

**EXH. JKP-1T
DOCKETS UE-22 ___/UG-22 ___
2022 PSE GENERAL RATE CASE
WITNESS: JANET K. PHELPS**

**BEFORE THE
WASHINGTON UTILITIES AND TRANSPORTATION COMMISSION**

**WASHINGTON UTILITIES AND
TRANSPORTATION COMMISSION,**

Complainant,

v.

PUGET SOUND ENERGY,

Respondent

Docket UE-22 ___

Docket UG-22 ___

PREFILED DIRECT TESTIMONY (NONCONFIDENTIAL) OF

JANET K. PHELPS

ON BEHALF OF PUGET SOUND ENERGY

JANUARY 31, 2022

PUGET SOUND ENERGY

**PREFILED DIRECT TESTIMONY (NONCONFIDENTIAL) OF
JANET K. PHELPS**

CONTENTS

I. INTRODUCTION1

II. PSE PROPOSES AN ANNUAL PROCESS FOR UPDATING
POWER COSTS TO COMPLEMENT THE PCORC3

 A. Overview of PSE’s Proposal in this Case3

 B. Background on the PCA and PCORC5

 C. The Commission has Confirmed the Importance of the PCORC in a
 Prior Proceeding.....9

 D. PSE Proposes a System of Annual Changes to the Variable Portion
 of the Baseline Rate Beginning in January 202411

 E. Proposed Annual Filings Would Be Combined With the Current
 Annual PCA Filing12

 F. The PCORC Would Continue to Facilitate Updates to Fixed
 Production Costs20

III. PCORCS AND ANNUAL CHANGES TO POWER COSTS AND
THE VARIABLE PORTION OF THE BASELINE RATE ARE
NECESSARY21

 A. Overview of Reasons for PCORC and Annual Rate Changes21

 B. PSE’s 2021 Integrated Resource Plan Indicates that PSE Needs to
 Add New Resources in the Next Few Years to Meet its
 Capacity and Renewable Energy Needs22

 C. Customers Need Proper Price Signals so they can Make Informed
 Decisions about their Energy Consumption and Conservation26

 D. The Current Regulatory Framework Does Not Provide for Timely
 Inclusion of New Resources or Changing Costs of Existing
 Resources28

E. Recent Under-recoveries Provide Evidence that New Resources and Changes to the Costs of Existing Resources are not Being Put into Rates Fast Enough	36
IV. THE PROPOSED ANNUAL POWER COST UPDATE IS BETTER THAN THE CURRENT SYSTEM	45
A. Annual Updates are Consistent with Practices in Neighboring States.....	45
B. Annual Power Cost Updates are Consistent with the Implementation of Annual Rate Changes in the Multiyear Rate Plan	47
C. The Proposed Process Allows More Time for Review than Provided by the PCORC Process	47
D. The PCA was Intended to Address Volatility in Load and Markets.....	48
E. PSE would Still Have Incentive to Effectively Manage its Power Costs.....	49
V. SUMMARY OF PSE’S PROPOSAL.....	49
VI. CONCLUSION.....	52

PUGET SOUND ENERGY

**PREFILED DIRECT TESTIMONY (NONCONFIDENTIAL) OF
JANET K. PHELPS**

LIST OF EXHIBITS

Exh. JKP-2	Professional Qualifications of Janet K. Phelps
Exh. JKP-3	Historical and Projected Portfolio Capacity 2019-2031
Exh. JKP-4	Generation Resource Start and Expiration Dates vs Dates Included in Rates
Exh. JKP-5	Mid-proceeding Updates to Power Costs in Prior Proceedings (Supplemental and Rebuttal Filings)
Exh. JKP-6	Historical Power Cost Adjustment Imbalances

1 **PUGET SOUND ENERGY**

2 **PREFILED DIRECT TESTIMONY (NONCONFIDENTIAL) OF**
3 **JANET K. PHELPS**

4 **I. INTRODUCTION**

5 **Q. Please state your name, business address, and position with Puget Sound**
6 **Energy.**

7 A. My name is Janet K. Phelps, and my business address is Puget Sound Energy,
8 P.O. Box 97034, Bellevue, Washington 98009-9734. I am employed by Puget
9 Sound Energy (“PSE”) as Manager of Energy Analysis – Power Costs.

10 **Q. Have you prepared an exhibit describing your education, relevant**
11 **employment experience, and other professional qualifications?**

12 A. Yes, I have. It is Exh. JKP-2.

13 **Q. What are your duties as Manager of Energy Analysis for PSE?**

14 A. I oversee a team of analysts in PSE’s Energy Supply Merchant (“ESM”)
15 department. The analysts provide day-to-day support and reporting for trading
16 operations, forecast PSE’s power costs and core gas costs for financial planning
17 and ratemaking purposes, and develop projected power costs in support of the
18 testimony of Director of Energy Supply Merchant Paul K. Wetherbee in PSE’s
19 general rate cases and power cost only rate cases (“PCORC”) as well as PSE’s
20 power cost adjustment (“PCA”) mechanism annual filings.

