Exhibit No. BGM-1T
Docket UE-161123
Witness: Bradley G. Mullins

BEFORE THE

WASHINGTON UTILITIES AND TRANSPORTATION COMMISSION

WASHINGTON UTILITIES AND TRANSPORTATION COMMISSION, Complainant, v. PUGET SOUND ENERGY Respondent.	))))))))))	DOCKET UE-161123

SETTLEMENT TESTIMONY OF BRADLEY G. MULLINS

ON BEHALF OF

THE INDUSTRIAL CUSTOMERS OF NORTHWEST UTILITIES

April 11, 2017

Q. PLEASE STATE YOUR NAME AND BUSINESS ADDRESS.

A. My name is Bradley G. Mullins, and my business address is 333 SW Taylor Street, Suite 400, Portland, Oregon 97204.

Q. PLEASE STATE YOUR OCCUPATION AND ON WHOSE BEHALF YOU ARE TESTIFYING.

A. I am an independent energy and utilities consultant representing large energy consumers throughout the western United States. I am appearing on behalf of the Industrial Customers of Northwest Utilities ("ICNU"). ICNU is a trade association whose members are large electric customers served by electric utilities throughout the Pacific Northwest, including Puget Sound Energy ("PSE" or the "Company").

Q. PLEASE SUMMARIZE YOUR EDUCATION AND WORK EXPERIENCE.

A. I have a Master of Science degree in Accounting from the University of Utah. After obtaining my Master's degree I worked at Deloitte, where I ultimately specialized in research and development tax incentives for multi-national corporate clients. Subsequently, I worked at PacifiCorp as an analyst involved in regulatory matters surrounding power supply costs. I currently provide services to utility customers on matters such as power costs, revenue requirement, rate spread and rate design. I have sponsored testimony in numerous regulatory jurisdictions throughout the United States, including before the Washington Utilities and Transportation Commission ("Commission"). A list of my regulatory appearances can be found in Exhibit No. BGM-2.

Q. WHAT IS THE PURPOSE OF YOUR SETTLEMENT TESTIMONY?

A. I discuss the support of ICNU for the Settlement Stipulation and Agreement ("Stipulation") that resolves all issues in this docket. A summary of the procedural background in this matter can be found in the Joint Memorandum in Support of the Settlement Agreement.

Specifically, I provide ICNU's perspective on the reasonableness of the $23.7 million "transition fee" that Microsoft has agreed to pay, pursuant to paragraph 10 of the Stipulation, and why ICNU considers this fee to be in the public interest given the circumstances of this case.[1/] I also discuss the relationship between the transition fee amount and Microsoft's potential obligation to contribute to Colstrip remediation, decommissioning and/or accelerated depreciation costs.

Q. PLEASE SUMMARIZE YOUR TESTIMONY.

A. The $23.7 million fee that Microsoft has agreed to pay in order to begin taking retail wheeling services will more than compensate the Company's remaining customers for any costs they may incur as a consequence of Microsoft's departure. This is because the amount of this fee does not account for the long-term benefits that the Company's remaining ratepayers will receive as a result of the departure of Microsoft load. This is particularly true considering the benefits that the departure of Microsoft load will provide to remaining customers when the Company retires Colstrip Units 1 and 2, which must occur no later than July 2022. Since the transition fee did not include the long-term benefits of avoiding replacement capacity for Colstrip Units 1 and 2, it was an important consideration for ICNU that the Stipulation contain language explicitly acknowledging that any potential obligations of Microsoft with respect to Colstrip were not resolved by the Stipulation and were reserved for future ratemaking proceedings.[2/] Such a provision

---

1/ Stipulation ¶ 10. See also Exh. No. JAP-1CT at 2:1-9.
2/ Stipulation ¶ 11.

will preserve parties' ability to consider costs and benefits reflected in the transition fee when evaluating any potential obligations Microsoft may have with respect to the retirement of Colstrip Units 1 and 2.

Q. DOES THE TRANSITION FEE ACCOUNT FOR THE FULL AVOIDED COST OF ACQUIRING REPLACEMENT CAPACITY FOR COLSTRIP UNITS 1 AND 2?

