"), All Outages, Single Year
- SAIFI for HIC and VP Excluding Institute of Electric and Electronic Engineers ("IEEE")-Defined Major Events (Adjusted to Exclude Catastrophic Days)
- System average interruption duration index ("SAIDI") for HIC and VP, All Outages, Single Year
- SAIDI for HIC and VP Excluding IEEE-Defined Major Events (Adjusted to Exclude Catastrophic Days)
- Peak Load Management Savings
- Peak Load Management Savings Attributable to Residential Customers
- Number of Customers Participating in Gas and Electric Energy Efficiency Programs (Including Low-Income Programs) who are from HIC and VP
- Number of EV Chargers Used in Managed Load Programs or TOU Rates (Single-Family Residential)
- Number of EV Chargers Used in Managed Load Programs or TOU Rates (Fleet)
- Number of Public Charging Ports Serving HIC and VP
- AMI Bill Read Success Rate – Electric
- AMI Bill Read Success Rate – Gas
- Remote Switch Success Rate
- Reduced Energy Consumption from Voltage Reductions
- Number of Low-Income Customers Receiving Bill Assistance (Gas and Electric)
- Share of Bill Assistance Customers who are in HIC and VP

[11] *See* Docket U-210151 regarding utility reporting and information filings. See also comments filed by Avista into this docket on April 22, 2022, which provides a useful illustration of the vast and varied reports required of utilities under the Commission's jurisdiction.

The Commission should review its existing reporting requirements, determine which measures are most strategically useful to measuring the goals and outcomes identified in the proceeding and whether new measurements are needed. As this work is undertaken, it presents an excellent opportunity for the Commission to strategically reassess existing reporting requirements and only retain reporting that has a clear purpose and use.

4. What metric design principles would need to be considered to develop metrics in order to determine which utility behaviors or achievements should be incentivized?

PSE recommends the following design principles be considered for metric development through this proceeding.

Relevant

Metrics should be relevant and clearly linked to the goals of regulation.

Controllable

Each metric should be well within the control of the utility. This is particularly true for metrics that will be assigned targets and used in PIMs.

Targeted

Metrics should address areas where utility performance is a special concern. For example, a metric may appropriately focus on areas that lack strong incentives or on a new performance issue where expectations are unclear.

Efficient

Efficiency matters when choosing metrics used in utility regulation. The creation and routine monitoring and review of metrics is costly. The number of metrics that are routinely monitored should be limited to ensure efficient use of dollars and time.

Prioritized

Metrics, like goals, require some prioritization in order to be relevant, targeted, and efficient.

Comparable

A metric is comparable if it is easy to compare its values between utilities and, for the same utility, over time. Comparability facilitates performance evaluations by making it easier to choose appropriate targets. Metrics that self-adjust for external business conditions are more comparable. For example, SAIDI is more useful than the total length of customer outages because it controls for a key external driver of outage duration: the number of customers that utilities serve. Comparability is also enhanced when the data used in metric construction are standardized and available for the subject utility and other utilities for many years. For example, the comparability of reliability metrics is increased by basing them on standard 1366 of the IEEE, so that definitions of major event days and sustained outages are standardized.

Clear

Metrics should have clear definitions. The required data and any formulas required for their calculation should be identified.

Quantifiable

Data should be readily available or easy to collect and understand.

Verifiable

Metrics, like other dimensions of performance metric systems, should be amenable to independent audit.

Adaptive

Metrics should be revisited every 5 years to ensure continued usefulness.

In practice, these goals cannot always be satisfied at once. The performance-based metric system established by the Commission should seek to strike a reasonable balance of these design principles.

5. What questions should the Commission ask related to regulatory goals, desired outcomes, and metric design principles for the next comment period?

The Commission will have an important task to consolidate the workshop discussion and written comment responses into a coherent framework that can be used to identify goals and outcomes that can provide a firm foundation for regulatory reform as we progress in Phase 1 and later phases of this proceeding. Prior to the next comment period, the Commission should outline common goals, outcomes, and metric design principles and highlight any areas of disagreement for future discussion and comment. It will be particularly important to understand commonalities and differences among stakeholders regarding the ultimate desired outcomes of this proceeding.

The Commission could also look for an opportunity to build on the record of comments to this Notice by asking for prioritization of goals and outcomes in the next round of comments. In particular, PSE suggests exploring the relative importance of various goals and outcomes, such as affordability and clean energy, in order to form a basis for regulatory mechanisms that incentivize utility performance commensurate with the desired outcomes.

PSE appreciates the opportunity to provide responses to the questions identified in the Commission's Notice. Please contact Wendy Gerlitz at (425) 462-3051 for additional information about these comments. If you have other questions contact me at (425) 456-2142.

Sincerely,

/s/ Jon Piliaris

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