1 **Q. What topics are you covering in your testimony?**

2 A. My testimony addresses the commitment made in the settlement in PSE’s 2020
3 PCORC to “include in its next general rate case (or another proceeding in 2022)
4 the issue of whether the PCORC should continue.”¹ I provide an overview of the
5 PCORC and PCA mechanism and propose modifications to the current system.

6 PSE’s proposal includes:

- 7 1. modification of the PCORC for periodic updates of fixed
8 production costs, which flow through the fixed portion of the PCA
9 baseline rate;
- 10 2. a process of annual changes to power costs, which flow through
11 the variable portion of the PCA baseline rate; and
- 12 3. annual updates to the surcharge or credit for recovery of costs that
13 are deferred through the PCA.

14 If PSE’s proposal is not accepted, the PCORC should be retained to update both
15 fixed and variable portions of the PCA baseline rate, for the reasons discussed in
16 my testimony.

¹ Docket UE-200980 Settlement Stipulation and Agreement, page 7.

1 **II. PSE PROPOSES AN ANNUAL PROCESS FOR UPDATING POWER**
2 **COSTS TO COMPLEMENT THE PCORC**

3 **A. Overview of PSE’s Proposal in this Case**

4 **Q. Please provide a high level overview of PSE’s proposal in this case with**
5 **respect to the PCORC and the PCA mechanism, and the reasoning for this**
6 **proposal.**

7 A. As discussed in more detail later in my testimony, to comply with the Clean
8 Energy Transformation Act (“CETA”), over the next ten years PSE will need to
9 acquire 3,838 megawatts (“MW”) of supply-side generation capacity additions,
10 which is 115 percent of the capacity of PSE’s current owned generating assets,
11 and 7,634,092 megawatt hours (“MWh”) of incremental energy from renewable
12 and non-emitting resources, which represents more than one-third of PSE’s
13 projected retail electric sales in 2030 (net of conservation and before demand-side
14 resources).

15 Given this historic need to acquire significant new resources and clean energy, it
16 is imperative for PSE to have the ability to update fixed production and power
17 costs in a timely manner to reflect these new resources in its baseline rate.

18 Therefore, PSE’s proposal is to continue a modified PCORC to allow for periodic
19 updates of fixed production costs, while also allowing an annual update of the
20 variable portion of the baseline rate in PSE’s PCA mechanism. This will allow for
21 more timely inclusion of these new clean and non-emitting resources (as well as
22 transmission contracts) in customers’ rates and will send more accurate price

1 signals to customers. It will allow the PCA sharing bands to work as they are
2 intended, which is to address unexpected and acute volatility in power costs,
3 rather than absorbing both the costs of new resources that have been placed in
4 service but not yet gone through prudence review and known changes to other
5 variables that could be reflected in the baseline rate with more timely power cost
6 updates.

7 The nature of PSE's portfolio has changed since the inception of the PCA
8 mechanism twenty years ago, as has the market. For the first 18 years, the sharing
9 bands in the PCA mechanism were able to absorb the over- and under-recoveries
10 of power costs without triggering a surcharge or credit. However, power cost
11 under-recoveries have jumped dramatically in the last three years. PSE
12 implemented a surcharge, approved by the Commission, to recover deferred
13 under-recovered costs from customers starting in December 2020 for the first
14 time, and power cost under-recoveries have continued into 2021. An annual
15 update of the PCA baseline rate for variable power costs, combined with periodic
16 PCORCs to update fixed production costs associated with new and existing
17 resources, will help to limit the need for surcharges or credits because the baseline
18 rate will reflect more up to date costs.

19 The PCORC is a necessary tool in PSE's toolbox if PSE is to successfully
20 transform its portfolio to clean energy, and it should be supplemented with an
21 annual update of the variable portion of the PCA baseline rate to reflect current
22 variable power costs.

1 **B. Background on the PCA and PCORC**

2 **Q. Why does PSE have a PCA mechanism?**

3 A. Volatility in wholesale energy markets coupled with variations in power supply
4 and load volumes can lead to significant differences between the actual cost of
5 PSE's power supply portfolio and the costs included in customer rates. The PCA
6 mechanism seeks to balance the risk of such power cost differences between
7 customers and PSE by providing a method to share costs and benefits if power
8 costs deviate significantly from those embedded in rates.

9 The PCA mechanism originally took effect on July 1, 2002 following a settlement
10 agreement that originated in PSE's 2001 general rate case. As part of PSE's 2013
11 PCORC, Docket UE-130617, PSE and parties to that proceeding initiated a
12 collaborative process to address issues relevant to the PCA mechanism. That
13 process resulted in a multiparty settlement that changed certain elements of the
14 PCA mechanism. The multiparty settlement was approved by the Commission
15 and changes became effective on January 1, 2017.