A. No. Pursuant to the July 12, 2016 Consent Decree lodged in the United States District Court, District of Montana, the Company and Talen Energy agreed to permanently cease operation of Colstrip Units 1 and 2 on, or before, July 1, 2022.[3/] Retirement of Colstrip Units 1 and 2—which were originally placed into service in 1975 and 1976, respectively—will represent a loss to the Company of approximately 307 MW of capacity.[4/] Due to this loss of capacity and as a result of expected load growth, the Company expects that it must acquire replacement capacity in order to serve its loads in the near future. In fact, based on recent presentations to the 2017 Integrated Resource Plan ("IRP") Advisory Group, the Company now believes that it will have a resource deficit of approximately 550 MW as soon as 2020 if Microsoft continues to be served as a cost of service customer.[5/] When Microsoft departs, however, the Company will be able to avoid acquiring a significant amount of this replacement capacity. However, the methodology used to calculate the transition fee only provided for minimal value associated with avoiding or deferring new resources due to the departure of Microsoft load.

3/ See WUTC v. PSE, Dockets UE-170033/UG-170034, Exh. No. RJR-18 at 6-7.

4/ See PSE 2015 IRP, Appendix K at K-3.

5/ Exh. No. BGM-3 at 14 (Att. A to the Company's Response to ICNU DR 015 (PSE 2017 IRP Advisory Group Presentation at 16)).

Q. WHAT METHODOLOGY DID THE COMPANY USE TO CALCULATE THE TRANSITION FEE?

A. The Company calculated the transition fee based upon a ratepayer impact measure, which accounted for both the savings resulting from the departing load, as well as lost revenue. The Company calculated the annual revenue requirement savings associated with the departure of Microsoft load using the Portfolio Screening Model III.[6/] These model runs, based on resource portfolio assumptions loosely aligned with the Company's 2015 IRP, calculated the savings in energy and capacity costs associated with the departing Microsoft loads. Next, the Company deducted the lost production cost revenues associated with the departure of Microsoft load in order to derive a ratepayer impact measurement associated with the departing load to remaining customers.[7/]

Q. DID THE ANALYSIS PROVIDE REASONABLE VALUE FOR THE CAPACITY AVOIDED AS A RESULT OF THE DEPARTURE OF MICROSOFT LOAD?

A. No. Two aspects of the Company's analysis undervalued the savings associated with avoided replacement capacity. First, the Company limited its calculation of the transition fee to the five-year period 2018 to 2022, limiting recognition of long-term capacity benefits that remaining customers will receive due to the departure of Microsoft load. Second, the Company based its analysis on severely outdated assumptions, which are inconsistent with the current understanding of the Company with respect to its near-term resource needs.

6/ Exh. No. JAP-1CT at 4:3-10.

7/ Id. at 4:11-5:4.

Q. HOW DID THE USE OF A FIVE-YEAR PERIOD IMPACT THE TRANSITION ADJUSTMENT?

A. Based on the resource portfolio assumptions the Company used, Microsoft gets credit for only one year of benefit for avoiding replacement capacity associated with the retirement of Colstrip Units 1 and 2. Notwithstanding, avoiding that replacement capacity will result in material revenue requirement savings to remaining ratepayers over a long-term period, not just for a single year.

Q. WHERE CAN IT BE NOTED THAT THE COMPANY ONLY PROVIDED ONE YEAR WORTH OF CAPACITY BENEFITS?

A. It can be noted in Exh. No. JAP-3C. Over the first four years of the study (2018 – 2021), the rate impact to remaining customers is negative. In the fifth year (2022), corresponding to the timing of the closure of Colstrip Units 1 and 2, the revenue requirement differential and ratepayer impact is positive. My understanding is that it flips as a result of the recognition of the benefits to remaining customers associated with avoided capacity costs driven by the departure of Microsoft load. This benefit extends throughout years five through 20 of the study period. Yet, by limiting the calculation of the transition fee to the five-year period 2018 - 2022, the methodology only provides one year of capacity benefits, even though remaining customers are expected to receive significant benefits over the 20-year study period.

