BEFORE THE WASHINGTON
UTILITIES AND TRANSPORTATION COMMISSION

In the Matter of the Petition of	)	DOCKETS UE-121697 and
	)	UG-121705
PUGET SOUND ENERGY, INC.,	)	
and NW ENERGY COALITION	)	
	)	
For an Order Authorizing PSE To	)	
Implement Electric and Natural Gas	)	
Decoupling Mechanisms and To	)	
Record Accounting Entries Associated	)	
With the Mechanisms	)	
	)	
. . . .	)	
	)	
WASHINGTON UTILITIES AND	)	DOCKETS UE-130137 and
TRANSPORTATION COMMISSION,	)	UG-130138
	)	
Complainant,	)	
	)	
v.	)	
	)	
PUGET SOUND ENERGY, INC.,	)	
	)	
Respondent.	)	
. . . .	)	

BRIEF OF PUBLIC COUNSEL

May 30, 2013

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I. INTRODUCTION

1. PSE proposes in these dockets a three-part alternative rate proposal that would result in annual automatic rate increases for customers, potentially totaling over 9 percent by 2017, and generating new combined gas and electric revenues for the Company of $350 million by that time, based on PSE's projections. Customers' rates would not benefit from any general rate case review until 2016 at the earliest.

2. Among the large number of substantive and legal issues, Public Counsel has two key concerns. First, PSE's new "K-Factor" is a *de facto* attrition adjustment that lacks the analytic and evidentiary support the Commission has previously required. The analysis that was provided by PSE, omits *inter alia*, important offsets for revenue growth and deferred taxes that PSE acknowledges in rebuttal were not included.

3. A second core objection to the rate plan is that, although the Decoupling/K-Factor rate plan substantially shifts risk to customers, PSE proposes no reduction in its cost of capital, locking the rate set in 2012 into rates for potentially more than three years. This is particularly troubling given the evidence in this case that PSE's capital costs are declining, independently of any decoupling adjustment.

4. While Public Counsel opposes adoption of the overly broad package contained in the Multiparty Settlement, Public Counsel nevertheless believes that it is reasonable for the Commission to take steps in this proceeding to address concerns about rate case frequency by approving an ERF mechanism. To that end, Public Counsel proposes an alternative rate plan that would allow PSE to obtain expedited rate relief to update its revenues based on a review of changes in actual costs, along the lines proposed by Commission Staff in PSE's 2011 general rate case. In addition, the plan would include full decoupling to allow for a balanced approach to revenue stabilization. Rates under the plan would incorporate a cost of capital adjustment to reflect PSE's reduced level of risk as a result of decoupling.

II. DESCRIPTION OF PSE PROPOSAL

A. Overview of ERF, Decoupling, and the K-Factor Rate Plan.

5. The proposed global settlement has three primary components which would increase rates both immediately, and in the future through automatic annual rate increases, using a predetermined K-Factor.

6. The first component, the Expedited Rate Filing (ERF) was filed on February 1, 2013, to provide an "update" to electric and natural gas delivery rates based upon a modified Commission Basis Report reflecting PSE's results of operations through June, 2012.[1] PSE's proposed ERF would increase electric revenues by $31.9 million and would decrease natural gas revenues by $1.2 million.[2]

7. The second component is the Amended Decoupling petition filed on March 1, 2013, which uses the ERF to establish baseline rates.[3] The modified electric and natural gas decoupling mechanisms constitute "full decoupling," such that PSE is guaranteed recovery of allowed delivery revenues on a "per customer" basis, regardless of changes in consumption due to any factor including abnormal weather, economic conditions, or conservation efforts.

8. The third component is a "rate plan," included within the Amended Decoupling proposal, the vehicle for which is a new type of "K-Factor." While the original PSE-NWEC decoupling proposal had a conservation-based "K-Factor," the new K-Factors are set at predetermined levels, 3.0 percent annually for electric, and 2.2 percent for natural gas, and would be applied to

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[1] Exh. No. KJB-1T (ERF), p. 2:5-7 (Barnard Direct).
[2] Exh. No. JAP-1T (ERF), p. 9, Table 2 (Piliaris Direct) and Exh. No. KJB-1T (ERF), p. 11:5-7 (Barnard Direct).
[3] *See* Exh. No. JAP-14 (Decoupling) for electric allowed delivery revenue per customer and Exh. No. JAP-15 (decoupling) for natural gas allowed delivery revenue per customer.

the revenue per customer calculation each time new rates are determined under the amended decoupling proposals.

9. The Amended Decoupling filing requests an electric revenue increase of $21.2 million and a natural gas revenue increase of $10.8 million in 2013. This is added to the ERF baseline levels so that, for example, the electric revenue increase in 2013 is $53.1 million. Subsequently automatic rate increases take place in 2014, 2015, 2016, and potentially in 2017.[4] As discussed below, as a result of the K-Factor Rate Plan, PSE projects it may recover an additional $350 million in revenues.

10. The Multi Party Settlement recommends approval of the ERF and Amended Decoupling proposals, as filed by PSE. The rates are based on the cost of capital set in the 2011 PSE general rate case with no adjustment to reflect decoupling or other cost of equity capital. Rates would not incorporate an update to cost of capital until 2016 or 2017, at PSE's option.

B. The Rate and Revenue Impact Of The Rate Plan.

1. The Impact on Monthly Rates and PSE Revenues.

11. The various components of the global settlement – particularly the K-Factor Rate plan – would result in substantial additional revenues to PSE during the term of the rate plan. With respect to the decoupling and K-Factor rate plan, PSE has provided a projection that Mr. Piliaris describes as "an illustration of how the mechanism would work for electric customers over

[4] Exh. No. JAP-8T (Decoupling) p. 28 Table 5 (electric) and p. 29 Table 6 (natural gas) for 2013 rate changes (Piliaris Supplemental Direct). Exh. No. JAP-14 (Decoupling) shows electric allowed delivery revenue per customer and Exh. No. JAP-15 (Decoupling) shows natural gas allowed delivery revenue per customer, for the duration of the rate plan, 2013 to 2017.

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time."[5] Total additional electric revenues are projected by PSE to be $227 million through February 2017.[6] The companion projection for the natural gas decoupling and K-Factor rate plan, prepared by PSE, shows additional revenues of $122 million.[7] Therefore, in total, the decoupling and K-Factor rate plan would result in additional revenues of $350 million for PSE, according to the Company's own projections. In addition, PSE would receive the ERF revenues, for which PSE has requested an additional $31.9 million on the electric side.

12. The Amended Decoupling proposal with the K-Factor is predicated upon adoption of ERF rates to establish the baseline for the new decoupling rates in Schedule 139.[8] Together, these proposals result in a net increase for electric residential customers of 3.4 percent, which should trigger a general rate case proceeding.[9] PSE's recent notice to customers showing the rate impact of both the ERF and Amended Decoupling proposals states in part, "The net effect of all these filings on the typical residential electric customer (using 1,000 kilowatt-hours of electricity per month) is a $3.29 bill increase, or 3.4 percent. The net effect of all these filings on the typical residential natural gas customer (using 68 therms per month) is a $1.33 monthly bill increase, or 1.7 percent."[10] Notably, PSE's customer notice does not mention the K-Factor, nor

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[5] Exh. No. JAP-8T (Decoupling) p. 27:10-11(Piliaris Supplemental Direct).
[6] Exh. No. JAP-22 and Exh. No. JAP-26X, Attachment A. Exh. No. JAP-26X was prepared by PSE in response to discovery, and extends the Company's projections provided in Exh. No. JAP-22 through the full potential term of the rate plan. *Please see* Exh. No. JRD-3 for a summary of these PSE revenue projections.
[7] Exh. No. JAP-23 and Exh. No. JAP-26X, Attachment B. Exh. No. JAP-26X was prepared by PSE in response to discovery, and extends the Company's projections provided in JAP-23 through the full potential term of the rate plan.
[8] Exh. No. JAP-14 (Decoupling) and Exh. No. JAP-15 (Decoupling) show "Test Year Allowed Delivery Revenues" and reference PSE's ERF workpapers filed in Dockets UE-130137 and UG-130138, respectively.
[9] This issue is discussed later in this brief.
[10] PSE April/May 2013 Customer Notice. The Notice is attached to this brief as Attachment A.

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does it mention that adoption of the proposal could result in automatic rate increases potentially until 2017.

13. Subsequent rate increases under the K-Factor and decoupling plan are projected by PSE to exceed 2 percent in some years. At hearing, when asked by Commissioner Goltz what the Commission should say in response to customers concerned about a two percent rate increase, NWEC witness Ralph Cavanagh responded as follows:

> And, Commissioner Goltz, I think this is the crucial question. And I think you say two things. First of all, you emphasize we are not raising rates here by two percent. We are not adding something to the cost of service.
>
> What we are doing is ensuring that the revenue requirement that we have deemed reasonable and approved is required no more and no less.[11]

This statement by Mr. Cavanagh contains three glaringly inaccurate assertions:

1. "We are not raising rates here by two percent."

The immediate rate increase is 3.4 percent for electric residential customers. As noted above, PSE has stated this in its customer notice. Subsequent rate increases under the K-Factor rate plan are expected to exceed 2 percent for residential customers, according to PSE's own projections. This is shown in Attachment B, which shows that according to PSE's projections, rate increases for residential electric customers would be 2.7 percent in May 2015, and 2.2 percent in May 2016. For residential natural gas customers, PSE projects a rate increase of 2.7 percent in May 2014.[12]

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[11] Cavanagh , TR. 176:6-12.
[12] *See* Attachment B to this brief, Rate Impact for Average Residential Electric and Natural Gas Customers. While the exact size of future rate increases will depend on customer counts and energy consumption, PSE's allowed

2. "We are not adding something to the cost of service."

The K-Factor provides for predetermined increases in the delivery cost of service. Ms. Barnard, for PSE, testifies that these predetermined increases to allowed revenues per customer are intended "to address the growth in non-energy costs that PSE continues to experience."[13]

3. "What we are doing is ensuring that the revenue requirement that we have deemed reasonable and approved is required no more and no less."

The ERF adds to the current revenue requirement by an update to base rates in 2013. In addition, initial application of the K-Factor would provide an immediate increase to the ERF baseline allowed delivery revenue per customer simultaneous to approval of ERF-updated rates. In each subsequent year through the term of the rate plan, the 3 percent K-Factor (electric) increases PSE's revenue requirement annually by increasing the allowed delivery revenue per customer. The 2.2 percent K-Factor would likewise increase PSE's allowed natural gas revenue per customer.[14] Thus, contrary to Mr. Cavanagh's assertion, the "revenue requirement" to be collected through the K-Factor will be significantly above that justified through the ERF.

14. At a fundamental level, Mr. Cavanagh does not seem to fully understand the implications and operation of the K-Factor rate escalators, nor their true potential impact on customers.

