

**BEFORE THE
WASHINGTON UTILITIES AND TRANSPORTATION COMMISSION**

WASHINGTON UTILITIES AND
TRANSPORTATION COMMISSION,

Complainant,

v.

PUGET SOUND ENERGY,

Respondent.

DOCKETS UE-190529 and
UG-190530 (*consolidated*)

In the Matter of the Petition of

PUGET SOUND ENERGY

For an Order Authorizing Deferral
Accounting and Ratemaking Treatment
For Short-life UT/Technology Investment

DOCKETS UE-190274 and
UG-190275 (*consolidated*)

In the Matter of the Petition of

PUGET SOUND ENERGY

For an Order Authorizing Deferred
Accounting associated with Federal Tax Act
on Puget Sound Energy's Cost of Service

DOCKETS UE-171225 and
UG-171226 (*consolidated*)

In the Matter of the Petition of

PUGET SOUND ENERGY

For an Order Authorizing the Accounting
treatment of Costs of Liquidated Damages

DOCKETS UE-190991 and
UG-190992 (*consolidated*)

**REPLY BRIEF OF
THE FEDERAL EXECUTIVE AGENCIES**

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INTRODUCTION

The Federal Executive Agencies (“FEA”) hereby submits its reply brief in this docket. The United States Department of the Navy (“Navy”) represents the Department of Defense and all other Federal Executive Agencies in this proceeding. The FEA is one of the largest consumers of electricity in the service territory of Puget Sound Energy (“PSE” or “the Company”) and takes electric service from the Company, primarily on Schedule 49. The FEA filed response and cross-answering testimony in this docket.

The FEA’s reply brief responds to certain arguments raised by the following parties in their initial post-hearing briefs that were filed in this proceeding on March 17, 2020:

- Puget Sound Energy (“PSE”);
- Public Counsel Unit of the Washington State Office of the Attorney General (“Public Counsel”);
- The Staff of the Washington Utilities and Transportation Commission (“Commission Staff”); and
- The Kroger Company (“Kroger”)

The FEA’s reply brief focuses on the following topics:

- Response to Public Counsel with respect to the classification and allocation of electric generation and transmission fixed costs;
- Response to PSE, Public Counsel, Commission Staff and Kroger regarding the allocation of electric base rate revenues, specifically with regard to the revenue allocation to Schedule 49; and
- Response to the Commission Staff with respect to PSE’s proposed Conjunctive Demand Service Option Pilot (“Pilot”).

CLASSIFICATION AND ALLOCATION OF GENERATION AND TRANSMISSION FIXED COSTS

Regarding the classification and allocation of generation and transmission fixed costs, the FEA urges the Commission to reject the Company's proposal to apply the peak credit method with updated assumptions. PSE's proposal would classify only 11% of fixed production and transmission costs as demand-related and 89% as energy-related.

Instead, it is the FEA's position that fixed production and transmission costs should be classified as 100% demand-related in this proceeding and allocated to the customer classes according to each class's demand during the system peak months of January, February, November and December 2018 (the "4 CP method"). During the aforementioned months, PSE's production and transmission resources are likely to be in use and operating at or close to their maximum capacities. The 4 CP method provides a much better reflection of cost causation for these fixed costs than classification or allocation methods that utilize energy usage to any significant degree.

However, if the Commission believes that it is appropriate to use energy usage (as measured by average demand) to classify and to allocate a portion of fixed production and transmission costs in this proceeding, a more appropriate and reasonable approach would be to rely on the "average and excess demand" method.^{1/} Specifically, the FEA recommends applying the average and excess 4 non-coincident peak demand ("A&E 4 NCP") method to allocate production and transmission plant costs to the customer classes using factors that combine the classes' average demands and non-coincident peak demands.

^{1/} See NARUC Manual at 49-52.