Q. HOW MUCH DO REMAINING CUSTOMERS BENEFIT OVER THE 20-YEAR STUDY PERIOD?

A. Compared to the $23.7 million transition fee the Company proposes, the Company calculated that remaining ratepayers benefit by approximately $23 million on a net present value revenue requirement basis over the 20-year study period. That figure is also likely understated as a result of the use of outdated resource assumptions.

Q. WHY DID THE COMPANY INITIALLY PROPOSE A FIVE-YEAR PERIOD?

A. The testimony of the Company on this topic is limited, though the Company appeared to rely primarily on the Commission's decision and parties' positions in Docket No. UE-132027, the accounting petition regarding the proceeds from the sale of assets to Jefferson County PUD.[8/] The Company noted that parties rejected the Company's position in that docket that it should be awarded the gain on the sale of assets based on a 20-year analysis showing a net benefit to customers from this sale, arguing that calculating benefits this far into the future was speculative. The Company has used similar reasoning in this docket to argue that it would be reasonable to calculate a transition fee over a five-year period.[9/]

Q. IS THIS PROCEEDING DISTINCT FROM THE JEFFERSON COUNTY PUD PROCEEDING?

A. Yes. The Jefferson County PUD proceeding involved proceeds from the sale of assets. In this proceeding, no assets are being sold. Microsoft will still receive distribution, retail wheeling and other services from the Company, and is not receiving ownership of any assets in consideration for its payment of the $23.7 million transition fee. The Commission's decision in the Jefferson County PUD proceeding to allocate the gain on the sale of these assets to customers was not based on a net present value analysis over any particular period. It was based on the principle that customers bore the risks and burdens associated with the sold assets and, therefore, should receive the rewards and benefits.

8/ Id. at 9:13-18

9/ Id.

Additionally, PSE is currently facing an unusual circumstance in that it knows with virtual certainty that it will lose 307 MW of capacity by no later than 2022 with the retirement of Colstrip Units 1 and 2. While ICNU generally agrees that calculations of long-term costs and benefits are more speculative the farther out they go, and was one of the parties that argued against using a 20-year benefits study in the Jefferson County PUD proceeding, it *is* appropriate to account for known future circumstances, and the savings core customers will realize through reduced capacity requirements associated with Microsoft's departure is such a known circumstance.

Q. IS THE PROPOSED TRANSITION FEE ALSO BASED ON OUTDATED ASSUMPTIONS?

A. Yes. The analysis performed by the Company is based on information from its 2015 IRP,[10] although the analysis was not based on any particular study filed in the 2015 IRP. Rather, it appears that the transition fee was based on a study populated with some assumptions from the 2015 IRP, but with a number of other modeling changes based on comments received in the Commission's IRP acknowledgement letter dated May 9, 2016. In reviewing the Company's filing, it was not clear to me why the Company made modeling changes to reflect the Commission's IRP acknowledgement letter but did not update all of its assumptions to be based on more recent information.

Q. IS THE COMPANY CURRENTLY OPERATING UNDER NEW ASSUMPTIONS?

A. Yes. On February 3, 2017, for example, the Company made a presentation to the 2017 IRP Advisory Group. In that presentation, the Company suggested that, after updating

[10] Id. at 7:1-13.

assumptions and incorporating guidance from the Commission's IRP acknowledgement letter, it will have a resource need as early as 2020.[11/]

Q. DOES THE 2020 RESOURCE NEED ASSUME MICROSOFT WILL CONTINUE TO BE SERVED AS A COST OF SERVICE CUSTOMER?

A. Yes.[12/] Accordingly, if Microsoft were to depart from the Company's system, the need to acquire a new resource in 2020, as identified in the 2017 IRP Advisory Group, would be diminished.

Q. WHAT IMPACT WILL THE UPDATED ASSUMPTIONS HAVE ON THE TRANSITION ADJUSTMENT CALCULATION?

A. In discovery, ICNU requested that the Company update the transition fee calculation based on the updated assumptions, as presented in the February 3, 2017 IRP Advisory Group meeting. The Company, however, was not willing to perform the calculation.[13/]

As noted previously, the departure of Microsoft load provides benefits to remaining customers by deferring or avoiding resource acquisitions, as confirmed by the Company's own analysis. Thus, the earlier resource need would mean more significant benefits to customers associated with avoided replacement capacity. In fact, it is possible that, if the assumptions were updated, the departure of Microsoft load would represent a benefit to customers, even if measured over a five-year period.

