

**BEFORE THE WASHINGTON UTILITIES AND TRANSPORTATION COMMISSION**

**In the Matter of the Petition of**

**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**

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**WASHINGTON UTILITIES AND  
TRANSPORTATION COMMISSION,**

**Complainant,**

**v.**

**PUGET SOUND ENERGY, INC.,**

**Respondent.**

**DOCKETS UE-121697 and  
UG-121705 (*consolidated*)**

**DOCKETS UE-130137  
and UG-130138 (*consolidated*)**

**POST-HEARING BRIEF OF COMMISSION STAFF**

**May 30, 2013**

**ROBERT W. FERGUSON  
Attorney General**

**GREGORY J. TRAUTMAN  
Assistant Attorney General  
Office of the Attorney General  
Utilities & Transportation Division**

**1400 S Evergreen Park Drive S.W.  
P.O. Box 40128  
Olympia, WA 98504-0128  
(360) 664-1187**

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## I. INTRODUCTION

1           On March 22, 2013, Puget Sound Energy, Inc. (“PSE”), Commission Staff (“Staff”), and the Northwest Energy Coalition (“NWECC”) entered into a Multiparty Settlement Agreement intended to compromise and settle all issues concerning: (1) the Joint Petition for Decoupling filed in Dockets UE-121697 and UG-121705; (2) PSE’s Expedited Rate Filing in Dockets UE-130137 and UG-130138, and; (3) PSE’s Petition for Reconsideration and Motion to Reopen the Record, filed in response to the Commission’s Order 03 in Docket UE-121373, pertaining to the Centralia Coal PPA. On May 7, 2013, The Energy Project joined the settlement, and on May 8, 2013, the Northwest Industrial Gas Users (“NWIGU”) also joined the settlement.

2           Staff believes that the Multiparty Settlement Agreement resolves all of the issues in these dockets in a manner that results in fair and reasonable rates, furthers the Commission’s policy directives, and is consistent with the public interest. The Commission should, therefore, approve this settlement.

## II. ARGUMENT

**A. The Commission should approve the Multiparty Settlement Agreement entered into by PSE, Commission Staff, NWECC, NWIGU, and The Energy Project.**

**1. Standard for Approval of the Multiparty Settlement Stipulation**

3           The Multiparty Settlement Agreement presented to the Commission for approval was entered into pursuant to WAC 480-07-730(3), by five of the parties to these proceedings representing a broad and diverse range of interests: PSE, Staff, NWECC, NWIGU, and The Energy Project. The Commission reviews settlement agreements under WAC 480-07-740 and WAC 480-07-750. The Commission must determine “whether the proposed settlement meets all pertinent legal and policy standards.” The Commission may approve a settlement

“when doing so is lawful, when the settlement terms are supported by an appropriate record, and when the result is consistent with the public interest in light of all the information available to the commission.”<sup>1</sup> This standard involves a three-part inquiry:

(1) We ask whether any aspect of the proposal is contrary to law; (2) We ask whether any aspect of the proposal offends public policy; and (3) We ask if the evidence supports the proposed elements of the Settlement Agreement as a reasonable resolution of the issue(s) at hand.<sup>2</sup>

The Commission has noted that settlements “are by nature compromises of more extreme positions that are supported by evidence and advocacy.” It also has observed that “ratemaking is not an exact science.”<sup>3</sup> Accordingly, when examining a settlement, “close scrutiny of individual adjustments is not required” so long as “the overall result in terms of revenue requirement is reasonable and well supported by the evidence.”<sup>4</sup>

4

Staff recommends that the Commission approve the Multiparty Settlement Agreement because it is consistent with the law and the public interest, and is supported by substantial evidence in the records developed in each of the five dockets covered by the settlement. In particular, the Agreement is supported by the written prefiled testimony and exhibits of the settling parties, as well as the oral testimony of the settling parties at the May 16, 2013, evidentiary hearing, provided in response to both the panel inquiry and to cross-examination by the non-settling parties.

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<sup>1</sup> WAC 480-07-750(1).

<sup>2</sup> *Washington Util. and Transp. Comm'n v. Cascade Natural Gas Corp.*, Docket UG-060256, Order 05, at 8, ¶ 23 (January 12, 2007).

<sup>3</sup> *Id.*, at ¶ 24.

<sup>4</sup> *Id.*; *Washington Util. and Transp. Comm'n v. PacifiCorp d/b/a Pacific Power & Light Co.*, Docket UE-032065, Order 06, at 26-27, ¶¶ 61-62 (October 27, 2004).

2. **The Commission has the authority to approve the Multiparty Settlement Agreement by approving the Agreement as an integrated whole. In the alternative, the Commission may effectively achieve the same result by approving all of the provisions of the Agreement by separate Orders entered in each of the five dockets (three matters) affected by the Agreement.**

5 RCW 34.05.476(1) states that the Commission shall maintain an official record of each adjudicative proceeding. RCW 34.05.476(3) then states that, with limited exceptions not applicable here, the agency record constitutes the exclusive basis for agency action in adjudicative proceedings. The Commission has inquired, by notice issued on May 14, 2013, and by subsequent questioning at the hearing on May 16, 2013, whether approval of the Multiparty Settlement Agreement would run afoul of the statutory requirement that agency action be based on the agency record. Staff believes there is no statutory bar to the Commission approving the parties' Agreement as an integrated whole, based on the extensive agency records developed in each of the five dockets implicated by the Agreement. However, Staff also is amenable to the Commission's alternative suggestion that each of the elements of the Agreement be approved by separate Commission Orders in the ERF, Decoupling, and TransAlta dockets.