In its initial post-hearing brief, Public Counsel asserts that the Probability of Dispatch (“POD”) and the Base-Intermediate-Peak (“BIP”) cost allocation methods produce reasonable class cost allocation results for generation and transmission fixed costs.^{2/}

Public Counsel’s contention that the POD and BIP methods are the preferred cost allocation methodologies for fixed generation and transmission costs is without merit and is inconsistent with sound principles of cost causation. As FEA witness Ali Al-Jabir discussed in his cross-answering testimony, the coincident peak (“CP”) method is the allocation method for these costs that is most consistent with cost causation. This is because the CP method most accurately reflects the central cost driver for generation investment, which is the system peak demand. Mr. Al-Jabir noted it is the Company’s system peak demands, which occur during the winter months, that drive the need for additional generation and transmission capacity. Demands during moderate-load times, whatever time of day or month of year, do not cause new generating capacity to be built because there is excess capacity on the system during those times. Moreover, generation and transmission capital costs are fixed, sunk costs that do not vary with the amount of energy consumed by customers. Economic principles dictate that such fixed, sunk costs should be allocated on a demand basis.

Mr. Al-Jabir also described why the POD and BIP allocation methods favored by Public Counsel contradict cost causation principles. First, these allocation methods are based on the faulty premise that load duration and the economic trade-off between capacity and energy costs are the driving forces behind generation investment decisions. This argument misrepresents the utility planning process. In reality, the most important consideration in the generation planning

^{2/} Initial Post-Hearing Brief of Public Counsel at pages 26-27.

process is the need to preserve system reliability by ensuring that there is sufficient generation capacity to meet the utility's system peak demand requirements, plus a reasonable reserve margin.

Public Counsel's arguments in favor of the BIP and POD methods also ignore the fact that there is no clear cost-causation relationship between the duration of customer loads and generation resource planning. Utilities identify a need for new generation resources when generating capacity is needed to meet peak day demands and capacity reserve requirements. These reserve margin requirements are tied to the utility's highest peak demands in the year. The generation resource ultimately selected would be the lowest-cost resource available to meet that need for additional peak day capacity. Therefore, the economics of the specific resource investment decision become a factor only after the need for additional capacity to reliably meet system peak requirements is established.

Finally, Mr. Al-Jabir testified that the POD and BIP methods are inappropriate because they oversimplify the utility generation planning process. Important factors such as fuel costs, technological innovations and environmental requirements can change significantly, distorting the dispatch order of a utility's generating resources over time. Changes in these factors can alter the frequency with which generating units are dispatched and can also impact the designation of units as Base or Intermediate. Moreover, the dispatch order of generating units can be distorted by the addition of new plants that produce a different generation mix.

The POD and BIP methods ignore these significant factors that can alter the dispatch arrangement of a utility's generation units and that can impact the designation of Base, Intermediate or Peak resources on a utility's system. Therefore, these allocation methods do not

properly reflect the dynamic nature and the complexities of the utility system planning or dispatch processes.^{3/}

For the reasons set forth above, the FEA urges the Commission to reject Public Counsel's arguments in favor of the POD and BIP methods for the classification and allocation of fixed generation and transmission investment. Instead, PSE's production and transmission fixed costs should be classified as entirely demand-related and these costs should be allocated to the customer classes exclusively based on the 4 CP method. If the Commission nevertheless believes that it is appropriate to use energy usage (as measured by average demand) to classify and to allocate a portion of fixed production and transmission costs in this proceeding, a reasonable approach would be to apply the A&E 4 NCP method to allocate these costs.

ELECTRIC REVENUE ALLOCATION

With respect to electric revenue allocation, the FEA's position is that the Commission should reject the electric revenue allocation proposals of PSE, the Commission Staff, Public Counsel and Kroger because they do not show sufficient movement toward cost-based rates or because they move further away from cost-based rates in the case of Public Counsel's proposal. These revenue allocation proposals should also be rejected because they excessively subsidize residential customers. Finally, these revenue allocation proposals are objectionable because they would impose rate increases on customer classes that should receive a rate reduction if cost-based rates were applied.