15. Over time, the cumulative impact of the K-Factor rate escalator would result in substantially higher rates for customers. For electric residential customers, PSE's projections

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electric delivery revenues would increase by 3 percent and natural gas allowed delivery revenues would increase by 2.2 percent as a result of the K-Factor.

[13] Exh. No. KJB-1T (Decoupling), p. 3:2-3 (Barnard Direct).

[14] Exh. No. JAP-14 (Decoupling) and Exh. No. JAP-15 (Decoupling). These exhibits show the increases to allowed revenue per customer for electric operations and natural gas operations, respectively, using baseline allowed revenue per customer as filed in PSE's ERF petition, Dockets UE-130137 &UG-130138.

show that the cumulative rate impact would grow to $7.48 per month for the average electric residential customer by May 2016.[15]

16. PSE's Response to Bench Request No. 1 shows that through the K-Factor, PSE's projects recovering an additional $250 million above the revenues that would be generated by the ERF and full decoupling alone. PSE's response shows that with full decoupling and no K-Factor, PSE projects additional electric revenues of $76 million, instead of $227 million with the 3 percent K-Factor, or about $150 million less.[16] PSE's response for natural gas shows $23 million of projected additional natural gas revenues with full decoupling but no K-Factor, compared with $122 million with the 2.2 percent K-Factor, or about $100 million less.[17]

2. The rate plan creates a "tail" which would continue after the end of the plan.

17. One additional aspect of the rate plan that has received limited attention to date is the "tail" effect. As explored with Mr. Piliaris at the evidentiary hearing, the rate plan is expected to generate a deferral balance whether the plan ends in 2016 or 2017. Any positive deferral balance will be collected from customers after the plan ends, concurrently with and in addition to the implementation of new rates should PSE file for new 2016 or 2017 rates.

3. The rate plan does not include a "stay out" with respect to other rate increases.

18. Both PSE and Commission Staff point to the general rate case "stay out" aspect of the Multiparty Settlement as a customer benefit. The "stay out," however, does not protect

[15] Exh. No. JAP-26X, Attachment A. Assumptions incorporated in PSE's projection include adoption of the ERF proposed rates, and PSE's 2012 forecasts for customer counts and energy sales through 2017. *Id.* at p. 1.
[16] PSE Response to Bench Request No. 1, Attachment A. PSE's projections of revenue recovery with the K-Factor for electric operations are shown in Exh. No. JAP-22 and JAP-26X, Attachment A.
[17] PSE Response to Bench Request No. 1, Attachment B. PSE's projections of revenue recovery with the K-Factor for natural gas operations are shown in Exh. No. JAP-23 and JAP-26X, Attachment B.

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customers from annual rate increases. Instead, it continues the pattern they have experienced for the last decade, in which PSE has filed for and received nearly annual rate requests. The "stay out" primarily benefits institutional participants in the regulatory process. From the customer perspective little will appear different. The assumption that continued PSE general rate cases would result in higher rates than the rate plan produces is mere speculation. PSE's last general rate case ordered an electric increase of 3.1 percent, as compared to the 8.1 percent requested by PSE. The natural gas increase was 1.3 percent, compared with the 3.0 percent originally requested.[18] Staff's recommendation in the 2011 case was for a $39 million electric increase (2 percent) and $2.2 million gas increase (0.2 percent). If capital investments and capital costs are declining, rate case outcomes could easily be lower than those established under the rate plan.[19] Given the changing economics, PSE may see significant benefit from a plan which insulates the Company from a thorough review for the next several years.

19. An additional aspect of the rate plan is that the "stay out" only applies to general rate cases. PSE is still permitted to file an unlimited number of power cost only rate cases, with no limits on the amounts requested. PCORCs are not necessarily simple cases. PSE's current filing involves over $700 million in rate year power costs, multiple prudence issues, testimony of 11 witnesses and hundreds of pages of exhibits. In addition, PSE may file one or more requests for rate recovery in connection with the newly available natural gas pipeline replacement tracker. Viewed as a component of a negotiated settlement, this is quite favorable to the Company.

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[18] *WUTC v. PSE,* Dockets UE-111048 & UG-111049, Order 08, May 7, 2012 (Order 08). PSE reduced their natural gas request to $28.6 million, or 2.7 percent, on brief. *Id.* at ¶ 15.
[19] Mr. Schooley agreed with Commissioner Goltz at the hearing that "locking in 9.8…cuts in favor of the company." TR. 131:9-13.

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While these mechanisms would also continue in any event absent a rate plan, the regular occurrence of a general rate case would ensure that rates would periodically be brought back into balance, adjusting for the impact of a PCORC or pipeline tracker. That will not occur under the settlement until 2016 or 2017.

III. THE K-FACTOR RATE PLAN SHOULD BE REJECTED

A. Additional Description of the K-Factor.

20. As noted, PSE's Amended Decoupling proposal in this case includes a "rate plan" the vehicle for which is a new larger K-Factor three times that included in the original filing. Mr. Piliaris, for PSE, describes the rate plan as "a series of predetermined annual increases in authorized rates or allowed revenues intended to afford the Company the ability to avoid the need to file a general rate case over the next two to three years."[20]

21. Under the K-Factor rate plan, the 3.0 percent and 2.2 percent escalation factors would be applied to the allowed revenue per customer on May 1, 2013, and then again on January 1st of 2014, 2015, 2016, and potentially on January 1, 2017, if PSE waits until the end of the 'stay out' period to file a general rate case.[21] For example, for residential electric customers, the allowed delivery revenue collected through volumetric rates would grow from an ERF baseline level of $291.71 per customer effective May 1, 2013,[22] to $303.37 per customer (also on May 1, 2013) through initial application of the 3 percent K-Factor. By January 1, 2017, the allowed delivery revenue collected through volumetric rates would be $353.62 per customer as a result of repeated

[20] Exh. No. JAP-8T (Decoupling) p. 3:15-17 (Piliaris Supplemental Direct).
[21] Exh. No. JAP-14 (Decoupling) (Piliaris) for electric allowed delivery revenue per customer and Exh. No. JAP-15 (Decoupling) for natural gas allowed delivery revenue per customer.
[22] PSE Response to Bench Request No. 001, p. 2, and Attachment A.

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application of the 3 percent escalation factor, for a cumulative increase of over 20 percent.[23] Customers would see new rates on May 1 of each year, according to PSE and NWEC's Amended Decoupling filing.[24]

B. The K-Factor Is A Form Of Attrition Adjustment Lacking The Required Support.

22. There can be little dispute that the K-Factor is simply a form of attrition adjustment. As the Commission has explained, an attrition adjustment is a form of revenue relief afforded to a utility to enable it to address issues of earnings erosion from certain causes, for example, high inflation, or high levels of capital expenditure. A company faces attrition when the relationship between revenues, expenses and rate base from the test period fail to hold in reality in the rate year, creating a revenue shortfall and a potential inability to earn the authorized return.[25] Staff witness Deborah Reynolds confirms in her testimony that the purpose of the K-Factor rate escalator is to "address attrition."[26] Staff witness Thomas Schooley, in his deposition, conceded, that the mechanism is designed to help PSE deal with attrition.[27] These statements are consistent with the fact that the decoupling proposal as a whole, with its K-Factor component, is no longer designed to simply address conservation-caused revenue losses. As it is now designed, it is a much broader revenue stabilization measure that can accurately be described as "attrition decoupling."

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[23] Exh. No. JAP-14 (Decoupling) (Piliaris). ($353.62 – $291.71)/$291.71=20%. The January 1, 2017 allowed RPC levels would take effect if PSE waits until the end of the stay out period to file its next general rate case.
[24] Exh. No. JAP-9 (Decoupling), p. 3 (Piliaris).
[25] PSE 2011 GRC, Order 08, ¶¶ 489-491.
[26] Exh. No. DJR-1T, p. 4:7 (Reynolds).
[27] Deposition of Thomas Schooley, p.36:6-p.37:2 (excerpt in Exhibit No. MCD-4, pp. 5-6).

23. Although the periodic cost escalation element of the K-Factor is an attrition adjustment mechanism by another name, PSE's case falls far short of providing the empirical evidentiary support required to establish attrition. As recently as its last general rate case, PSE's inadequately supported claims of earnings erosion were rejected by the Commission.[28] PSE did not provide an attrition study, which Commission Staff argued was fatal to its claims of earnings erosion.[29] Mr. Schooley testified in the 2011 GRC that PSE had not adequately proven its claim of persistent earnings erosion:

> [I]n general, the Company could have, but did not, provide an attrition study to determine whether, and by how much, PSE is experiencing attrition due to its need to invest in new rate base....If an attrition study had been presented and had confirmed that situation, additional revenues could have been proposed. PSE's presentation of actual versus authorized returns on equity, however, is insufficient to support a claim of attrition.[30]

The PSE 2011 GRC Order discussed Staff's view of what was required for an attrition study.[31] The Order, issued in May 2012 only ten months before the filing of the K-Factor, was clear that while the Commission was open to considering an attrition allowance in a future case, an attrition allowance request would need to be based on an attrition study.[32]

24. Subsequent to the PSE Order, Avista Utilities (Avista), in its 2012 GRC, expressly requested an attrition adjustment, the first such request for many years in Washington. Avista supported its request with a detailed attrition study. Avista's attrition study was largely developed by considering historic trends in expenses and rate base that was concurrently

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[28] Order 08, ¶ 489.
[29] Order 08, ¶¶ 483-491.
[30] Exhibit No. MCD-4, p. 37 (Deen, Excerpt of Testimony of Thomas E Schooley, Dockets UE-111048 & UG-111049, Exhibit No. TES-1T, p. 6).
[31] Order 08, ¶ 487.
[32] Order 08, ¶ 491. The Commission also opined that decoupling was never intended to address incremental impacts of regulatory lag. *Id.*, ¶ 454.

supported by a "cross-check" analysis and adjustments with detailed projections for plant additions, depreciation expense, and Accumulated Deferred Income Tax through the rate effective year.[33]

25. In the Avista 2012 GRC, Staff did substantial discovery and independent analysis. Staff prepared its own attrition study and attrition adjustment recommendation.[34] As a general matter, both the Company and Staff attrition studies in the Avista record contained a detailed examination of historic revenues, expenses, and rate base, as well as budgeted, or forecasted revenues, expenses and rate base.[35] Notwithstanding the attrition evidence in the record, when a settlement was reached, the parties did not agree on whether and how much attrition was present. The Commission's final order declined to make a finding that an attrition adjustment was being adopted, stating:

> Historically, the Commission has approved attrition adjustments only in the context of litigated rate cases, although the Commission has not ruled on such an adjustment in recent years. Such a context permits a thorough review of the evidence necessary for an appropriate adjustment. In the context of the Settlement, however, *we have not had the opportunity either to articulate the appropriate standards by which to assess a proposed attrition adjustment nor evaluate thoroughly the evidence in support of such an adjustment.*[36]

The Commission went on to say:

> [W]e intend to clarify the conditions wherein attrition can be considered when setting rates. As noted above, the Settlement has limited our opportunity to do so here. Accordingly, we will in the near future initiate an inquiry into the appropriate use of attrition analysis in setting rate, including the appropriate methodology to use in preparing attrition studies.[37]

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[33] Exh. No. JRD-1T, p. 26:4-11 (Dittmer, citing Avista testimony).
[34] The procedural schedule for the Avista 2012 GRC permitted sufficient time for detailed discovery and analysis to allow consideration of the attrition request.
[35] Exh. No. JRD-1T, p. 26:11-15 (Dittmer).
[36] *WUTC v. Avista,* Dockets UE-120436 & UG-120437, Order 09, consolidated with *WUTC v. Avista,* Dockets UE-110876 & UG-110877, Order 14, ¶ 70 (emphasis added). (Avista 2012 GRC) (Order 09).
[37] Avista 2012 GRC, Order 09, ¶ 77.