6 The Commission has faced this same situation before, when it approved a multiparty settlement in three separate, unconsolidated dockets: *In the Matter of the Application of GTE Corporation and Bell Atlantic Corporation for an Order Disclaiming Jurisdiction or, in the Alternative, Approving the GTE Corporation-Bell Atlantic Merger*, Docket UT-981367; *WUTC v. GTE Northwest Incorporated (access charge complaint)*, Docket UT-990672; and *Informal Staff Investigation of GTE Northwest's Earnings and Revenue*, Docket UT-991164. Those dockets involved a merger application, an access charge complaint, and an earnings review. Thus, while they concerned the same company (GTE)

and the same ratepayers, they were otherwise related only in that the resolution of those dockets would directly or indirectly affect the rates paid by ratepayers, and the revenues earned by GTE.

7           Nevertheless, the Commission approved an omnibus settlement agreement by Order that resolved the “three separate dockets.”<sup>5</sup> It noted that it was doing so based on the evidentiary records developed in each of the proceedings.<sup>6</sup> The Commission found, based on those evidentiary records, that the omnibus settlement resolved all of the issues presented consistent with the public interest. That is what the settling parties are requesting be done here.

8           The Commission noted at the May 16, 2013, hearing that it has entered Order 03, designated as a Final Order, in the TransAlta proceeding.<sup>7</sup> While that is true, PSE has also filed a motion for reconsideration of that Order and a motion to reopen the proceeding in that docket. The Commission plainly has the power to alter or amend the conditions in Order 03, if it deems that doing so would be consistent with the public interest. Staff sees no reason why the Commission could not also reconsider Order 03, in conjunction with the Multiparty Settlement Agreement that is now before it (which also modifies and limits the relief originally requested in PSE’s motion), and determine whether the totality of the relief requested in the ERF, Decoupling, and TransAlta dockets by the settling parties results in just, fair, and reasonable rates, and an overall result that is consistent with the public interest.

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<sup>5</sup> *In the Matter of Application of GTE, et al., supra*, Fourth Supplemental Order (December 1999).

<sup>6</sup> *Id.*, at 23-24.

<sup>7</sup> *In the Matter of the Petition of PSE for Approval of a Power Purchase Agreement for Acquisition of Coal Transition Power, as Defined in RCW 80.80.010, and the Recovery of Related Acquisition Costs*, Docket UE-121373, Order 03, Final Order Granting Petition, Subject to Conditions (January 9, 2013).

This would not, in Staff's view, require the Commission to say that it was somehow "wrong" when it originally entered Order 03. It would merely entail the Commission opining that the result obtained by accepting certain modifications to that Order, together with the other relief requested in the entire Multiparty Settlement Agreement, leads to an outcome that is consistent overall with the public interest.

9           However, Staff is aware, as both Judge Moss and Commissioner Goltz indicated at the May 16, 2013, hearing, that the Commission may be more comfortable—assuming that it finds the elements of the Multiparty Settlement Agreement to be substantively acceptable—with approving the elements of the Agreement by separate Orders in the ERF, Decoupling, and TransAlta dockets.<sup>8</sup> Although Staff filed the testimony of Mr. Schooley in support of the settlement, taken as an integrated whole, Staff does not object to the Commission approving each of the settlement's elements separately. The Commission clearly has the authority to determine, based on the administrative records before it, that the elements comprising each of the three portions of the settlement agreement—ERF, Decoupling, and TransAlta—are all lawful and consistent with the public interest, when considered separately. Staff also concurs that the Commission's taking this approach would provide it with additional assurance that the APA's procedural requirements have been met, and its Orders wholly defensible on appeal.<sup>9</sup>

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<sup>8</sup> See Tr., at 111-13, 122-23.

<sup>9</sup> *Id.*, at 123.



3. **The ERF tariff filings agreed to in the Multiparty Settlement Agreement are consistent with the Commission’s directive in PSE’s 2012 general rate case, appropriately address regulatory lag, and result in a small, one-time increase in electric rates—and a *decrease* to natural gas rates—that is fair, just, and reasonable. The objections raised by Public Counsel and ICNU to the ERF filings are all without merit.**

10 In the Multiparty Settlement Agreement, the settling parties have agreed to support the ERF tariff filings made by PSE in Dockets UE-13-0137 and UG-130138 on February 1, 2013. These tariffs would effect a one-time, 1.6 percent increase to PSE’s electric rates, and a 0.1 percent *decrease* to PSE’s natural gas rates.<sup>10</sup> PSE also submitted a property tax tracker as directed by the Commission in its Final Order in PSE’s 2012 general rate case.<sup>11</sup> The Settling Parties have agreed to support the property tax tariff as filed, together with the ERF.

11 In supporting the ERF proposed by PSE in this case, the Multiparty Settlement Agreement is carrying out precisely the policy that the Commission recently encouraged in PSE’s 2012 general rate case. The Commission there stated that it “recognizes the dynamic nature of the financial and economic tides that affect utilities, including PSE, and its customers,” and that it “strives to maintain reasonable and appropriate flexibility in its regulatory process to address this ebb and flow.”<sup>12</sup> The Commission continued:

We appreciate Staff’s willingness to bring forward the outline of a proposed process mechanism to help address the particular problems associated with PSE’s current position in a cycle of capital investment that places unusually high demands on utilities from time to time as they face the need to maintain and replace significant amounts of aging infrastructure.

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<sup>10</sup> Multiparty Settlement Agreement, at 5, ¶ 8.

<sup>11</sup> *WUTC v. Puget Sound Energy, Inc.*, Dockets UE-111048 and UG-111049, Order 08, at ¶ 143.

<sup>12</sup> *Id.*, at ¶ 506.

... If PSE accepts Staff's invitation 'to meet with PSE to confirm mutual expectations' for a filing along the lines Staff suggests, or the Company on its own initiative makes such a filing, we certainly will give it fair consideration. Alternatively, Staff and PSE may enter into a broader discussion with other interested participants in the regulatory process and bring forward for consideration specific proposals that may satisfy a range of both common and diverse interests. *In this connection, the Commission would be particularly interested in proposals that might break the current pattern of almost continuous rate cases.*<sup>13</sup>

(Emphasis added.)