11/ Exh. No. BGM-3 at 14 (Att. A to the Company's response to ICNU Data Request No. 15 (PSE 2017 IRP Advisory Group Presentation at 17)).

12/ Id. at 15 (the Company's response to ICNU Data Request No. 017).

13/ Id. at 16 (the Company's response to ICNU Data Request No. 018).

Q. GIVEN THESE CONCERNS, WHY DOES ICNU BELIEVE THAT THE TRANSITION FEE IS REASONABLE?

A. The transition fee is reasonable because it is acceptable to Microsoft. With respect to the transition fee calculation, Microsoft shared many of my concerns discussed above.[14/] Notwithstanding, it appears that Microsoft was willing to accept the transition fee amount proposed by the Company for a number of business reasons, many of which have less to do with the economics of the Company's system and more to do with achieving sustainability objectives and supporting its local communities. More than 40,000 Microsoft employees live and work in the Puget Sound area, and accordingly, Microsoft has an interest in ensuring that local communities remain robust and healthy. These types of social considerations are difficult to quantify in terms of IRP portfolio modeling. Yet, they appear to have played an integral role in the willingness of Microsoft to accept the transition fee the Company proposed. Taking these factors into consideration, I view the transition payment to be reasonable not on the basis of stranded costs, but rather on the basis that it represents goodwill on the part of Microsoft.

Q. DOES THE SPECIAL CONTRACT AUTHORIZED BY THE SETTLEMENT MEET THE COMMISSION'S REQUIREMENTS FOR SUCH CONTRACTS?

A. I believe so. The Joint Memorandum explains these requirements in detail and describes why the special contract meets these requirements. I would add that the transition fee Microsoft has agreed to pay more than ensures that the contract charges will recover all costs resulting from PSE's provision of service to Microsoft under the contract. Regardless of Microsoft's commitments to purchase its power from carbon-free energy

14/ See Exh. No.__(GSS-1T).

sources, ICNU considers the net economic benefit that remaining customers will realize through Microsoft's departure to make the special contract in the public interest.

Q. HOW DOES THE LANGUAGE REGARDING COLSTRIP REMEDIATION RELATE TO THE TRANSITION ADJUSTMENT?

A. The ability of the Commission to consider the transition fee amount when evaluating the allocation of Colstrip remediation costs was also an important consideration for ICNU to support the transition fee amount. In paragraph 11 of the Stipulation, parties agreed that the treatment of any of Microsoft's potential obligations with respect to Colstrip remediation expenses would be addressed in future filings. Given the fact that the transition fee provided minimal benefits associated with avoided replacement capacity for Colstrip Units 1 and 2, it would violate the matching principle if, for example, Microsoft were required to pay 18 years' worth of accelerated costs associated with retiring Colstrip Units 1 and 2. Thus, the language in paragraph 11 was important because it preserved the right of parties to consider the transition fee amount when making ratemaking proposals regarding Colstrip remediation, decommissioning and/or accelerated depreciation costs in future rate proceedings.

Q. DOES ICNU SUPPORT THE COMMISSION OPENING AN INVESTIGATION ON RETAIL WHEELING?

A. Yes. Paragraph 11 of the Joint Memorandum identifies a new docket that Staff will request the Commission open to hold a broader discussion of retail wheeling in Washington State. ICNU generally supports customer choice, including the ability of customers to choose how and where they source their power, provided that non-participating customers are not materially harmed, and a state-wide retail wheeling program could provide these customer benefits. While I do not have an opinion about the

Commission's legal authority to adopt such a program, I am aware that the state legislature has expressed a policy preference for at least some level of customer choice by refusing to mandate exclusive service territories in the state. Accordingly, an in-depth examination of the types of customer choice policies that would be in the public interest is warranted.

Q. DOES THIS CONCLUDE YOUR SETTLEMENT TESTIMONY?

A. Yes.