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26. In contrast to the Avista 2012 GRC, neither PSE, nor Commission Staff, purport to have conducted or presented an attrition study in this docket.[38] While PSE did present some historic trend information, it ultimately disregarded that information in finally establishing K-Factor escalation. PSE also failed to address revenue growth trends, as discussed below. As regards rate base projections, PSE offered only a short one-page summary in its initial filing regarding Net Plant in Service.[39]

27. While Staff supports the PSE K-Factor rate plan, its supporting testimony remains at the general policy level, and offers no detailed analysis of earnings erosion or attrition. Mr. Schooley states he relied on PSE's analysis for his conclusions.[40] His chief effort to show earnings erosion is to point to the frequency of PSE GRCs in the last decade.[41] This factor was equally present in PSE's 2011 GRC, a case in which Staff strongly rejected PSE's claims of earnings erosion, including PSE's efforts to rely on such indicators as trends in actual, per-books earnings.[42] Mr. Schooley's conclusion that the Commission can base a finding of earnings erosion on the number of rate cases filed is a marked contrast to the careful analysis Staff has brought to this issue in past cases.

C. The K-Factor Is Methodologically Flawed.

1. PSE failed to properly consider revenue growth/customer growth as an offset.

[38] Exhibit No. JRD-1T, p. 27:18-21 (Dittmer).
[39] Exh. No. KJB-5 (Decoupling) (Barnard).
[40] Deposition of Thomas Schooley, p. 32:19 – 33:18 (excerpt in Exh. No. MCD-4, p. 1:19 – 2:18).
[41] Exh. No. TES-1T, p. 12:18 – 13:5 (Schooley Direct Testimony in Support of Multiparty Settlement).
[42] Order 08, ¶ 484.

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28. PSE's K-Factor analysis has serious flaws, as explained in Mr. Dittmer's testimony.[43] First, unlike Avista, PSE failed to consider how its rate escalators would be impacted by offsets in the form of revenue growth. This is a significant omission from any attrition analysis, a fatal flaw in determining the starting point of analysis. While conceding in discovery that revenue growth is an offsetting factor, PSE initially argued, that in general, new revenues from customer growth would not fully offset increases. No attempt was made, however, to determine the specific offsetting impact of growth on delivery margins.[44] Staff is similarly dismissive of this issue. In his deposition, Mr. Schooley stated Staff had not examined the issue, or asked PSE to provide any analysis regarding revenue growth.[45] Staff's failure to analyze revenue growth offsets to expected cost escalation contrast with Staff's attrition analysis in the Avista GRC and suggests that Staff did not fully analyze the need for the K-Factor escalator.

29. Mr. Dittmer's analysis of customer growth data provided by PSE shows that the impact of growth can be expected to be significant. For example, with customer growth of only 1 percent, the K-Factor would fall fully 1/3 from 3 percent down to 2 percent.[46] On rebuttal PSE witness Katherine Barnard did not dispute Mr. Dittmer's basic criticism that the K-Factor development did not consider customer growth. Instead, she argued that even if taken into account, it still yielded a K-Factor of 3.43 percent (as compared to PSE's original 4.06 percent).[47]

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[43] Exh. No. JRD-1T, p. 23:4 – 38:19 (Dittmer).
[44] *Id.*, p. 30: 3-11.
[45] Exh. No. TES-7X, pp. 2-3 (excerpt of Deposition of Thomas Schooley, TR. 45:24 – 47:7).
[46] Exh. No. JRD-1T, p. 32, Table 3 (Dittmer).
[47] Exh. No. KJB-11T, p.23 (Barnard).

30. Given that this testimony was filed one week prior to the hearing and after the discovery cut-off, a full review of this rebuttal analysis was effectively precluded. However, at least one significant conclusion can be drawn. PSE's flawed calculation – the omission of the revenue growth offset—by itself alters the K-Factor by over 15 percent.

31. An effect of this magnitude on the final calculation, based on correcting for only one of the identified flaws, should be an ample basis to discount the reliability of this "attrition" analysis as a basis for setting rates. Moreover, correcting for this one omission has a significant effect on the so-called 1 percent "stretch" factor pointed to by Staff and PSE as a justification for the negotiated K-Factor level. Even if Ms. Barnard's 3.43 percent were assumed to be reliable, the "stretch" factor is reduced by over 50 percent.

2. The rate base used to calculate the K-Factor is overstated.

32. As noted, when presenting its attrition adjustment proposal, Avista presented detailed support for projected construction expenditures, Plant-in-Service closings, growth in the Accumulated Depreciation Reserve, and growth in the Accumulated Deferred Income Tax Reserve that provided a "cross check" for its rate base attrition that had been prepared utilizing historic trends.[48] However, in contrast to Avista, PSE provided a only one-page schedule of projected growth in Gross Plant in Service, Accumulated Depreciation Reserve and the resultant Net Plant in Service as support for its rate base attrition claims.[49]

33. PSE's abbreviated version of Avista's "cross check" analysis contained a significant error in the calculation of rate base. PSE failed to calculate the well-accepted offset to rate base for

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[48] Exh. No. JRD-1T, p. 37:8-15 (Dittmer).
[49] Exh. No. KJB-5 (Decoupling).

Accumulated Deferred Income Tax (ADIT). In the Avista 2012 GRC attrition studies, this offset was specifically taken into account. In this case, PSE did not initially conduct the analysis or present it in the initial evidence. Staff did not provide any analysis or projection regarding the ADIT offset.

34. In her rebuttal testimony, Ms. Barnard admits that PSE did not initially analyze the ADIT offset, but then attempted to minimize the impact of the omission. She purports to calculate the impact of the ADIT omission and goes on to suggest that the omission does not significantly impact the initial calculation of growth in rate base depicted in Exhibit No. KJB-5.[50] Ms. Barnard's rebuttal analysis Exhibit No. KJB-17 is highly suspect. Even a cursory review of page 3 the exhibit reveals a "hole" in the data presented. While Ms. Barnard reflects 18 months of growth in Net Plant in Service (June 2012 through December 2013), she includes only twelve months of growth in Plant Related ADIT.[51] The omission of six months growth in Plant-related ADIT for this particular time period is significant. During 2012, companies were still permitted to claim "Bonus Depreciation" which can generate significant levels of Plant Related ADIT, which in turn is an offset to rate base. Accordingly, Ms. Barnard's calculation of "Incremental Net Plant less ADIT" has been understated for the period ending December 2013 – and probably significantly.

35. Mr. Dittmer indicated in testimony that ADIT growth, and hence the growth in offset to rate base, could be significant given the impact of utilizing the NOL Carryforward-related

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[50] Exhibit No KJB-17. The procedural schedule effectively precluded inquiry through discovery about the calculations offered in rebuttal testimony.
[51] Exh. No. KJB-17, p. 3.

ADIT.[52] In an attempt to refute Mr. Dittmer's analysis regarding the impact of utilization of NOL Carryforward-related ADIT on rate base growth, when calculating the impact of NOL Carryforward-related ADIT, Ms. Barnard relies on the NOL Carryforward ADIT balance as of June 30, 2013.[53] However, a review of the Company data in Exhibit No. JRD-6C reveals that a significantly higher utilization of NOL Carryforward amounts can be expected in calendar years 2014 and 2015 than Ms. Barnard has shown to be utilized in 2013.[54] It therefore appears probable that Ms. Barnard understates the impact of utilization of the NOL Carryforward in projecting rate base growth in Exhibit No. KJB-17.

36. In summary, PSE's last minute attempt to discount the impact of its admitted omission of ADIT as an offset to projected rate base growth has failed. PSE has not provided credible evidence that the growth in rate base suggested by the historic analysis can be supported by projections of growth in Plant in Service, Accumulated Depreciation *and* Accumulated Deferred Income Taxes. This means that the rate base used in calculating the K-Factor is overstated and does not provide a basis for establishing fair, just, and reasonable rates.

3. PSE's capital investment may be shrinking.

37. As noted above, PSE's initial evidence provided a only one-page schedule of projected growth in Gross Plant in Service, Accumulated Depreciation Reserve and the resultant Net Plant

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[52] NOL Carryforward-related ADIT results in an "addition" to rate base. On the other hand, the "utilization" or *reversal* of NOL Carryforward-related ADIT *reduces* rate base valuation. In other words, the more NOL Carryforward ADIT declines (is "utilitzed"), the larger the ADIT offset to rate base.
[53] Exh. No. KJB-17, pp. 1-2 (Barnard).
[54] The utilization of NOL Carryforward amounts suggested on Exh. No. JRD-6C has not been broken into gas and electric operations, nor have the amounts attributable to "production" versus "ERF" electric operations' rate base been delineated, due to time and discovery constraints.

in Service as support for its rate base attrition claims.[55] At hearing, during questioning from Commissioner Jones, Mr. Schooley conceded that PSE's apparent declining trend in capital investment during the term of the rate plan "could be" a concern.