12           The "proposed process mechanism" of which the Commission approvingly spoke of above was, in fact, the filing of an expedited rate filing, or ERF. Although a specific proposal was not put before the Commission in 2012, then Staff witness Kenneth Elgin proposed the general outline of an ERF, as part of "Staff's Recommendation for Regulatory Lag." The ERF would essentially be "an update to the relationships between rate base, revenues, and expenses." The Company could not request a change to the rate of return, except to update debt costs for known changes. The filing would contain restating adjustments only, "to 'clean' the books in order to allow proper ratemaking." Finally, there would be no rate spread or rate design changes.<sup>14</sup>

13           While it is true that Mr. Elgin's general outline envisioned the filing of an ERF "immediately following the determination of a fully contested rate case," it also would permit the Company to use the ERF process for two consecutive years.<sup>15</sup> Here, while the ERF was not filed immediately after the 2012 general rate case, the Multiparty Settlement Agreement permits only one ERF to be filed prior to PSE's filing of another general rate

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<sup>13</sup> *Id.*, at ¶¶ 506-07.

<sup>14</sup> *WUTC v. PSE*, Dockets UE-111048 and UG-111049, Elgin, Exh. No. KLE-1T, at 81.

<sup>15</sup> *Id.*, at 81-82.

case, which must occur between April 2015 and April 2016. It is thus consistent with the general approach proposed by Staff in PSE's 2012 general rate case.<sup>16</sup>

14 Furthermore, as PSE witness Ms. Barnard noted in her testimony, PSE discussed several alternatives with Staff and other stakeholders over the eight months prior to February 1, 2013, before finalizing the ERF tariffs it filed with the Commission.<sup>17</sup> As Mr. Schooley testified, the resulting tariffs comport with the "mutual expectations" of Staff and the Company, as the Commission envisioned in its 2012 PSE general rate case Order.<sup>18</sup> Staff emphasizes again that the procedure followed was one of the options specifically authorized by the Commission, which was for "PSE [to] accep[t] Staff's invitation 'to meet with PSE to confirm mutual expectations' for a filing along the lines Staff suggests."<sup>19</sup>

15 PSE's electric ERF is based on a test period for the 12 months ending June 30, 2012. As Mr. Schooley noted, the ERF was filed following the rules for Commission-basis reports (CBRs), where adjustments to the per-books results may include only the necessary adjustments as accepted by the Commission in the utility's most recent general rate case; adjustments for any material out-of-period, non-operating, nonrecurring, and extraordinary items; and adjustments to reflect operations under normal temperature and power supply

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<sup>16</sup>Commission Staff notes that it has objected to the offering of new opinion testimony by Mr. Elgin in these dockets, through Public Counsel's deposition of Mr. Elgin, since he is not a witness in these dockets. The Commission has concurred with this determination. Order 05, at ¶ 21 (April 16, 2013). However, Mr. Elgin's testimony in PSE's 2012 general rate case is the subject of judicial notice, pursuant to the request of Public Counsel, (Tr. at 185) and hence, may be cited by the parties in their briefs.

<sup>17</sup> Barnard, Exh. No. KJB-1T (ERF), at 4.

<sup>18</sup> Schooley, Exh. No. TES-1T, at 5-6; Dockets UE-111048 and UG-111049, Order 08, at ¶ 507.

<sup>19</sup> Order 08, at ¶ 507.

conditions. The intent of the ERF is to derive a baseline for the “delivery,” or non-production electric operations.<sup>20</sup>

16 PSE followed the 2011 CBR, but excluded certain adjustments. Power costs were not updated because they are excluded from non-production electric operations. Certain minor adjustments were excluded in the interests of expediency.<sup>21</sup> Public Counsel’s witness Mr. Dittmer raises this as a “concern,” though he concedes that “I have concluded, based on discovery that this omission probably does not have a material revenue impact[.]”<sup>22</sup> Indeed, it does not. In fact, Mr. Schooley noted that collectively, had these minor adjustments been made, they would have *increased* electric revenue requirements.<sup>23</sup> PSE’s natural gas ERF likewise followed the 2011 CBR in most respects. Staff reviewed the adjustments to the per books accounts for both the electric and natural gas ERF and found them to be proper and reasonable.<sup>24</sup>

17 Public Counsel and ICNU raised four points in opposition to the ERF, all of which Mr. Schooley persuasively countered in his rebuttal testimony. First, they contend that the rate of return is too high.<sup>25</sup> They each contend that the cost of capital and rate of return should be issues that are fully litigated in the context of an ERF. But to do this would completely defeat the very premise of an ERF. The reason for having an ERF receive

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<sup>20</sup> Schooley, Exh. No. TES-1T, at 8.

<sup>21</sup> *Id.*

<sup>22</sup> Dittmer, Exh. No. JRD-1T, at 16-17.

<sup>23</sup> Schooley, Exh. No. TES 1T, at 8-9 and n. 6. The omitted minor adjustments would collectively decrease natural gas revenue requirements by \$156, 777. *Id.*, at 10-11 and n. 9.

<sup>24</sup> The other major adjustment removes property taxes from both the electric and natural gas ERFs. However, property taxes are proposed to be recovered in a separate tariff, as noted above at p. 6 of this brief.

<sup>25</sup> Public Counsel and ICNU further contend that an additional reduction in the rate of return is necessary due to implementation of a decoupling mechanism. This issue is addressed later in this brief, at pp. 18-20.

expedited processing is to keep certain ratemaking variables constant—including namely, the rate of return. Staff’s outline for an ERF in the 2012 PSE general rate case recognized as much. Public Counsel and ICNU essentially would turn this into simply another drawn-out, ten-month PSE general rate case, which is exactly what the Commission has been saying it wants to avoid, year after year.