^{3/} Docket Nos. UE-190529, UG-190530, UE-190274 and UG-190275, Cross-Answering Testimony of Ali Al-Jabir on behalf of the FEA, January 15, 2020, pages 5-7.

Instead, the FEA has proposed an electric revenue allocation that would significantly reduce cross subsidies among the rate classes and create greater movement towards cost-based rates relative to the proposals of the other parties to this proceeding. Specifically, the FEA recommends that no customer class receive an electric rate increase in this proceeding if it would be entitled to a rate reduction under cost-based rates. This means that Schedules 24, 25, 26, 31 and 46/49 should be maintained at their present rates and should receive no rate increase in this proceeding. Consistent with the Company's electric revenue allocation proposal, the FEA recommends that the revenue deficiency for the Retail Wheeling, Special Contract and Firm Resale classes be directly assigned to the applicable rate schedules.

In its initial post-hearing brief, PSE argues that its proposed electric rate spread is the most balanced approach of all the electric revenue allocation proposals that were submitted in this proceeding.^{4/} PSE's electric revenue allocation proposal is based on the application of certain criteria that guide its proposed allocation of electric revenues to the customer classes. Specifically, PSE proposes to apply 100% of the adjusted system average rate increase to retail customer classes that are within 5% of full revenue parity. Rate classes that are more than 5% but less than 10% above full parity would receive a rate increase that is 75% of the adjusted average increase. Rate classes that are below full parity and that fall within a parity ratio bandwidth of 0.89 to 0.95 would receive 125% of the adjusted system average increase. Rate classes that are below full parity and have a parity ratio of less than 0.89 would receive 150% of the adjusted average increase. The adjusted average rate increase calculated by the Company accounts for the effect of above-average and below-average increases to certain classes. Under the Company's proposal, the revenue

^{4/} Initial Post-Hearing Brief of PSE at page 56.

deficiency for the Retail Wheeling, Special Contract and Firm Resale classes is directly assigned to the applicable rate schedules.^{5/}

The Commission Staff asserts that the Commission should accept its proposed electric rate spread because it most appropriately balances the revenue allocation factors used by the Commission. The Commission Staff contends that revenue allocation should be approached by establishing parity ranges that can be used to evaluate the parity ratios of the customer classes under the Company's class cost of service study results. Under the Commission Staff's paradigm, customer classes that fall within $\pm 5\%$ of parity are deemed to be within the error range. Classes that fall within $\pm 10\%$ of parity are considered to be within what the Commission Staff calls a "range of reasonableness." Classes with parity ratios that are $\pm 20\%$ of parity or higher fall into a range of what the Commission Staff considers unreasonable ($\pm 20\%$), excessive ($\pm 30\%$) or grossly excessive ($\pm 40\%$) cross-class subsidization.^{6/}

Based on these parity ranges, the Commission Staff proposes an electric revenue spread that would allocate 150% of the adjusted system average rate increase to Schedules 35 and 43. The Lighting class would receive 125% of the system average increase, while the Staff would allocate 100% of the adjusted system average increase to Schedule 7 (Residential), Schedule 24 and Schedule 31. Finally, Schedules 25, 26 and 46/49 would receive 75% of the adjusted system average increase.^{7/}

By contrast, Public Counsel argues that the Commission should allocate an equal percentage rate increase to almost all of the electric customer classes, including the High Voltage

^{5/} Docket Nos. UE-190529, UG-190530, UE-190274 and UG-190275, PSE's Response to FEA Data Request No. 18.

^{6/} Docket Nos. UE-190529, UG-190530, UE-190274 and UG-190275, Response Testimony of Jason L Ball on behalf of the Commission Staff, November 22, 2019, pages 14-17.