> COMMISSIONER JONES: And so if you're basing your support for quote "under earnings and regulatory lag" on 2006 to '11 when CAPX was fairly high, and CAPX is going to go down during the period of the rate plan, that's -- that could be a concern, at least to me, the way this new mechanism would operate.
>
> MR. SCHOOLEY: It could be. I don't think the rate plan aspects of it are fully -- fully capturing increases or decreases in the CAPX expenditures. I think it's also part of the ongoing expenses that it's addressing as well.
>
> COMMISSIONER JONES: The A&G or the operations and maintenance?
>
> MR. SCHOOLEY: Correct, yes.[56]

8. Mr. Schooley appears to be saying that the rate plan is not just about capital investment plans, it's also justified on the basis of other ongoing expenses, including A&G and operations and maintenance (O&M). However, capital expenditures for technology investments are often justified by O&M savings expected to be achieved as a result of such investment. Given that the primary justification for attrition adjustments in an era of low inflation is high capital expenditure, Mr. Schooley's apparent dismissal of Commissioner Jones' concern is surprising, particularly in light of statements he made during his deposition that the "primary purpose" of

[55] Exh. No. KJB-5 (Decoupling).
[56] Schooley, TR. 282:3-13.

the K-Factor rate plan "is to address the Company's known capital needs and expense growth over the next few years."[57]

39. Moreover, it may in fact be the case that PSE's recent technology investments will result in reduced A&G and O&M costs. Ms. Barnard, for PSE, testified that capital investment was large in 2013 due to "big technology projects" including OMS, GIS, and a customer information system.[58] These types of capital investments in technology are often pursued because they generate future operations and maintenance cost savings, by identifying and implementing efficiencies or by substituting capital costs for labor costs. No party has analyzed whether the surge in technology investments that PSE has incurred, or projects, between June 30, 2012 and December 2013, can be expected to achieve operational savings. If in fact operational savings are the drivers for such significant technology investments, it would be inappropriate to consider or use historic growth or forecasted CPI changes in O&M expense as a component of escalator development underlying the K-Factor without consideration of the savings. In sum, PSE's forecasts indicate shrinking rather than growing capital investment in non-production plant, and also raise doubts as to whether cost trends in A&G and O&M expenses will persist in the future. This is another indication of why Public Counsel recommends use of an expedited rate filing (ERF) mechanism, based on updates using actual data, rather than the K-Factor rate plan advocated by PSE, NWEC, and Staff.

[57] Deposition of Thomas Schooley, p. 35:22-24 (excerpt in Exh. No. MCD-4, p. 4:22-24; *see also* p. 3:3-8).
[58] Barnard, TR. 163:-164:6.

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4. Jefferson County sale.

40. An added issue with the rate base calculation is the impact of the sale of the Jefferson County service territory to Jefferson County PUD. This is an issue explored by ICNU and raised at hearing. Public Counsel is also concerned that the failure to account for this sale distorts the rate base calculation in the K-Factor.

D. Customer Protections Are Not Adequate.

41. PSE and Staff attempt to assuage fears about the rate plan by pointing to the "rate cap." As Mr. Dittmer points out, however, the benefits of the rate cap are likely illusory. Since the K-Factor only applies to one-third of base rates (the delivery rate), it is unlikely that the cap would ever be reached. Even if the cap is exceeded, the cap merely postpones rate impacts, allowing them to be collected in full at a later time, with interest.[59] This is hardly a customer protection. The earnings test allows PSE to earn 25 basis points above its authorized level before coming into effect. Even at that point, the company is allowed to keep 50 percent of its overearnings. Given that there is substantial evidence in the record that the proposed rates are based on an inflated cost of capital, this earnings test is scant comfort to ratepayers.

E. The K-Factor Is Not A Sound Basis for Setting Fair, Just, and Reasonable Rates.

42. In addition to the important technical flaws discussed in the previous sections there are other reasons why adoption of an attrition adjustment like the K-Factor is not appropriate in this case. The Commission has not adopted an attrition adjustment for many years, and has not done

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[59] Exh. No. JRD-1T, pp. 38-39 (Dittmer).

so outside of a general rate case.[60] Attrition adjustments that have been allowed were one-time additions to the revenue requirement.[61] Public Counsel is not aware of an instance where the Commission has approved multi-year automatic attrition adjustments. While the Commission has indicated it was open to considering attrition adjustments, it has not yet established current policy guidance on the issue. The Commission was clear that its order in Avista did not constitute a precedent on attrition. Indeed, the Commission stated that it would conduct a workshop on the subject following the rate case in order to establish attrition policy guidelines and parameters for attrition studies.[62] That proceeding has not yet taken place.

43. The duration of the rate plan is also of concern. The Commission was appropriately cautious in its approval of a "rate plan" in the Avista 2012 GRC for only two years. Even when presented with fully developed attrition studies for the first of the two years, the Commission was concerned about extending past the first rate year, due to the lack of information that would justify providing returns on investments that were not yet made and might never be made. In this case, the grounds for such concern are magnified where there is substantially less information available and the rates increases could continue for up to four years. There is no basis for the Commission to conclude that PSE rates in 2016 or 2017 will be fair, just, reasonable, and sufficient, when they are based on a 2010 test year, "updated" to a now dated Commission Basis Report, and then escalated by a poorly supported K-Factor.

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[60] The last attrition adjustment adopted in Washington was in 1986. *Washington Utilities & Transportation Commission v. Pacific Power & Light Co.,* Cause No. U-86-02, Second Suppl. Order, 1986 Wash. UTC Lexis 7, 47-50.
[61] *See, e.g., Washington Utilities & Transportation Commission v. The Washington Water Power Co.*, Cause Nos. U-81-16, Second Suppl. Order (November 25, 1981), 1981 Wash. UTC Lexis 3.
[62] Avista 2012 GRC, ¶ 77.

44. Mr. Schooley observed at the hearing that he would "welcome the chance of experimenting in this case, and I think the commission should too." [63] Certainly, there is role for new mechanisms, if they are within statutory authority, carefully developed, based on solid data analysis and have stakeholder input and Commission guidance. Experiments involve risk however. Pilot projects with limited duration and impact and with planned-for evaluations are ordinarily the preferable vehicle for "experiments." Without a policy foundation, and without a record to support attrition, approval of the K-Factor becomes nothing more than risky experimentation on PSE customers.[64] In this case, on this record, approval of such an experiment on over one million residential and business customers, perhaps lasting until 2017 if PSE chooses, at a potential cost of hundreds of millions of dollars, is not justifiable.

IV. THE EXPEDITED RATE FILING (ERF)

45. Commission Staff proposed a recommendation in the last PSE GRC which would address the issue of PSE's regulatory lag. Mr. Elgin emphasized that any response should be "consistent Commission practice and long-standing rate making principles embodied in an historical rate

[63] Commissioner Goltz asked Mr. Schooley "To what extent is Staff's endorsement of the settlement based on a desire to basically engage in some experimentation?" Goltz, TR. 177:10-12.

[64] Mr. Schooley at the hearing cited the Periodic Rate Adjustment Mechanism (PRAM) as an experimental rate mechanism that was approved for PSE in the early 1990s. TR. 177:21-25. The PRAM was not deemed a successful experiment and was ultimately terminated. The Commission concluded: "[w]e have learned from PRAM that new approaches to regulation must explicitly address the balance of risks and costs between customers and the company. As we have long noted, ratepayers should not shoulder the burden of risks shifted to them by any regulatory mechanism without receiving demonstrable and commensurate benefits." *Washington Utilities and Transportation Commission v. Puget Sound Power & Light Company*, Docket UE-950618, Third Suppl. Order, p. 7. By contrast with the current K-Factor proposal, the PRAM had a statutory basis (RCW 80.28.260) and was initiated only after five months of work by stakeholders in a collaborative docket (Notice of Inquiry). *Id.*, p.3.

base matched with test period revenues and expenses that are normalized and include accepted adjustments to the test period." [65]

46. Mr. Elgin envisioned that immediately following the determination of a fully contested rate case, PSE could filed an "expedited rate case" using an updated test year. This case would be an "update" to the relationships between rate base, revenue and expense. The Company would be precluded from seeking a changes in the rate of return, except to update debt costs, and rate spread/rate design. Further, the filing would only contain restating adjustments to minimize controversy.[66]

47. The Expedited Rate Filing (ERF) at issue in this case was filed on February 1, 2013.[67] The purpose of the filing is to address regulatory lag and provide an "update" to electric and natural gas delivery rates.[68] The ERF filed in this case differs in several respects from the ERF proposed in the PSE 2011 GRC, as discussed by Mr. Dittmer in his testimony.[69] The proposed ERF revenue requirement is based on a modified Commission Basis Report (CBR) prepared by PSE, but with a test year for twelve months ending June 30, 2012. The filing does not include any "proforma" adjustments, but does include certain "restating" adjustments. Notably, the ERF reflects a rate base valuation using end-of-period (EOP) rather than the average of monthly averages (AMA) rate base approach used in PSE's last general rate case and typically reflected

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[65] Exh. No. B-2 (Dockets UE-111048 & UG-111049, Exh. No. KLE-1T, p. 80).
[66] *Id.*, p. 81.
[67] It is Public Counsel's understanding that the February 1, 2013 ERF filing resulted from late January 2013, meetings between PSE and Staff that did not involve other stakeholders. In September and October 2012, PSE held two meetings with stakeholders, including Public Counsel, regarding an ERF proposal, which did not result in resolution of issues. To Public Counsel's knowledge, no further meetings occurred until after the February 1, 2013, filing. Letter of Public Counsel, March 13, 2013, n.2 (filed in Centralia, ERF, Decoupling dockets).
[68] Exh. No. KJB-1T (ERF), p. 2:5-7 (Barnard Direct).
[69] Response Testimony of James R. Dittmer, Exh. No. JRD-1T, pp. 16:18-18:18.

in the Company's CBRs.[70] PSE's proposed ERF requests an *electric* revenue increase of $31.9 million or a 1.6 percent average increase.[71] With respect to *natural gas* operations, the ERF filing shows a surplus of $1.2 million, resulting in an average decrease of about 0.1 percent.[72]

48. With the modifications recommended by Mr. Dittmer, Public Counsel can support the use of an ERF mechanism as part of an alternative rate plan, as discussed below.[73] The impact of Mr. Dittmer's modifications results in an ERF increase for electric operations in the amount of $14,838,021 and an ERF reduction for gas operations in the amount of $13,024,871.[74] As Mr. Elgin, explained, the ERF mechanism has several beneficial characteristics:

- The new rates would be based upon known costs—not budgets.
- The process captures changes to customer growth in a timely manner.
- It provides a mechanism to implement rate changes to maximize the impact of financial results.
- The process is transparent and retains the self-regulating aspects of historical test-period ratemaking which dampen the Company's incentive to overinvest in new infrastructure.[75]

From Public Counsel's perspective, these characteristics make the ERF a more desirable alternative ratemaking mechanism than the K-Factor.

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[70] Exh. No. JRD-1T p. 12:3-19.
[71] Exh. No. JAP-1T (ERF), p. 9, Table 2 (Piliaris Direct).
[72] Exh. No. KJB-1T (ERF), p. 11:5-7. The decrease casts doubt on the need for use of a K-Factor on the gas side.
[73] Exh. No. JRD-1T, p. 7 (Dittmer).
[74] Exh. No JRD-1T, p. 20 (Dittmer Direct). In rebuttal PSE witness Barnard proposes corrections to certain adjustments proposed by Mr. Dittmer in his ERF analysis and calculates a new revenue deficiency to reflect these corrections. Upon further analysis, it is possible Mr. Dittmer could be able to accept some of these corrections. Upon Commission request, Public Counsel could direct Mr. Dittmer to conduct the further analysis required to determine which adjustments proposed by Ms. Barnard might be acceptable and calculate what the final revenue requirement for the ERF would be with these updates. That information could be provided in response to bench request.
[75] Exh. No. B-2 (Dockets UE-111048 & UG-111049, Exh. No. KLE-1T, p. 82).