18           Moreover, the Commission determined that 7.8 percent was a fair and sufficient rate of return for PSE just last year.<sup>26</sup> And the Commission approved this same 7.8 percent rate of return for Avista as part of a settlement agreement just five months ago.<sup>27</sup> Given that the Avista settlement is less than five months old, Staff believes that this rate of return remains within the range of reasonableness. Certainly in this case, the Commission does not have before it sufficient or balanced presentations that would enable it to arrive at a rate of return other than 7.8 percent.<sup>28</sup>

19           Furthermore, as Mr. Schooley pointed out in both his direct and rebuttal testimony, PSE’s CBR rate of return results over the past several years show that the Company has actually been earning less than its authorized rate of return, at times by upwards of 250 basis points. In fact, PSE has not achieved its authorized rate of return for electric operations since 2006, and for natural gas operations since at least 2004. Mr. Schooley’s updated Exh. TES-3 shows that even with the rate increase instituted in 2012, PSE’s electric earnings were about 70 basis points less than, and its natural gas earnings were 30 basis points less than, the authorized rate of return granted in 2012. For these reasons, Staff does not believe

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<sup>26</sup> Dockets UE-111048 and UG-111049, Order 08 (May 7, 2012).

<sup>27</sup> *WUTC v. Avista*, Dockets UE-120436 and UG-120437, Order 09 (December 26, 2012).

<sup>28</sup> Schooley, Exh. TES-4T, at 3-4.

that PSE will fully achieve its authorized 7.8 percent rate of return. However, the ERF will improve PSE's opportunity to do this, to the extent that the Company manages its expenses. Staff thus considers the ERF (and the rate plan associated with the decoupling mechanism) a reasonable plan to encourage the Company to do this.<sup>29</sup> Public Counsel's and ICNU's call for a relitigation of the rate of return in conjunction with the ERF is misplaced.

20           The second issue raised in opposition to the ERF (this by Mr. Deen for ICNU) is the supposed use of a "hybrid" test year.<sup>30</sup> But, as Mr. Schooley notes, there is nothing unusual here. The gas and electric ERFs are both based on a test period for the twelve months ending June 30, 2012. It is a common practice to use test years ending on dates other than calendar-year-end, and the current PacifiCorp general rate case<sup>31</sup> also uses a test year ending June 30, 2012.<sup>32</sup> ICNU's objection is without merit.

21           The third issue raised in opposition to the ERF, by both Public Counsel and ICNU, is the use of end-of-period (EOP) rate base, rather than average of monthly averages (AMA) rate base. Mr. Deen for ICNU goes so far as to label the use of EOP rate base as "novel."<sup>33</sup> While Staff agrees that AMA is the usual method employed, the use of EOP in certain cases is not at all novel. The use of EOP rate base was accepted by the Commission in *WUTC v. Olympic Pipeline Company* in 2002, to address the effects of regulatory lag that Olympic

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<sup>29</sup> Schooley, Exh. TES-1T, at 12-13; Exh. TES-4T, at 4.

<sup>30</sup> Deen, Exh. MCD-1T, at 10.

<sup>31</sup> *WUTC v. PacifiCorp*, Docket UE-130043 (January 11, 2013).

<sup>32</sup> Schooley, Exh. TES-1T, at 6.

<sup>33</sup> Deen, Exh. MCD-1T, at 11.

had experienced since 1999.<sup>34</sup> EOP rate base was also approved in *WUTC v. Washington Natural Gas*<sup>35</sup> in 1981, a case that also references and cites with approval Commission cases from 1972-73 and 1973-74.

22 In fact, the Commission has expressly acknowledged and approved the use of EOP rate base in four distinct circumstances, at least two of which are present here. In *WUTC v. Washington Natural Gas*, the Commission stated:

Year-end rate base is an appropriate regulatory tool under one or more of the following conditions:

- (a) Abnormal growth in plant
- (b) Inflation and/or attrition
- (c) As a means to mitigate regulatory lag
- (d) Failure of utility to earn its authorized rate of return over a historical period.<sup>36</sup>

23 Factors (a) and (d) are present in this case. Regarding factor (a), the Company is faced with having to replace substantial amounts of old infrastructure, with cost impacts that are directly affected by regulatory lag. The Commission stated in Cause U-80-111 that this lag “has long been a concern of both the utilities and their regulators” that can have a “deleterious effect,” and that “as regulators we have the responsibility to mitigate that effect to the extent possible.”<sup>37</sup> More recently, in the 2012 PSE general rate case, the Commission reiterated that it was “open to considering” the “[u]se of plant accounts (rate base) measured

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<sup>34</sup> Docket TO-011472, Twentieth Supp. Order, at 44, ¶ 160 (September 27, 2002). *See also* Docket TO-011472, Twitchell, Exh. MLT-1T, at 43-46.

<sup>35</sup> Cause No. U-80-111, Third Supp. Order, at 5-7 (September 24, 1981).

<sup>36</sup> *Id.*, at 6.

<sup>37</sup> *Id.*

at the end, or subsequent to the end of the test-year rather than the test-year average.”<sup>38</sup>

Regarding factor (d), Mr. Schooley’s testimony and exhibits demonstrate in detail, as discussed above, that PSE has failed to earn its authorized rate of return over a prolonged historical period extending back seven to nine years. The use of EOP is thus a viable and appropriate way to mitigate regulatory lag and the historical under-earning of PSE.<sup>39</sup>

24           Finally, both Public Counsel and ICNU claim that the ERF—together with the rate plan that is included as part of the decoupling mechanism in the Multiparty Settlement Agreement—will lead to revenue increases for PSE amounting to hundreds of millions of dollars, from May 2013 through possibly February 2017. Mr. Deen for ICNU calculates the total figure as \$351 million;<sup>40</sup> Mr. Dittmer for Public Counsel calculates the total figure as \$465 million.<sup>41</sup> The point of reciting these total revenue figures is apparently to convey the impression that the ERF and rate plan will inevitably result in huge, and unreasonable, rate increases for individual ratepayers.