^{7/} Initial Post-Hearing Brief of the Commission Staff at pages 50-51.

class. The exceptions to Public Counsel's general electric revenue allocation approach are the Retail Choice/Retail Wheeling, Special Contract and Firm Resale classes, which would receive a directly assigned revenue increase as proposed by the Company.^{8/}

Kroger recommends that any rate schedule that is at 106% of parity under PSE's class cost of service study should receive a rate increase that is 50% of the adjusted system average percentage base rate increase, rather than the 75% of the adjusted system average percentage increase that the Company recommends for such rate schedules. Under Kroger's proposal, the High Voltage class would receive a base rate increase of 4.10% (including PSE's attrition adjustment).^{9/}

The Commission should reject the electric revenue allocation proposals of PSE, the Commission Staff, Public Counsel and Kroger because they do not exhibit sufficient movement towards cost-based rates, particularly with regard to the High Voltage class (Schedules 46 and 49). As Mr. Al-Jabir demonstrated in his cross-answering testimony, the High Voltage class is above cost of service under the Company's cost of service study in this proceeding and provides a significant cost subsidy to other customer classes under present rates. Therefore, the High Voltage class should receive a base rate reduction to bring its base rates completely in line with cost of service. Mr. Al-Jabir also explained that the revenue allocation proposals of PSE, the Commission Staff, Public Counsel and Kroger would all impose base rate increases on the High Voltage class and would therefore fail to adequately address the cross-subsidies embedded in PSE's base rates.

The electric revenue allocation proposals put forth by both PSE and the Commission Staff would increase the base rates of the High Voltage class by 75% of the system average percentage

^{8/} Initial Post-Hearing Brief of Public Counsel at pages 27-28.

^{9/} Initial Post-Hearing Brief of Kroger at page 6.

increase. Mr. Al-Jabir's cross-answering testimony demonstrated that the electric revenue allocation proposals of PSE and Commission Staff are flawed because they require the High Voltage class to bear a significant share of the base rate increase in this proceeding, despite the fact that a base rate reduction is justified for this class to bring it to cost-based rates under the Company's cost of service study.

Mr. Al-Jabir further testified that Public Counsel's proposal to allocate a base rate increase to the High Voltage class that is equivalent to the system average percentage increase would impose a significantly larger base rate increase on the High Voltage class relative to PSE's proposed base rate increase of 75% of the adjusted system average increase. Therefore, Public Counsel's proposal is a step in the wrong direction because it would exacerbate the misalignment between costs and rates for the High Voltage class by requiring the High Voltage class to pay an even larger subsidy to other classes relative to PSE's proposal. This result is inconsistent with the goal of maximizing the movement to cost-based rates.

In addition, Mr. Al-Jabir explained that Kroger's proposal to reduce the magnitude of the cost subsidy imposed on the High Voltage class by moderating the base rate increase for this class to 50% of the adjusted system average base rate increase results in inadequate movement toward cost-based rates. This is the case because Kroger's proposal would impose a sizeable base rate increase on the High Voltage class, when a base rate reduction would be appropriate to achieve full movement to cost-based rates for this class under the Company's class cost of service study.

In its initial post-hearing brief, the Commission Staff claims that the FEA's proposed electric revenue allocation violates principles of equity and perceptions of fairness.^{10/} This argument is without merit. As Mr. Al-Jabir discussed in his cross-answering testimony, it is

^{10/} Initial Post-Hearing Brief of the Commission Staff at page 51.

inappropriate to impose a base rate increase on the High Voltage class simply because the overall PSE system is experiencing a rate increase. Mr. Al-Jabir explained that fairness and equity in the revenue allocation process should be measured by the degree to which the rates of a customer class accurately reflect the costs that the class causes the utility system to incur. If the goal is to ensure that rates are fair and equitable, then the Commission should adopt a revenue allocation that maximizes movement toward cost-based rates for each customer class. When the rates for any customer class are not based on the cost of service, some customers on the utility's system subsidize the cost to serve other customers. This result is inherently inequitable.