V. DECOUPLING

49. PSE and NWEC originally filed a joint petition for decoupling on October 25, 2012. That proposal was the first filed in Washington to include a K-Factor as an adjustment to the revenue per customer calculation. The K-Factor included in the original proposal was characterized as "conservation-based," but resulted in a proposal similar to the Conservation Savings Adjustment (CSA) proposed by PSE and rejected in the Company's last rate case.[76]

50. PSE and NWEC filed an Amended Decoupling petition on March 1, 2013. The amended gas and electric decoupling mechanisms are "full decoupling," such that PSE is guaranteed recovery of allowed delivery revenues on a "per customer" basis, regardless of changes in consumption due to any factor including abnormal weather, economic conditions, or conservation efforts. The allowed delivery revenues from the ERF filing would serve as the baseline for the modified decoupling mechanisms.[77] The Amended Decoupling filing requests an initial *electric* revenue increase of $21.2 million, an average increase of 1.0 percent, and a *natural gas* revenue increase of $10.8 million, an average increase of 1.1 percent.[78] The increases for residential customers are higher, at 1.6 percent and 1.8 percent respectively for electric and natural gas.[79]

51. Public Counsel does not oppose Commission approval of full decoupling so long as an appropriate adjustment is made to cost of capital, as recommended in the next section of the brief. Full decoupling is a more balanced approach that provides more fairness to customers than

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[76] Exh. No. JRD-1T, p. 21:9 – p. 22:8 (Dittmer).
[77] *See* Exh. No. JAP-14 (Decoupling) for electric allowed delivery revenue per customer and Exh. No. JAP-15 (Decoupling) for natural gas allowed delivery revenue per customer.
[78] Exh. No. JAP-8T (Decoupling) p. 28 Table 5 (electric) and p. 29 Table 6 (natural gas) (Piliaris Supp Direct).
[79] *Id.*

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the earlier proposal in this docket. With a cost of capital adjustment, it is generally consistent with the Commission's Policy Statement on decoupling. Public Counsel can support decoupling as a part of our Alternative Rate Plan described later in the brief.

VI. COST OF CAPITAL

A. If Decoupling Is Adopted, PSE's Cost of Capital Must Reflect The Resulting Reduction in Risk.

52. PSE's cost of capital is an issue in this proceeding, in part by virtue of the request for full decoupling. This Commission has recognized in prior orders that decoupling lowers a utility's risk and should, therefore, be reflected in a lower cost of capital.[80] In its Policy Statement on decoupling, the Commission stated:

> By reducing the risk of volatility of revenue based on customer usage, both up and down, such a mechanism can serve to reduce risk to the company, and therefore to investors, which in turn should benefit customers by reducing a company's debt and equity costs. This reduction in costs would flow through to ratepayers in the form of rates that would be lower than they otherwise would be , as the rates would be set to reflect the assumption of more risk by ratepayers.[81]

53. The Administrative Law Judge at the evidentiary hearing rejected PSE's position that cost of capital is "somehow beyond the scope of this proceeding."[82] As he observed:

> This proceeding involves not only the ERF, but also decoupling, and consideration of the rate of return is a matter expressly called out in the decoupling statement as something that should be considered in the context of a full decoupling proposal.[83]

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[80] 2011 GRC, Order 08, ¶ 446.

[81] *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, November 4, 2010, ¶ 27 (Decoupling Policy Statement).

[82] ALJ Moss, TR. 92:8-12.

[83] ALJ Moss, TR. 92:13-17.

54. The Commission's position on decoupling, risk and allowed return is clear. Decoupling lowers risk and the cost of capital. As a result, an allowed return under a decoupling regime should be lower than that appropriate for traditional rate base/rate of return regulation. The Commission Staff's testimony in this docket is consistent with this view. Staff witness Deborah Reynolds testifies that:

> Full decoupling should reduce substantially the utility's revenue risk by guaranteeing a specific amount of revenue per customer regardless of typical causes of fluctuation in revenue related to weather, economic conditions, or any other condition. Reduced revenue volatility reduces risk which should translate into lower capital costs, either as lower required return on equity or the need for less equity in the utility's capital structure.[84]

At the evidentiary hearing, the issue of whether a risk shift always occurs under decoupling, and therefore whether an adjustment to cost of capital is always necessary, was further explored. Commissioner Goltz inquired as to whether an ROE reduction is justified in situations where revenues are decreasing under decoupling.[85] Mr Hill explains that a risk shift adjustment is always justified under decoupling because the overall effect is that the risk is lowered:

> So what that goes to is the risk of the investment. And so when you—when you—when the decoupling is able to reduce that volatility of revenues, then—and you'll lose some ones that you might win, but you also get pushed up on ones that you're going to lose. So the overall effect is a risk reduction."[86]

Revenue stabilization is a risk reduction in the favor of the Company, regardless of the varying results over time under the decoupling mechanism.

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[84] Direct Testimony of Deborah Reynolds, Exh. No. DJR-1T, p. 8:23 – 9:2.. Staff's recommendation to postpone recognition of the reduction in capital costs for several years until the next general rate case is addressed elsewhere.
[85] Hill, TR. 300:23-301-7.
[86] Hill, TR. 302:4-9.

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55. A reduction of return on equity (ROE) represents the best avenue for the Commission to compensate ratepayers for assuming the volatility risk shifted to them by decoupling.[87] Public Counsel's cost of capital witness Stephen Hill estimates that adoption of PSE's decoupling proposal (not including the K-Factor) would lower PSE's cost of equity capital by approximately 50 basis points, from the current 9.8 percent to 9.3 percent.[88] ICNU witness Michael Gorman recommends an ROE reduction of 50 basis points as well to reflect decoupling.[89]

1. Postponing the recognition of reduced cost of capital harms customers.

56. While agreeing that full decoupling substantially reduces PSE's revenue risk, Staff witness Ms. Reynolds recommends that no action be taken to recognize the reduction in capital costs until several years hence, when PSE next chooses to file a general rate case. This approach cannot produce just and reasonable rates. Absent a determination and incorporation of the reduced capital costs at the present time, ratepayers will be absorbing PSE's volatility risk while at the same time providing excessive returns to PSE's investors. This would continue until 2016 or 2017, at PSE's option.

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[87] At the evidentiary hearing Chairman Goltz asked Mr. Hill what the merits were of changing the capital structure versus an ROE reduction in the context of decoupling, if there was one. Mr. Hill testified that while both methods worked to produce the same result, reducing ROE was preferable: "I think they work to produce the same thing. You're looking to how you can come to the same overall return and there's more than one way to do it. You can change the capital structure, essentially assign a hypothetical capital structure to set rates on, which has been done before. The purpose of it is recognize the lower risk of decoupling, and you can do that through lowering the common equity ratio, effectively raising the debt ratio and|setting rates on that basis using the same capital costs. I don't think that that's a preferable method.....But in this exercise, my preference is to lower the common equity ratio. I think that's the causation focus here with decoupling." TR. 295:22-296-6 and TR. 297:17-19.

[88] Exh. No. SGH-1T (Hill Direct), p. 11:12 – p. 12:17. Mr. Hill also addresses the option of adjusting PSE's capital structure to reflect reduced risk, but recommends the ROE reduction as the preferred approach. As noted, he addressed this point at the hearing.

[89] Direct Testimony of Michael Gorman, Exh. No. MPG-1T, p. 5:13 – p. 6:3.

57. Under the PSE/Staff approach, ratepayers will be forced to forego the flow-through of the reduced costs reflected in lower rates for years, and there would be no opportunity to retroactively recoup those lost financial benefits. It is difficult to imagine that a utility, with demonstrable evidence of *increased* capital costs, would be willing to wait for years to have rates increased to recover those costs, and then only prospectively. Yet, PSE and Staff ask the Commission to impose that very outcome on PSE's customers in the reverse scenario.

58. Neither Staff nor PSE convincingly explain why cost of capital cannot be evaluated in this docket. They argue on procedural grounds that cost of capital can only be established in a general rate case, when this problem is of PSE's own making. PSE chose voluntarily to file its decoupling petition outside of a general rate case, notwithstanding clear guidance in the Commission's Policy Statement to the contrary.[90] It is too convenient for PSE to now argue that cost of capital is beyond review.

59. It is also noteworthy that PSE and Staff are comfortable with the Commission adopting a novel rate mechanism such as the K-Factor outside a general rate case, while objecting that cost of capital cannot be addressed. Given that PSE has brought forward at the hearing evidence of its reduced cost of debt, and agreed that it should be taken into account, PSE cannot reasonably object to the Commission also determining and reflecting the current cost of equity capital.

60. The argument that we should wait and see what happens over the course of the rate plan betrays a confused understanding of the nature of a cost of capital determination. Cost of capital analysis determines what the cost of capital is at the time of the determination. In a rate case, the cost of capital is determined as of the time of the test year, effectively a present cost of capital for

[90] Decoupling Policy Statement at ¶ 18 n.33 and at ¶ 28, ¶ 34, and ¶ 36.

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the company – a known and measurable cost. PSE has a cost of capital now. It can be determined now, in this case, by a current analysis and has been in this record, in Mr. Gorman's analysis. Mr. Hill's testimony is corroborative of Mr. Gorman's conclusions, though it is not a full analysis. While a cost of capital determination made in 2015 or 2016 will tell the Commission what the cost of capital is at that time for purposes of prospective rate setting, it would have little if any value in determining what impact decoupling had on capital cost in the intervening years. It certainly would have no benefit for customers during the years of the rate plan.

2. The studies regarding decoupling cited in rebuttal are not persuasive.

61. PSE and NWEC both cite studies in rebuttal that purport to show that decoupling should not cause reduced capital costs. A closer look at both of the studies shows that they do not support the points for which they are offered.