25           But just as tellingly, neither Mr. Deen nor Mr. Dittmer actually says this. Neither of them tells the reader what the average percentage increase in rates will be for the average ratepayer. And that is likely because, in fact, the rate increases contemplated by the settlement, taken as a whole, are eminently fair and reasonable.

26           As previously noted, the ERF would effect a one-time, 1.6 percent increase to PSE’s electric rates, and a 0.1 percent *decrease* to PSE’s natural gas rates. The rate plan, as

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<sup>38</sup> Dockets UE 111048 and UG-111049, Order 08, at ¶ 491.

<sup>39</sup> At the May 16, 2013, hearing, Public Counsel witness Mr. Dittmer agreed that the use of EOP rate base reduces regulatory lag. Tr., at 291.

<sup>40</sup> Deen, Exh. MCD-1T, at 2.

<sup>41</sup> Dittmer, Exh. JRD-1T, at 9.



explained in greater detail below, only applies to delivery revenues.<sup>42</sup> But even if one takes the total revenues generated by the ERF and rate plan together, and accepts Mr. Dittmer's figure of \$465 million over 46 months as correct for argument's sake, this constitutes only slightly more than four percent of PSE's total revenues from today's rates, which will exceed \$11.6 billion over that same time period. In other words, the total rate increase from both the ERF and the rate plan, under the most extreme scenario posed by Public Counsel, is slightly more than one percent per year. Mr. Schooley calculates it as 1.05% in his revised Exhibit TES-3, using Mr. Dittmer's numbers.<sup>43</sup>

27 In summary, the ERF proposal set forth in the Multiparty Settlement Agreement is supported by substantial evidence in the record, carries out the policy directives set forth in PSE's 2012 general rate case, appropriately addresses regulatory lag, and results in a one-time increase in electric rates and a decrease in natural gas rates that is fair, just, and reasonable.

**4. The rate plan and amended decoupling proposal in the Multiparty Settlement Agreement provide for full decoupling and small, limited, and reasonable revenue increases based on a reasonable K-factor. The amended decoupling proposal is consistent with the Commission's policy directives, as set forth in PSE's 2012 general rate case and the Commission's Decoupling Policy Statement, and should be approved.**

28 In Dockets UE-121697 and UG-121705, PSE has filed with the Commission an amended decoupling proposal and rate plan. This proposal is the culmination of months of

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<sup>42</sup> The ERF and rate plan, taken together, result in approximately a 3.3 percent increase in electric revenues in the first year, and approximately a 1.7 percent increase in natural gas revenues in the first year. In subsequent years, the increase is slightly more than one percent, as calculated by Public Counsel.

<sup>43</sup> This is consistent with the figures set forth in Public Counsel's press release of April 26, 2013, informing the public of the effect of the ERF and rate plan, which states that the settlement proposal will result in an initial 3.3 percent increase in electric rates [consistent with Mr. Schooley's testimony], "with additional annual increases of slightly more than one percent in subsequent years," and that natural gas customers would receive "an annual rate increase of approximately one percent per year."

<http://www.atg.wa.gov/pressrelease.aspx?id=31167>.

technical conferences, stakeholder workshops, and discussions with numerous parties concerning options for implementing decoupling. It is not a new issue. As Judge Moss stated at the March 22, 2013, prehearing conference, “[W]e’ve been kicking this decoupling thing around at the Commission for a long time. And all of you have participated to one degree or another in various aspects of that. More recently we’ve looked at it very thoroughly in both the [2012] Avista and the [2012] PSE general rate cases, and a lot of discussion.”<sup>44</sup> The current amended decoupling proposal follows a previous proposal that PSE filed in October 2012, which in turn was followed by technical conferences on the subject on November 6, 2012, and January 15, 2013. In short, the issue of decoupling has been examined and vetted by many parties, in addition to Staff.

29 In PSE’s 2012 general rate case, the Commission stated, “The Commission remains open to proposals for a full decoupling mechanism, even to one that may vary somewhat from what is described in our [Decoupling] Policy Statement.” The Commission further noted that the Policy Statement “was not intended to set forth immutable doctrine on this issue or to negatively imply that we would be receptive to nothing else.”<sup>45</sup>

30 Staff points this out because Public Counsel and ICNU object to PSE’s amended decoupling proposal largely because it does not conform to the Commission’s 2010 Decoupling Policy Statement<sup>46</sup> in every respect.<sup>47</sup> Mr. Deen for ICNU, in particular, takes

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<sup>44</sup> Tr., at 50-51; *See also* Order 04, Granting Late-Filed Petition to Intervene; Overruling Objection to Order 02, at ¶¶ 13-14 (Commission overruled Public Counsel’s objection to the procedural schedule).

<sup>45</sup> *WUTC v. PSE*, Dockets UE-111048 and UG-111049, Order 08, at 167 and n. 617.

<sup>46</sup> Docket U-100522, Investigation Into Energy Conservation Incentives, *Report and Policy Statement on Regulatory Mechanisms, Including Decoupling, To Encourage Utilities to Meet or Exceed Their Conservation Targets* (November 4, 2010) (“Decoupling Policy Statement”).

<sup>47</sup> Dittmer, Exh. JRD-1T, at 21, lines 1-2 (“PSE’s amended full decoupling proposal does not contain all elements that the Commission stated should be included in a full decoupling proposal” [citing the Decoupling

Staff witness Ms. Reynolds to task for supposedly “reversing her position” in her testimony in this case.<sup>48</sup> He asserts that she “defend[ed] the [Decoupling] Policy Statement” in testimony in the 2012 PSE general rate case, but is changing course now.<sup>49</sup> What Ms. Reynolds has actually done, as she points out at the very outset of her testimony, is reconcile the principles in the Decoupling Policy Statement (which is not “immutable doctrine”) with the Commission’s more recent pronouncements in Order 08 of PSE’s 2012 general rate case.<sup>50</sup> Mr. Deen evidently decided not to do so.