Therefore, the appropriate analytical approach to measure equity in rate setting involves a class-specific comparison of rates relative to the class cost of service. The fact that the utility is proposing an overall system average increase in its electric rates is irrelevant to this analysis. Moreover, this fact should not drive the allocation of the overall rate increase to the classes.^{11/}

Furthermore, Public Counsel's reliance on Commission precedent to support its electric revenue allocation proposal is misplaced. In its initial post-hearing brief, Public Counsel conceded that its primary rationale for allocating an equal percentage rate increase to the majority of PSE's electric rate classes was based on a flawed understanding of the Commission's precedent on this issue. Specifically, Public Counsel's witness on this topic, Mr. Glenn Watkins, incorrectly argued that the Commission's general practice has been to allocate the system average percentage rate increase to rate classes with parity ratios that are within plus or minus 10% of unity. Relying on this misunderstanding of the Commission's policy, Mr. Watkins justified his recommendation to allocate the system average percentage increase to the High Voltage class by asserting that the

^{11/} Docket Nos. UE-190529, UG-190530, UE-190274 and UG-190275, Cross-Answering Testimony of Ali Al-Jabir on behalf of the FEA, January 15, 2020, pages 9-15.

High Voltage's class's parity ratio of 106% under the Company's electric class cost of service study falls within this plus or minus 10% range.^{12/}

However, in its initial post-hearing brief, Public Counsel conceded that its characterization of the Commission's general practice with respect to class revenue allocation was in error. Specifically, Public Counsel acknowledged that the Commission's preferred range of accuracy for class parity ratios as established in Docket No. UE-152253 is actually a much narrower range of plus or minus 5% of unity.^{13/} Applying this plus or minus 5% standard to the electric class parity ratios in this case, it is apparent that the parity ratio of 106% for the High Voltage class under the Company's class cost of service study falls outside of the plus or minus 5% standard of deviation that is reflected in Commission precedent. Therefore, there is no basis in Commission precedent for Public Counsel's proposal to allocate the system average percentage increase to the High Voltage class in this proceeding.

For the foregoing reasons, the FEA urges the Commission to reject the electric revenue allocation proposals of PSE, the Commission Staff, Public Counsel and Kroger. These proposals are flawed because they either exacerbate or fail to adequately remedy the misalignment between costs and rates for the High Voltage class. Instead, the Commission should adopt the FEA's proposed electric revenue allocation because it would ensure that no customer class receives a base rate increase if it would be entitled to a rate reduction under cost-based rates. The FEA's recommendation would avoid the inequity of imposing a base rate increase on the High Voltage class as recommended by PSE, the Commission Staff, Public Counsel and Kroger when this class is in fact entitled to a base rate reduction to fully align its base rates with its cost of service.

^{12/} Docket Nos. UE-190529, UG-190530, UE-190274 and UG-190275, Response Testimony of Glenn A. Watkins on behalf of Public Counsel, November 22, 2019, pages 39-40.

^{13/} Initial Post-Hearing Brief of Public Counsel, page 28, footnote 127.

CONJUNCTIVE DEMAND SERVICE OPTION PILOT

The FEA urges the Commission to approve PSE's proposed Conjunctive Demand Service Option Pilot. The proposed Pilot should be approved because it would give customers with multiple locations across PSE's service territory an opportunity to manage their power costs more effectively. At the same time, the Pilot would benefit all customers on the Company's system by providing Pilot participants with more efficient, cost-based price signals to control their maximum simultaneous demands in a manner that would help to reduce incremental generation and transmission investment on the Company's system. After PSE has gained experience with conjunctive billing through the Pilot, the FEA recommends that the Company expand the scope of the conjunctive billing program to other rate schedules, such as Schedule 49, that contain customers with multiple electricity accounts or locations.