62. Mr. Cavanagh places substantial reliance on the Graceful Systems Report (Pamela Morgan) to argue that no capital cost adjustment need be made for decoupling and that rate impacts generally are overstated. The Morgan study does not support his claims. Contrary to the assertion that decoupling is everywhere, the Morgan report shows the majority of states still do not have decoupling. There are 27 states with no gas decoupling and 30 with no electric decoupling.[91] The report shows that decoupling did not lead to balanced outcomes, but instead: "[a]cross all electric and gas utilities and all adjustment frequencies, 63 percent were surcharges

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[91] Exh. No. RCC-5 (Graceful Systems/Morgan Report), p. 3: Indication on the map in the Morgan paper that a given state has adopted decoupling for its gas or electric utilities, or both, does not necessarily mean that every utility in the state has a decoupling mechanism. So, even if the majority of utilities in a state have no decoupling, the state is counted in the decoupling column in the report. See n.5.

and 37 percent were refunds."[92] With regard to cost of capital adjustments nationally, the study found that over half of the time a utility has adopted decoupling, it has been as the result of commission approval of multi-party settlement agreements, without the need for a cost of capital decision.[93] The next most common reason for the lack of a specific ROE reduction is that the issue, while recognized, was incorporated in the overall analysis that resulted in an ROE decision.[94]

63. The Brattle Group Study was referred to in the Rebuttal Testimony of PSE Witness Doyle.[95] Mr. Doyle asserts that this study found that decoupling may actually increase a utility's overall business risk, albeit to a very small extent.[96] This conclusion is contrary to one of the fundamental tenets of modern finance -- that risk and volatility are directly related. This principle is *inter alia,* the foundation of the CAPM and the beta.

64. Furthermore, based on Public Counsels' review of the cited study, Mr. Doyle fails to address a number of elements of the study which cast doubt on its value. A threshold problem is that the study period encompassed the 2008-2009 financial crisis, an unprecedented period of dislocation of financial markets, which would make any cost of equity estimate made during that time suspect as a basis for drawing generally applicable conclusions. In addition, the companies

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[92] *Id.*, p. 4. Mr. Cavanagh cites numerous small "rate adjustments" reviewed but the study acknowledges that some of adjustments are monthly, which makes the average amount of the rate adjustment appear smaller.
[93] The Graceful Systems (Morgan) paper identifies the primary reason (pp. 14, 15):
[94] *Id.,* For example, the Morgan paper states: "In Massachusetts, Connecticut and Hawaii, the Commissions found that decoupling reduces the utility's business risk but declined any specific quantification and considered this along with model results, comparisons to proxy companies, and other considerations such as management quality and public policy changes in choosing an ROE within the range to which experts had testified." *Id,* p. 15.
[95] Exh. No. DAD-1T, p. 12:5 (Doyle).
[96] The study concludes that the cost of capital with decoupling was 5.6 basis points (0.056%) *higher* with decoupling than without. This is a very small margin on which to base any conclusions, even if the study were given some credence.

studied were gas distribution holding companies, many of which have substantial unregulated energy marketing operations, making equity cost estimates poor approximations of regulated cost of capital. A further problem with the study is that the results are based on cost of capital estimates authored by Brattle Group members on behalf of gas distributors during the period 2005-2010,[97] which causes the study to lack objectivity. Finally, for the group of gas holding companies studied, nearly two thirds *had no decoupling.*[98]

65. Public Counsel's recommended 50 basis point adjustment to the Company's ROE works out to be approximately a 1 percent reduction in the Company's total revenue requirement (about $15 Million out of a $2B revenue). As such, according to the Morgan (Graceful Systems) report, our adjustment is commensurate with the level of rate increases that ratepayers may receive as a result of decoupling and, therefore, constitutes an appropriate "give and take" for the ratepayers absorbing the rate volatility risk. If decoupling proponents urge that it is "not about the money," when discussing a decoupling rate increase of 2 percent, then its fair to inquire why the Company would be concerned about an ROE reduction that amounts to only 1 percent of rates.

B. The Cost of Capital Is Trending Down.

66. There is convincing evidence in the record that PSE's cost of capital is trending down. PSE's current ROE of 9.8 percent was set using data from 2011, now approximately two years old. Mr. Hill provides evidence that capital costs have declined since then, based on his review

[97] Brattle Study, p. 5.

[98] Brattle Study, p. 6. 63 percent of the gas holding companies had no decoupling, 26 percent had some form of decoupling and the remaining 11 percent had straight fixed variable rate design, which was considered to be decoupling in the study.

of corporate bond yields.[99] Current bond yields are about 125 basis points below that levels that existed in early 2011, and 50 basis points below the level in late 2011. Anecdotally, Mr. Hill cites a recent full cost of capital analysis he performed which concluded that a reasonable ROE range was from 8.5 to 9.5 percent for BBB-rated electric utilities.[100] The Commission itself noted in its Avista 2012 General Rate Case order that "equity returns continue to trend downward" and that had the Avista case not been settled "may very well have decided that an ROE of less than 9.8 percent [for Avista] would have been warranted."[101]

67. As just noted, PSE has now conceded that its cost of capital is lower than that set in the 2011 GRC, by reporting a reduction in its debt cost. This new information helps corroborate the other evidence in the record of declining capital costs and is consistent with Mr. Hill's prediction in testimony. PSE was asked to quantify the impact of the change in Bench Request No. 2.

68. With the lower cost of debt just reported by PSE, Table I on page 14 of Mr. Hill's

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[99] Exh. No. SGH-1T, p. 9, Chart 1 (Hill).
[100] *Id.*, p. 11.
[101] Avista 2012 GRC, Order 09, ¶ 74.

testimony would now read as follows:

	Share percent	Cost percent	Weighted Cost percent
Equity	48.00	9.00	4.32
Long-Term Debt	48.00	6.16	2.96
Short-Term Debt	4.00	2.68	0.11
OVERALL ROR			**7.39**

It is appropriate also for the Commission to reset the cost of equity capital to reflect current conditions. Mr. Hill's recommendation of a 9 percent ROE, which includes additional declines in the cost of equity (30 basis points) and decoupling (50 basis points), is the same ROE recommended by Staff in PSE's last general rate case,[102] and was also Staff's recommendation in the 2012 Avista GRC.[103] Seen in this context, Mr. Hill's analysis is conservative.

VII. PUBLIC COUNSEL'S ALTERNATIVE RATE PLAN

69. In many respects the best approach to unraveling the critical issues in these dockets would be for the Commission to initiate an attrition Notice of Inquiry/collaborative, and for PSE to then file a general rate case. This would enable PSE, the Commission and all parties to analyze attrition in a policy framework, set cost of capital, and review any related longer term rate plan proposals on a full record.

70. If the Commission wishes to adopt an alternative ratemaking mechanism at this stage, Public Counsel respectfully offers an alternative plan that heeds recent Commission guidance, and provides balance by recognizing a need for expedited rate relief for PSE while also honoring

[102] Staff Response to Bench Request Regarding Full Decoupling, PSE 2011 GRC, Dockets UE-111048/UG-111049, December 7, 2011, p. 10. "The low end of Staff witness Mr. Elgin's discounted cash flow estimate range in this case is 9.00 percent, but that value could be lower under full decoupling. *Id.*

[103] Exh. No. KLE-1T, p. 2. *Washington Utilities and Transportation Commission v. Avista Corp.*, UE-120436 *et al.*

critically important regulatory principles and precedent. Specifically, Public Counsel's alternative plan includes the following components:

- *ERF proceedings*. To address any earnings shortfall attributable to providing delivery service between rate cases, PSE would be allowed to file up to two additional expedited rate filings (ERF) prior to its next general rate case.
- *Full decoupling*. Public Counsel supports full decoupling provided there is a reduction of the cost of equity capital to reflect the shift in risk to ratepayers. This would address concerns of the NW Energy Coalition and others regarding the throughput incentive.
- *Cost of capital adjustment*. In testimony of Mr. Stephen Hill, Public Counsel recommends a return on equity of 9.0 percent, to reflect the shift in risk resulting from full decoupling as well as PSE's ability to seek rate increases through expedited rate filings.
- *One additional PCORC*. Beyond the recently-filed PCORC, PSE would be allowed to file one more additional PCORC during the term of the rate plan.[104]
- *Rate Plan/Rate Case Stay out*. In light of the expedited rate relief and ability to file an additional PCORC, PSE would be prohibited from filing a general rate case before April 1, 2015, but would be required to do so no later than April 1, 2016, like the plan offered by PSE and included in the Multiparty Settlement.

Public Counsel's alternative is described in more detail in the testimony of Mr. James Dittmer, and also in the cost of capital testimony of Mr. Stephen Hill.[105]

71. Public Counsel offers an alternative in recognition of the Commission's guidance in PSE's last general rate case, encouraging stakeholders to consider alternative approaches to address the frequency of rate cases. The plan advocated by PSE and endorsed by NWEC and Staff, however, is tilted heavily to the benefit of the Company and its shareholder/owners, by failing to acknowledge substantial reduction in risk and increased revenue stabilization afforded PSE.

[104] Public Counsel acknowledges that, depending on the timing of the PCORC and its rate impact, this could raise some procedural issues that would have to be addressed, as discussed later in the brief.
[105] Exh. No. JRD-1T, pp. 42-44 (Dittmer Responsive Testimony) and Exh. No. SGH-1T (Hill Responsive Testimony), p. 11:19 – 12:17.

72. Under Public Counsel's alternative, PSE would be afforded an opportunity to file up to two additional ERF proceedings. The benefits of the ERF proceedings as compared with the K-Factor Rate Plan are significant. The ERF offers greater transparency, examination of known costs, as well as actual changes to customer growth and capital investment, in an expedited fashion, while also retaining the self-regulating aspects of historical ratemaking.[106] Granting full decoupling mechanisms for electric and natural gas operations, subject to the modifications discussed in Mr. Dittmer's testimony, would address the throughput incentive and the concerns of the NW Energy Coalition. In recognition of this reduction in risk, and PSE's ability to seek expedited rate relief, as well as the downward trend in cost of capital, PSE's cost of equity should be reduced to 9.0 percent, as recommended by Mr. Hill.

73. Public Counsel's alternative offers balance, honors fundamental ratemaking principles, and provides for expedited rate relief to update cost recovery, while reducing rate case frequency.

VIII. LEGAL AND PROCEDURAL ISSUES

A. The Decisions in the ERF and Decoupling Dockets Must Be Based Solely On the Record in These Dockets.

74. Washington's Administrative Procedure Act (APA), RCW 34.05.461(4) requires, in pertinent part, that: "[f]indings of fact shall be based exclusively on the evidence of record in the adjudicative proceeding and on matters officially noticed in that proceeding." This principle is reinforced by RCW 34.05.476 which requires the agency to maintain an official record of the adjudicative proceeding and details the required matters to be included in the record.

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[106] Exh. No. JRD-1T, p. 11:8-18 (Dittmer; citing advantages identified by Mr. Elgin, for Staff, in 2011 PSE GRC).

75. The statute then states:

> Except to the extent that this chapter or another statute provides otherwise, the agency record constitutes *the exclusive basis for agency action* in adjudicative proceedings under this chapter and for judicial review of adjudicative proceedings.[107]

Accordingly, in these proceedings, the UTC must make a decision in the ERF adjudication and the Decoupling adjudication based solely upon the record in these adjudications. It cannot base its decision in the rate dockets on the record in the Centralia docket. Nor can it base its decision in the Centralia docket on the record in the ERF and Decoupling proceedings.