31 For example, the Commission in PSE’s 2012 general rate case made it quite clear that it supports the concept of an expedited rate filing—an ERF—which by its very nature is *not* a full general rate case, because it does not include, among other things, litigation regarding the Company’s rate of return.<sup>51</sup> The Commission has also indicated that a full decoupling mechanism could benefit both the Company and ratepayers, and has indicated its receptiveness to such a proposal. Staff is likewise receptive to this concept. Mr. Deen, on the other hand, has effectively put the Commission in a box. If decoupling can *only* be implemented as part of a general rate case, then the Commission’s endorsement of an ERF means that no decoupling can be approved at all, and the Commission is simply left with kicking decoupling down the road for even more years, without resolution. In Staff’s view, this is not the only choice, nor the best choice.

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Policy Statement]); Deen, Exh. MCD-1T, at 23-24 (stating that the Decoupling Policy Statement allows for decoupling only if filed as part of a general rate case).

<sup>48</sup> Deen, Exh. MCD-1T, at 29.

<sup>49</sup> *Id.*

<sup>50</sup> Reynolds, Exh. DJR-1T, at 3-5.

<sup>51</sup> The Commission reiterated its support for expedited rate proceedings, in a January 15, 2013, letter to Governor Gregoire, who also endorsed such proceedings. Exh. TES-2T.

Turning to the merits of the rate plan and the decoupling proposals themselves, Staff believes they are both eminently reasonable and amply supported by the record. The rate plan, implemented through a K-factor, is intended to give PSE minor revenue increases for a limited period of time. The K-factor is implemented as a fixed-percentage increase applied only to the revenues that support the non-generation portion of the business (delivery revenues).<sup>52</sup> From the ERF, the delivery revenues are divided by the number of customers to derive revenues per customer (RPC). The rate plan applies 3.0 percent increases per year to the electric delivery RPC, and 2.2 percent increases per year to the gas delivery RPC.<sup>53</sup> Staff is comfortable with the K-factor because it is limited to delivery revenues, addresses attrition, and will be completely reset in the next PSE general rate case, which must be filed between April 1, 2015, and April 1, 2016. This means it will be in place for only a limited period of time, which will serve to limit its possible impacts. There is also a three percent soft cap on rate increases compared to total revenue, which provides additional ratepayer protection by addressing both increases due to the underlying decoupling mechanism and those due to operation of the K-factor.<sup>54</sup>

The K-factor is roughly based on PSE's delivery plant and expense growth rates. However, it is substantially less than the indicated plant or growth rates of the past several years. The weighted average basis for the K-factor, using historical growth rates, would be 4.06 percent for electricity and 3.8 percent for gas. However, the K-factors being used in

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<sup>52</sup> Schooley, Exh. TES-4T, at 10.

<sup>53</sup> Schooley, Exh. TES-1T, at 4.

<sup>54</sup> Reynolds, Exh. DJR-1T, at 4.

the amended decoupling proposal are only 3.0 percent and 2.2 percent, which are about 25 to 40 percent less than the potential plant and expense growth rates.<sup>55</sup>

34 ICNU objects to the K-factor because it is not based on conservation achievement and allows revenues to grow with additional customers. As Mr. Schooley noted, however, the K-factor is not intended to be a measure of conservation success or impact.<sup>56</sup> It is intended to give PSE minor revenue increases for a limited period of time. Moreover, it is reasonable to apply the K-factor to the number of actual customers each month. There is no “found margin” attributable to customer growth. This would require either that each new customer be cheaper to serve than average, or each new customer consume more electricity or gas than average. Neither situation is likely, and neither is supported by the data.<sup>57</sup>

35 The K-factor and rate plan will result in an approximate 1.7 percent rate increase for ratepayers during the first year, with additional annual increases of approximately 1.0 percent in future years, until the Company files a general rate case, which must occur between April 1, 2015, and April 1, 2016. These are small, reasonable, and time-limited rate increases. Furthermore, as Mr. Schooley demonstrated, PSE has been earning less than its authorized rate of return for several years. The rate plan will improve PSE’s opportunity to earn this amount. However, as stated above, PSE will need to manage its expenses, and Staff believes it is highly unlikely that the rate plan increases will result in PSE earning greater than its authorized rate of return.<sup>58</sup>

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<sup>55</sup> Schooley, Exh. TES-1T, at 13-15.

<sup>56</sup> Schooley, Exh. TES-4T, at 10.

<sup>57</sup> *Id.* at 10-11.

<sup>58</sup> Schooley, Exh. TES-1T, at 12-13, 15.

36 Public Counsel and ICNU also oppose the amended decoupling proposal because it does not include a reduction to PSE's return on equity. ICNU proposes that PSE's return on equity be reduced at least 25 basis points<sup>59</sup> (in addition to a reduction in return on equity from 9.8 percent to 9.3 percent in the ERF proceeding)<sup>60</sup> while Public Counsel proposes an even greater reduction, from 9.8 percent to 9.0 percent.<sup>61</sup> Staff believes that imposing an immediate, arbitrary reduction to the return on equity or the rate of return is unwise and unjustified, and that the Commission should not require the Multiparty Settlement Agreement to be amended to reflect such reductions.

37 Staff is aware that the Commission, in its Decoupling Policy Statement, contemplated that full decoupling may reduce the Company's cost of capital:

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.<sup>62</sup>

The Commission added that a full decoupling mechanism should "evaluat[e] the impact of the proposal on risk to investors and its effect on the utility's ROE."<sup>63</sup>

38 The question is, how should this policy be implemented? Or more specifically, what should be the timing of implementing this policy? PSE has not filed a general rate case at this time; rather, PSE has filed an ERF (in which the rate of return should not be relitigated), together with a decoupling petition. Staff strongly believes that adjustments to return on

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<sup>59</sup> Gorman, Exh. MPG-1T, at 28.