In its initial post-hearing brief, the Commission Staff contended that the Commission should require the Company to refile the Pilot to incorporate any guidance that the Commission provides in its final order in this docket.^{14/} The Commission Staff recommended several pricing pilot program design and evaluation elements in this proceeding, many of which it would presumably like the Commission to incorporate into the guidance that it provides to PSE. Specifically, the Commission Staff asserted that, prior to Pilot approval, PSE must provide additional clarity surrounding the Pilot with respect to matters such as the Pilot's goals, target audience, customer outreach, the measurement of benefits, program evaluation, practicality and relationship to cost causation.^{15/}

^{14/} Initial Brief of the Commission Staff at page 68.

^{15/} Docket Nos. UE-190529, UG-190530, UE-190274 and UG-190275, Response Testimony of Jason L. Ball on behalf of the Commission Staff, November 22, 2019, pages 59-61.

As. Mr. Al-Jabir explained in his cross-answering testimony, the concerns raised by the Commission Staff do not justify delaying approval and implementation of the Pilot. Indeed, the Commission Staff acknowledged that some of its proposed guidelines may not even be applicable to PSE's proposed Pilot.^{16/}

By definition, pilot programs are experimental in nature and are used to test customer interest in and responsiveness to a particular pricing structure. Therefore, the process of implementing the Pilot will allow both PSE and the Commission to assess on an ex-post basis the interest of specific customers in conjunctive billing and their ability to respond to the pricing structure in a manner that benefits both the customer and the utility system as a whole. In the context of implementing a pricing pilot, it is not necessary to define the target audience and the customer outreach strategy at the level of detail suggested by the Commission Staff prior to program implementation, particularly for larger customers with multiple locations who are generally more sophisticated users of electricity.

Mr. Al-Jabir also demonstrated that the Company made a strong case for the Pilot and its relationship to cost causation in its application and supporting testimony in this proceeding. PSE's testimony sets forth the goals of the Pilot, the structure of the program and the connection between conjunctive billing and cost causation on PSE's system. The Company specifically provided evidence through the direct testimony of Mr. Jon Piliaris showing that conjunctive billing is more consistent with the manner in which it conducts its generation and transmission planning.^{17/} Based on this evidence, there is no need to delay implementation of the Pilot or to require PSE to provide additional support for Pilot implementation as proposed by the Commission Staff.

^{16/} Initial Brief of the Commission Staff at page 68.

^{17/} Docket Nos. UE-190529, UG-190530, UE-190274 and UG-190275, Prefiled Direct Testimony of Jon A. Piliaris on behalf of PSE, June 20, 2019, pages 31-32.

Moreover, Mr. Al-Jabir testified that the Commission Staff's concerns regarding the measurement of Pilot benefits can be addressed in the Company's pilot program performance report to the Commission. As part of this performance report, the Company can provide an ex-post analysis of program benefits. This analysis could include metrics that measure the extent of customer participation in the Pilot, the mix of pilot program participants, the degree to which pilot program participants were able to reduce their conjunctive demands relative to the status quo billing method, and any other program results that the Commission finds useful to assess the benefits of the Pilot. Based on this information, the Commission can make an informed assessment as to whether the Pilot results merit expanding conjunctive billing to a wider set of PSE's customers.^{18/}

For these reasons, the Commission should approve PSE's request to implement the Pilot in this proceeding without additional delay. The record in this docket provides solid support for the Pilot and its relationship to cost causation on the Company's system. Moreover, the Pilot's benefits can be adequately measured through an ex-post analysis that PSE can provide to the Commission in its pilot program performance report. Therefore, there is no justification to delay the implementation of the Pilot or to require the Company to refile the Pilot to address the pricing pilot guidelines proposed by the Commission Staff.

^{18/} Docket Nos. UE-190529, UG-190530, UE-190274 and UG-190275, Cross-Answering Testimony of Ali Al-Jabir on behalf of the FEA, January 15, 2020, pages 17-19.

CONCLUSION

The FEA respectfully requests that the Commission issue a final order in this proceeding that is consistent with the positions set forth in its testimony, initial post-hearing brief, and reply brief. The FEA also requests all other relief at law or in equity to which it may be entitled.

Respectfully submitted,

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