76. The approach requested by PSE and Staff to resolve the five dockets in one settlement cannot be reconciled with APA provision. The Multiparty Settlement contemplates expressly that the result in the ERF and Decoupling dockets will be a function of the result in the Centralia docket, and vice versa.[108]

77. The Commission has noted that this presents a serious obstacle. Parties were given notice by the Administrative Law Judge that the issue would be addressed in oral argument at the beginning of the May 16 evidentiary hearing. As Commissioner Goltz framed the issue at the oral argument:

> So that seems to me like the premise of the settlement in ERF and decoupling is premised on a record in a different case. And likewise, the same with you, you're --- the company's view is that it's willing to acquiesce in the equity issue in the Transalta docket because of the record in a different case, the ERF and decoupling cases.[109]

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[107] RCW 34.05.476 (3) (emphasis added).
[108] Multiparty Settlement, ¶¶ 1, 2, 15, 21.
[109] TR. p. 103:21-p. 104:1 .

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Commissioner Goltz later commented:

> No, I'm just wondering if it becomes a legal issue that we're basically looking at the record in one as a justification for the other. If that's true, and we rely on that, then we're looking at extra-record evidence, and we have to base our decision in each of the dockets on a record in that case.[110]

78. PSE[111] and Staff[112] do not appear to dispute that their request requires the Commission to consider the interplay of records in the dockets, but instead argue that the Commission has "been involved in such proceedings before."[113] The settling parties point to multi-docket settlements of the past to suggest that the statute need not be a concern. The cases cited, the PSE 2001 GRC Multiparty Settlement,[114] and the GTE/Bell Atlantic merger case[115] are distinguishable. The Commission had not issued a final order in any of the settled dockets. In addition, the cited cases were all-party settlements.[116] The APA issue was not raised or addressed in the cited orders.

79. Here all the adjudications remain contested dockets which require findings to resolve the disputes on the basis of the appropriate record. The ERF, Decoupling, and Centralia dockets remain separate. The separation is underlined by the fact that notice was not issued for the Centralia docket for the May 16 evidentiary hearing.[117] Absent consolidation, the result requested by PSE and Staff would require the Commission to impose a result on parties to the

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[110] TR. p. 105:3-8.
[111] Carson, TR. p. 101: 21- p. 102:10.
[112] Trautman, TR. p. 108:19-24.
[113] Carson, TR. p. 101:15-16.
[114] *WUTC v. PSE,* Dockets UE-011570/UG-011571, Twelfth Suppl. Order.
[115] *In the Matter of the Application of GTE Corp. and Bell Atlantic Corp.*, Dockets UT-981367, *et al.* Fourth Suppl. Order.
[116] In the PSE 2001 settlement, the Public Counsel residential exchange docket was related to customer rate levels, the issue in the GRC. In the GTE/Bell Atlantic docket, the earnings review and access charge dockets were germane to the merger, since merger review, under Washington's "no harm" standard, examines *inter alia* whether the merger will affect rates and competition. There were no formal proceedings in the Staff's informal earnings review, and the access charge case was dismissed.
[117] Letter from Commission Staff counsel, via email, May 15, 2013. The Administrative Law Judge noted the issue, but did not treat the hearing as "improperly noticed" which would have required delay. ALJ Moss TR. 98:16-24 The hearing was noticed and conducted as a hearing in the ERF and Decoupling dockets.

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ERF and Decoupling dockets, based on an outcome in the unrelated docket (the Centralia docket). While not permissible in any event, this is additionally objectionable in that some parties to the ERF and Decoupling cases are not parties to the Centralia case (NUCOR, Kroger, Federal Executive Agencies).

80. Public Counsel has previously objected to the linkage of the Centralia docket to the PSE rate dockets.[118] There is no relationship between the cases. Centralia does not involve any ratemaking mechanism proposal, and is not a decoupling docket. The Centralia record was closed and an order issued before either the ERF or the Decoupling proposals now at issue were filed with this Commission. PSE's position, expressed in its Petition for Reconsideration, is that if the Commission does not change its Centralia order to meet its objections, "PSE must reject the [Centralia] agreement."[119]

81. At the May 16 hearing Commissioner Goltz questioned Ken Johnson of PSE about the linkage between the dockets.

> Q: "You basically said that the consequence of failing to approve the settlement, would be you'd walk away from the execution of the power purchase agreement, correct?"
>
> A: "I-I think we have made it clear that there-that the conditions in the final order, barring resolution as they are proposed in the global settlement, would prevent the Company from executing the purchase power agreement."
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> Q: "The conditions in the final TransAlta order?"

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[118] Docket UE-121373, Public Counsel Response to Staff Motion for 30-Day Extension (February 5, 2013); Joint Public Counsel and ICNU Response to Staff and PSE Motion for Second Extension (March 12, 2013).
[119] Petition for Reconsideration, ¶ 5 ("Absent reconsideration of these conditions by the Commission, PSE must reject the agreement.") The Commission has expressed concern in the past when placed in this type of situation. *Washington Utilities & Transportation Commission v. Avista Corp.*, Dockets UE-090134, UG-090135, UG-060518, Order 10, ¶ 224.

A: "Correct."

Q: So--

A: Which have been addressed in the settlement."

In further questioning, Chairman Goltz expressed concern that PSE was establishing "a line in the sand" saying "take this settlement or we walk,"[120] effectively asking the Commission to "rubber stamp" the settlement,[121] or to treat it as an "all or nothing"[122] proposition.[123] Mr. Johnson later appeared to moderate the Company's position, ultimately stating that if the Commission did not approve the settlement and modified the rate plan or imposed different conditions, PSE would "re-evaluate"[124] rather than simply not execute the Centralia agreement.

82. This relates directly to the APA issue under discussion. By asking the Commission to resolve the ERF and Decoupling dockets, so as to obtain a certain result in the Centralia docket, PSE is asking the Commission to consider matters outside the rate dockets which have no bearing whatever on the ERF proposal, decoupling or the K-Factor. The fact that the settling parties have been willing to make such "trade offs"[125] does not mean that the Commission must do so.

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[120] Exchange between Commissioner Goltz and Ken Johnson, TR. 126:25-129:2 .
[121] Commissioner Goltz TR. 128:5.
[122] Commissioner Goltz TR. 128:10-11.
[123] The Commission has expressed concern in the past about being placed in a situation of this nature. Avista 2009 GRC Order, ¶ 206.
[124] Johnson, TR. 128:13-129:2.
[125] ALJ Moss, TR. 101:3-6.

B. The Multiparty Settlement Seeks Unlawful Commission Delegation Of Decisionmaking.

83. The Commission rules state that "[t] he Commission cannot delegate to the parties the power to make final decisions in an adjudicative proceeding."[126] The Staff/PSE settlement however, has the effect of requiring the Commission to take certain actions with respect to all three of the dockets. Because PSE and Staff treat the three dockets as one interrelated package, in order to achieve a certain result in the Centralia docket, the Commission is asked to essentially abrogate its rate setting and decision making responsibilities in the ERF and Decoupling dockets and to accept the outcomes prescribed by the parties. This violates the rule.

C. PSE's Rate Requests Constitute a General Rate Case Under Commission Rules.

84. The Commission rules provide that a rate filing which results in a revenue increase for any customer class of 3 percent or more constitutes a "general rate proceeding."[127] There is no dispute that the combined effect of the PSE ERF and Decoupling proposals exceeds that threshold for electric customers. The impact of the rate proposals in 2013 is a 3.4 percent rate increase that will take effect on customer bills on the same day.[128] Moreover, the cumulative effect of the annual K-Factor additions to rates, means that for each subsequent year the cumulative impact of the rate increases further exceeds the 3 percent limit. If the rate plan continues into 2017 the net result is that a residential electric customer will experience a 9 percent increase in rates relative to today's rates, based on PSE's current projections.[129]

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[126] WAC 480-07-700(1).
[127] WAC 480-07-505(1).
[128] This is a logical result of the fact that the ERF acts as the baseline for the Decoupling/K-Factor "rate plan", as described elsewhere in the brief. This is not in dispute.
[129] Attachment B to this brief.

85. The ERF and Decoupling dockets clearly meet the standard for consolidation under the rule --- that the "facts or principles of law are related."[130] The Decoupling mechanism incorporates the ERF as its baseline for calculating additional rate increases under the rate plan.[131] The Commission has treated the two dockets jointly for procedural purposes. The evidentiary hearings were held as "joint proceedings."[132] A further indication of the unity of the dockets is the customer notice issued by PSE, a copy of which is attached.[133] The notice communicates the combined effect of both the increases, describing it as "notice of requested rate increases and public hearing" and in boldface type stating "the net effect of all these filings" for the typical electric and natural gas residential customer.[134]

86. This is an important issue. The Commission's analysis in a general rate case is different than that which has been conducted to date on these requests. In order to enable the Commission to conduct this analysis, any rate request which exceeds 3 percent is required to be accompanied by the specified detailed supporting evidence listed in the rule.[135] PSE has not provided this supporting information to the Commission or other affected stakeholders. The Commission described the analysis which it undertakes in a rate case in detail in its order in PSE's 2009

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[130] WAC 480-07-320. Public Counsel and other parties requested consolidation of the dockets.
[131] Exh. No. JAP-14 (Decoupling) and Exh. No. JAP-15 (Decoupling) show "Test Year Allowed Delivery Revenues" and reference PSE's ERF workpapers filed in UE-130137 and UG-130138, respectively.
[132] ALJ Moss, TR. 86:15 – 87:4 and TR. 98:13-15.
[133] Attachment A. Public Counsel requests that the Commission take official notice of the PSE notice under WAC 480-07-495(2)(i) .
[134] Attachment A. A further issue raised by failure to treat this as a general rate filing is the sufficiency of the customer notice. The notice does not appear to provide "before and after" rates, nor does it accurately describe the proposal, omitting reference to the multiyear rate plan proposal.
[135] WAC 480-07-510.

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GRC,[136] describing its extensive review of revenue, expense, rate base, and rate of return issues, applying the rate-making formula which has been explained by the Washington Supreme Court as the "basic equation," "commonly accepted and used" by regulatory commissions.[137] PSE and Commission Staff's only argument is that because the rate increase arises from the combined effect of two separate dockets, neither of which exceeds the 3 percent level, that the filing does not constitute a general rate case. This is an artificial distinction that elevates form over substance.