<sup>60</sup> *Id.*, at 6.

<sup>61</sup> Hill, Exh. SGH-1T, at 5.

<sup>62</sup> Decoupling Policy Statement, at ¶ 27.

<sup>63</sup> *Id.*, at ¶ 28.

equity or to capital structure are only appropriate within a general rate case, where the Commission can look at all the offsetting factors.<sup>64</sup> PSE will be required to file a general rate case between April 1, 2015, and April 1, 2016, at which time the Commission will have an opportunity to do just that.

39           Moreover, Staff believes it far better for the Commission to wait until it has actual, empirical evidence on which to make a reasoned decision, rather than make a hasty, arbitrary choice to simply reduce the rate of return now based on an inadequate record and a mere supposition of whether, and how, decoupling might reduce a company's risk. Mr. Schooley explained:

*The claim that decoupling reduces risk for regulated utilities has theoretical appeal, but is at best hypothetical and unsupported by empirical evidence. Here we have the opportunity to test that hypothesis. This full decoupling program will compare the financial revenues determined by multiplying the number of customers by the delivery revenues per customer versus the cash collected through volumetric rates intended to generate the same level of dollars. The magnitude of the refunds and surcharges will be direct evidence of the volatility dampened by the decoupling program. Given that this program addresses only delivery costs it cannot be extrapolated to the full impact on the utility's rate of return. However, it will be a good measure of decoupling's impact on the one-half to one-third of the revenues represented by the delivery of gas or electricity. It is important to understand these impacts on real world operations before establishing an "adjustment" to rates of return.*<sup>65</sup>

(Emphasis added).

40           Mr. Schooley is precisely right. This is borne out by what numerous other utilities commissions nationwide, which have already addressed this very issue, have concluded. For in fact, the proposals of Public Counsel and ICNU to immediately and substantially reduce PSE's rate of return are far outside the mainstream. NWECA witness Mr. Cavanagh's

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<sup>64</sup> Reynolds, Exh. DJR-1T, at 8-9.

<sup>65</sup> Schooley, Exh. TES-4T, at 5.

Exhibit RCC-5 shows that out of 76 decisions, 60—nearly 80 percent—have resulted in *no* reduction to return on equity, and nine resulted in a reduction of only ten basis points. Of those nine decisions, four resulted from settlement agreements.<sup>66</sup> The overwhelming weight of evidence, thus, argues in favor of not making any return on equity or rate of return adjustment until the next general case, when empirical evidence on the effects of decoupling will be available and all factors can be considered.

41 Public Counsel and ICNU raise certain other objections to the amended decoupling proposal, but they, too, are either without merit or may be satisfactorily addressed. ICNU witness Mr. Deen states that the decoupling proposal will not remove barriers to acquiring all cost-effective conservation. Staff finds that assertion puzzling, because it appears to stem from considering the K-factor in the rate plan as a decoupling feature. In fact, the decoupling proposal clearly removes PSE's incentive to sell more kWh and therms, which is the proposal's intent.<sup>67</sup>

42 Mr. Deen also objects that the amended decoupling proposal does not directly capture additional off-system sales to be returned to customers. Ms. Reynolds and Mr. Schooley both address this point. In Staff's view, this issue is best addressed within a power cost only rate case and the power cost adjustment filings, or in a general rate case. This will sufficiently address any off-system sales concerns.<sup>68</sup>

43 Finally, Public Counsel witness Mr. Dittmer states that a full decoupling proposal would be reasonable with an earnings test. As Mr. Schooley notes, the amended decoupling

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<sup>66</sup> See also Cavanagh, Exh. RCC-4T, at 6.

<sup>67</sup> Schooley, Exh. TES-4T, at 11.

<sup>68</sup> Reynolds, Exh. DJR-1T, at 16-17; see also Schooley, Exh. TES-4T, at 11-12.



proposal does contain an earnings test, but with a higher baseline than Mr. Dittmer proposes. The earnings test in the amended proposal is reasonable, in Staff's view. Mr. Dittmer also states that he would like certain reporting requirements.<sup>69</sup> Staff has indicated that it is amenable to the addition of reporting requirements.<sup>70</sup>

44 In summary, the rate plan and amended decoupling proposal in the Multiparty Settlement Agreement provide for full decoupling and small, limited and reasonable revenue increases based on a reasonable K-factor. The amended decoupling proposal is consistent with the Commission's policy directives, as set forth in PSE's 2012 general rate case and the Commission's Decoupling Policy Statement, and should be approved.

**5. The Multiparty Settlement Agreement contains additional provisions to address the needs of low-income individuals.**

45 In the initial settlement agreement filed on March 22, 2013, the settling parties reserved the right to negotiate a timely addendum to the settlement to make additional changes to PSE's low income bill assistance program and budget.<sup>71</sup> On May 6, 2013, as part of The Energy Project's joinder in the Multiparty Settlement Agreement, several provisions were added to strengthen the settlement and address the needs of low-income individuals.

First, PSE, Staff, and NWECA will support a \$1.5 million increase to the annual funding for the HELP program, which brings the total low-income assistance to \$21.7 million. The increase will continue until rates become effective in PSE's next general rate case. PSE and Staff will not advocate for a decrease in low-income bill assistance funding in PSE's next general rate case. PSE agrees to work with Staff and all interested parties to

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<sup>69</sup> Dittmer, Exh. JRD-1T, at 22-23.

<sup>70</sup> Schooley, Exh. TES-4T, at 12.

<sup>71</sup> Multiparty Settlement Agreement, at ¶ 12.

discuss the merits of the existing HELP program and other potential design options prior to PSE's next general rate case. Finally, PSE will contribute additional shareholder funding of \$100,000 per year during the rate plan period for low-income energy efficiency programs, for a total of up to \$400,000 in additional non-recurring shareholder funding, with this commitment terminating in 2016.

46 All of these additions addressing the needs of low-income individuals serve to strengthen the Multiparty Settlement Agreement and help further the public interest.

6. **The Multiparty Settlement Agreement resolves the outstanding issues concerning the TransAlta PPA and will ensure that the contract will actually be implemented, providing substantial benefits to ratepayers and Washington residents, consistent with legislative intent. Staff thus views resolution of the TransAlta docket as an integral part of the overall settlement agreement.**

47 The Multiparty Settlement Agreement not only resolves the pending ERF and Decoupling dockets, but also resolves the outstanding issues in the pending TransAlta proceeding, Docket UE-121373. Staff is aware that the Commission has determined to address that matter, and PSE's pending motion for reconsideration of Order 03 (to which Staff is filing a response in a separate pleading), as a separate, docketed matter. However, it is critical to keep in mind that the TransAlta PPA and its proposed amendment are an integral part of the global settlement entered into between PSE, Staff, and NWECC.<sup>72</sup>

48 Public Counsel does not refer at all to the TransAlta docket, or to the parties' settlement agreement. Indeed, at the May 16, 2013, hearing, Public Counsel insisted that the Commission should not even discuss the TransAlta docket, or ask any of the settlement

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<sup>72</sup> The Energy Project and NWIGU are later signatories to the Multiparty Settlement Agreement. They have each taken no position regarding the TransAlta portion of the settlement.

panel participants any questions about it. The Commission, quite correctly, refused to do this:

THE COURT:

Okay. Thank you. And I think I just need to make one comment in return, and that is with respect to your [Public Counsel's] suggestion that we will not mention today the TransAlta docket. That is not something that is going to happen.

This is a multiparty settlement filed in the decoupling dockets and the ERF dockets. That settlement of those matters implicates the TransAlta matter. So to the extent that's part of the settlement in these four dockets, clearly we have to be able to talk about it, and we will.

The settlement panel will be here with us momentarily, and we can certainly range into that territory of how that—how that is part of the proposed settlement in the decoupling and the ERF docket, so I just wanted to make that clear so we don't have some unnecessary objections.<sup>73</sup>

The Commission has recognized that the TransAlta PPA *is* an integral part of the Multiparty Settlement Agreement, and it simply is not realistic for Public Counsel to pretend otherwise.

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ICNU witness Mr. Deen addresses the TransAlta PPA briefly in his testimony, but he entirely misses the point of its inclusion in the settlement agreement. Mr. Deen states that “ICNU is extremely skeptical of PSE’s ability to effectively challenge the Commission’s ruling [in the TransAlta matter] in a fully litigated proceeding with a full procedural schedule and final order which carefully considered both the Company and parties’ positions.”<sup>74</sup> Whether this statement is correct or not, this is not the relevant point regarding the settlement agreement. The relevant point, from Staff’s perspective, is that PSE is *not* ultimately obligated to implement the TransAlta PPA at all. It ultimately makes no difference what the terms or conditions are, if the PPA is not implemented.

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<sup>73</sup> Tr., at 120.

<sup>74</sup> Deen, Exh. MCD-1T, at 15.

50 Chairman Danner emphasized this point as well. He made clear, in his questioning of PSE, that the Commission wanted a firm commitment that the TransAlta PPA would be implemented if the Multiparty Settlement Agreement—or the component parts of the settlement agreement—are approved. Mr. Johnson provided this assurance.<sup>75</sup>

51 Staff believes that if the Multiparty Settlement Agreement is not approved, and as a result, PSE does not implement the PPA, this would not serve the public interest. However, the Multiparty Settlement Agreement resolves this problem in a way that *does* serve the public interest. As Mr. Schooley points out, the power generated under the contract will be relatively inexpensive, as compared to the alternatives, thus benefitting ratepayers. The Lewis County economy will reap substantial benefits from the PPA, thus carrying out the Legislature’s intent in enacting the TransAlta statutes.<sup>76</sup> The PPA will also further the environmental goal of transitioning away from coal generation to cleaner fuel sources.<sup>77</sup>

52 Finally, approving the proposed TransAlta amendment to the PPA,<sup>78</sup> as part of the Multiparty Settlement Agreement, will appropriately address issues concerning cessation of generation from the Centralia plant, and termination of the TransAlta Memorandum of Agreement with the State. Issues concerning prudence and deferral are also addressed and resolved, and PSE has agreed that it will no longer pursue any issues regarding the statutory “equity adder” applicable to the PPA.<sup>79</sup>

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<sup>75</sup> Tr., at 125-26.

<sup>76</sup> RCW 80.80.100.

<sup>77</sup> Schooley, Exh. TES-4T, at 13.

<sup>78</sup> The proposed amendment to the TransAlta PPA is contained in the testimony of Mr. Garrett that is included in PSE’s pending motion for reconsideration and to reopen the record in Docket UE-121373.

<sup>79</sup> Schooley, Exh. TES 1T, at 4, 18-19.

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None of this requires the Commission to state that it was “wrong,” or “incorrect,” in issuing Order 03 in the TransAlta docket. It simply means, in Staff’s view, that the Commission can—and should—approve the Multiparty Settlement Agreement, either as a whole or as component parts approved separately, which will ensure that ratepayers and Washington residents receive the benefits of the TransAlta PPA under fair and reasonable terms.

### III. CONCLUSION


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The Multiparty Settlement Agreement, joined in by five parties representing a broad and diverse range of interests, resolves all of the issues in these dockets in a manner that results in fair and reasonable rates, furthers the Commission’s policy directives, and is consistent with the public interest. The Commission should, therefore, approve the Multiparty Settlement Agreement.

DATED this 30<sup>th</sup> day of May 2013.

Respectfully submitted,

ROBERT W. FERGUSON  
Attorney General

  
GREGORY J. TRAUTMAN  
Assistant Attorney General  
Counsel for Washington Utilities and  
Transportation Commission Staff