D. The Settlement Violates the Power Cost Only Rate Case (PCORC) Provisions Of the 2001 PSE GRC Order and Settlement.

87. The Multiparty Settlement proposal by PSE and Staff raises issues with respect to Power Cost Only Rate Cases (PCORC). The PCORC was established as part of PSE's Power Cost Adjustment mechanism pursuant to a settlement in the PSE 2001 GRC.[138] Under the PCORC agreement, PSE is required to file a general rate case within three months following the conclusion of a PCORC proceeding which results in "an increase to general rates."[139] This requirement provides an opportunity for the Commission to examine offsetting factors, so as to avoid a prolonged violation of the "matching principle" that would result from the single-issue

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[136] *Washington Utilities & Transportation Commission v. Puget Sound Energy, Inc.*, Dockets UE-090704/UG-090705, Order 11, ¶¶ 18-35 (PSE 2009 GRC).
[137] *People's Organization for Washington Energy Resources v. Washington Utilities & Transportation Commission*, 104 Wn. 2d 798, 807-809 (1985).
[138] *WUTC v. PSE*, Dockets UE-011570 & UG-011571, Twelfth Suppl. Order, Exhibit A to Settlement Stipulation.
[139] *Id.*, p. 6, ¶ 10.

ratemaking which the PCORC represents.[140] The PCORC settlement requirements are now a matter of Commission order.

88. This raises two issues. First, the Multiparty Settlement creates a potential violation of the PSE GRC 2001 order establishing the PCORC. Under the Multiparty Settlement in this docket, PSE is permitted to file an unlimited number of PCORCs during the term of the rate plan, but is not required to file a general rate case until 2016. If one or more future PCORC filings results result in "an increase to general rates," the PSE 2001 GRC Order would require a general rate case filing. The Multiparty Settlement directly conflicts with this provision.[141]

89. The second issue involves notice and reopening of the 2001 docket. The 2001 PCA/PCORC settlement agreement was executed by PSE, Commission Staff, Public Counsel, AT&T Wireless Services, Inc., Cogeneration Coalition of Washington, NW Energy Coalition jointly with Natural Resources Defense Council, Federal Executive Agencies, Kroger Co., and Cogeneration Coalition of Washington.[142] Some of these parties are not parties to this case and have had no notice that the PCORC settlement is potentially to be modified. Other parties oppose the modification. Neither PSE nor Staff have requested that the 2001 docket be reopened, or that the PSE 2001GRC order be modified.

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[140] *WUTC v. PSE,* UE-011570 & UG-011571, Twelfth Supp Order, p. 25, citing testimony of Staff witness Merton Lott (the PCORC "is an exception to the general rule that a company should not be allowed to file single issue rate cases.").

[141] During the pendency of the ERF and Decoupling dockets, PSE filed its 2013 PCORC filing. Because as filed, it requests a reduction in rates, this PCORC does not appear at this time to trigger the GRC requirement.

[142] *WUTC v. PSE,* UE-011570 & UG-011571, Twelfth Suppl. Order, Exhibit A to Settlement Stipulation, Settlement Terms for the Power Cost Adjustment Mechanism (PCA), at A1.

E. The Schedule Deprived Public Counsel Of A Fair Opportunity To Review PSE Filings And To Prepare And Present Its Case.

90. The schedule adopted for the ERF and Decoupling dockets was unreasonably and unnecessarily abbreviated to the detriment of Public Counsel's procedural rights.[143] The procedural schedule adopted was inadequate to deal with the numerous complex and significant matters in the cases. The schedule allowed parties one day short of 8 weeks from the initial prehearing conference to the evidentiary hearing to develop their cases. The schedule allowed only 19 calendar and 13 business days (dated from the prehearing conference) to issue and review discovery and prepare and file expert testimony. Parties had one week (5 business days) to review rebuttal testimony and prepare for hearing, and 3 and ½ business days to provide cross-exhibits.[144]

91. The discovery cut-off for the remainder of the case after April 10 effectively precluded discovery of both the response and rebuttal testimony.[145] The schedule impaired the ability of Public Counsel's expert witnesses to conduct necessary analysis of PSE and Staff positions.[146] As a result, the procedural schedule in this case prevented "full disclosure of all relevant facts and issues" and did not provide Public Counsel an adequate "opportunity to respond, present

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[143] The Commission has recognized that part of establishing just rates is that they are based on a record "developed in the proceeding following principles of due process of law." PSE 2009 GRC Order 11, ¶ 18.

[144] On rebuttal, PSE filed testimony of five witnesses, including two new witnesses. Public Counsel's request for leave to present oral surrebuttal at the hearing was denied.

[145] Although the ALJ at the prehearing conference indicated he would entertain requests to conduct discovery past the deadline, this is not an effective substitute for full discovery. As an example, the 3 ½ business days between rebuttal and the deadline for cross-examination exhibit filing made it impractical to review testimony, request and obtain a ruling, review discovery responses and identify potential hearing exhibits, at the same time as hearing preparation. Public Counsel did tender 7 data requests to PSE (5 answered) and 1 to Staff after the deadlines on a consent basis and some answers were provided. The availability of limited discovery at the consent of the adverse party does not substitute for full discovery rights normally accorded parties in Commission proceedings..

[146] Exh. No. JRD-1T, p. 4:1-3: Exh. No. SGH-1T, p.12:15-16 (Response Testimony of Stephen G. Hill); see also Exh. No. MCD-1T, pp. 43-16-17 (Response Testimony of Michael Deen on behalf of ICNU).

evidence and argument, conduct cross-examination, or submit rebuttal evidence" as contemplated under the APA.[147]

IX. PUBLIC COMMENTS

A. Written Public Comments.

92. The Public Comment exhibit in this case consists of letters, e-mails, and other written materials submitted by the public to provide comment on this case. The exhibit includes a total of 218 comments, of these 203 oppose and the requested rate increase and four support the increase; the remaining 11 neither oppose nor support the request. Many of the comments eloquently express concerns with the automatic rate increases and the oversight these will receive, as well as the overall burden experienced by customers facing yet another rate increase from PSE. Another common theme expressed in the comments was that the notice describing the rate increase was unclear and confusing. Mr. Aaron Arkin testified to this in comments submitted to the Commission website:

> "I do not understand why, when the cost of natural gas has been going down, that PSE is requesting a rate increase. I see nothing in their flyer (included in my bill) that clearly explains why this increase is needed or deserved. Their only explanation has to do with what they are calling, "decoupling gas revenues from energy sales." Perhaps they (or their lawyers) think this provides an adequate explanation. But to a lay person like myself, this is nothing more than a smoke screen to discourage rate payers from inquiring as to what the exact reasons for the increase are. If there is a case to be made for this request and the bill flyer is their means to do it, force them to provide a detailed in plain English explanation so that we can make an informed decision as to whether such an increase is justified."[148]

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[147] RCW 34.05.449(2).
[148] Exh. No. B-1, Attachment "PSE Public Comments as of May 17," p. 4.

93. In opposition to the rate increase, Mike and Kay Tuben, wrote, "PSE continues to ask for increases in rates. The people of this state are still reeling from the depression that this country is struggling to pull itself out of. PSE wants increases, yet many remain on wage freezes. Our family has not had a wage increase since 2008. I urge the Commission to take current economic conditions when considering this latest request."[149] Douglas Rauh of Bainbridge Island, expressed his concerns with a lack of oversight associated with future rate cases, writing, "It did not appear to me as if the charges for infrastructure would receive as thorough of a review as is done now. I like the idea of the Attorney General's Public Counsel reviewing all PSE proposed charges on a regular basis."[150] Ms. Geraldine Miles of Kent wrote: "This is to let the Commission know that I am so opposed to another rate increase. As a senior citizen on a very fixed income, this is hard to survive."[151] Robin Smith wrote concerning the impacts of the rate increase on small business:

> "I'm doing all I can right now just to keep my staff employed, and so far have not had to lay off anyone, but neither are they getting any 'rate increases.' Why should PSE? Maybe its time to tighten their belts too. I commented on the previous rate increase, which I believe was only last year—maybe the year before—objecting to that. They told me their shareholders wanted more money. I'm sorry, we all want more money, but right now is NOT the time to grant ANYONE more money. It's time we get tough and say NO for a change! It's either that, or more unemployment as more and more businesses go under."[152]

The concerns of business were also reflected in a letter from The Washington Retail Association which cited concerns, in particular, with the automatic rate escalators. [153]

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[149] Exh. No. B-1, Attachment "Comments Received by Public Counsel," p. 1.
[150] Exh. No. B-1, Attachment "Comments Received by Public Counsel," p. 10.
[151] Exh. No. B-1, Attachment "Comments Received by UTC," p. 13.
[152] Exh. No. B-1, Attachment "Comments Received by Public Counsel," p. 3.
[153] Exh. No B-1, Attachment "Comments Received by UTC," p. 14.

B. Public Hearings.

94. The Commission held a public comment hearing on May 16, in Olympia. Members of the public that attended the public comment hearing echoed similar concerns to those heard in written comments, particularly with regard to fairness of automatic rate increases. Mr. Kim Dobson, a farm-owner in the Olympia area, commented:

> So I'm a little confused about the rate increase, but I think its unfair that the Company should get an automatic rate increase without having to come to this body to check and see if it's actually necessary, and if they've actually made any losses.[154]

95. These are just a few of the over 200 written and oral comments which PSE customers have provided in this case, the vast majority opposing the rate increases under decoupling and ERF rate proceedings. The Commission should keep these concerns clearly in mind in determining a fair, just and reasonable outcome of this case.

X. CONCLUSION

96. The PSE rate proposals before the Commission, combined in the Multiparty Settlement Agreement, are far-reaching in scope and unprecedented in many aspects of substance and structure. Under an extraordinarily abbreviated schedule, PSE asks the Commission to embark upon a wholesale and dramatic departure from Commission ratemaking principles, rules, precedents, and statutory authority which have over time protected both company and customers in a balanced regulatory framework.

97. While individually, portions of these concepts have had some attention in the past, none has been approved by this Commission in the form now presented, nor has the Commission

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[154] TR. 362:17-21.

completed a policy docket or rulemaking concerning the ERF or attrition mechanisms. The evidentiary support provided by PSE (and Commission Staff) for the proposals is notable for its limited analysis, omissions, lack of empirical data, and disregard of previous Commission requirements.

98. A striking feature of the proposals before the Commission is the combination of three company-favorable mechanisms, each a substantial departure from traditional ratemaking principles, in a single package. Each mechanism in its own rite shifts risk from PSE investors to its customers. In combination, as filed, all three create a multiplier effect that tilts PSE's ratemaking regime heavily towards PSE investors' interests and against those of customers. Nevertheless, PSE opposes any reflection of, or even examination of, reductions to cost of capital that follow the reduced risk profile.

99. The best approach to resolve the thicket of issues presented by the PSE proposals is to address them in a near term general rate case where attrition and cost of capital issues could be fully reviewed. If the Commission wishes to approve a balanced alternative ratemaking approach in this docket, Public Counsel recommends adoption of its ERF and Decoupling alternative rate plan, with an adjusted cost of capital. The K-Factor should be rejected.

100. DATED this 30th day of May, 2013.

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