16 **Q. How does the PCA mechanism work?**

17 A. The PCA mechanism accounts for differences in PSE's actual power costs
18 relative to the power cost baseline recovered in rates. The costs or benefits of such
19 variances are shared between PSE and customers according to three graduated
20 levels of power cost variance, or bands. The dead band includes the first \$17
21 million of power cost variance (positive or negative). Within the dead band, 100

1 percent of costs or benefits are retained by PSE. The first sharing band includes
2 power cost variances between \$17 and \$40 million (positive or negative). Within
3 this band, costs (under-recovered) are shared 50 percent to PSE and 50 percent to
4 customers while benefits (over-recovered) are shared 35 percent to PSE and 65
5 percent to customers. The second sharing band includes power cost variances over
6 \$40 million (positive or negative). All variances in this band are shared ten
7 percent to PSE and 90 percent to customers, regardless of whether they are costs
8 or benefits.

9 The customers' share of power cost variances is accounted for each year and
10 deferred until the cumulative balance in the deferral account triggers a credit or
11 allows a surcharge.

12 **Q. When are surcharges or credits to customers triggered?**

13 A. The PCA settlement terms state:

14 The surcharging of deferrals can be triggered by the Company when
15 the balance of the deferral account is approximately \$20 million.
16 The Company shall make a filing to refund deferrals when the
17 balance in the deferral account is a credit of \$20 million or more.²

18 **Q. What was the intent of the PCA mechanism when it was established?**

19 A. The PCA mechanism was intended to “achieve an appropriate balance between
20 risks to customers and risks to utility shareholders,”³ to provide “PSE incentives

² Dockets UE-130583, UE-130617 and UE-131099, Order 11, Attachment A to Settlement Stipulation, page 2 at A.3.a.

³ Dockets UE-011570 and UG-011571, Twelfth Supplemental Order at 22.

1 to control power costs,”⁴ and “promote rate stability.”⁵ The Commission
2 described the PCA mechanism in its Twelfth Supplemental Order in Dockets UE-
3 011570 and UG-011571 this way:

4 A power cost adjustment mechanism designed to enhance the
5 Company’s financial stability by addressing concerns associated
6 with potentially volatile wholesale power markets and fluctuations
7 in hydropower availability due to uncertain weather conditions.⁶

8 The overview of the PCA in both the original settlement stipulation and the
9 revised settlement stipulation also states that “the factors influencing the
10 variability of power costs included in the mechanism are primarily weather or
11 market related.”⁷

12 **Q. Did the settlement that established the PCA mechanism provide for cost**
13 **recovery for new resources and increased costs of existing resources?**

14 A. Yes. The settlement that established the PCA mechanism included the ability to
15 periodically update rates to reflect power supply costs including costs associated
16 with new resources. Quoting Commission Staff witness Mr. Lott, the Commission
17 stated in its Twelfth Supplemental Order:

18 new resources will not be recovered directly through the PCA, but
19 the Company may periodically update its general rates to reflect
20 increased power supply costs associated with new resources or
21 increased costs of existing resources.⁸

⁴ *Id.* at 24.

⁵ *Id.* at 24.

⁶ *Id.* at 19.

⁷ Dockets UE-130583, UE-130617 and UE-131099, Attachment A to Settlement Stipulation, page 1 at A.1; Dockets UE-11570 and UG-11571, Exh. A to Settlement Stipulation, page 1 at B2.

⁸ Dockets UE-011570 and UG-011571, Twelfth Supplemental Order at 25.

1 The intention was for costs of new resources and increased costs of existing
2 resources to be put into the baseline rate on a timely basis rather than flow
3 through the PCA sharing bands. As the Commission stated, “[t]he objective is to
4 minimize deferral balances by only capturing power cost variability that is
5 extraordinary”⁹ through the PCA bands and to “set the Power Cost Baseline Rate
6 as close as possible to what is expected to be experienced in the rate year.”¹⁰

7 **Q. How are costs of new resources intended to be recovered?**

8 A. The settlement stipulation and order establishing the PCA mechanism established
9 the PCORC so that new resources could undergo a prudence review and be added
10 to the baseline rate. The PCA settlement provided a process that would allow new
11 resources in the baseline rate when they enter service. The Settlement Stipulation
12 states:

13 One objective of a new resource proceeding is to have the new
14 Power Cost Rate in effect by the time the new resource would go
15 into service.¹¹

16 **Q. Is the PCORC only intended to address power cost updates associated with**
17 **the acquisition of new resources?**

18 A. No. As the Commission has recognized,

19 the PCORC was never intended to be limited to power cost updates
20 associated with the acquisition of new resources. The PCORC’s
21 update of the power cost baseline under the PCA is an important
22 feature that helps keep deferral balances within reasonable bounds,
23 making the PCA better suited to its purpose, which is to address

⁹ *WUTC v. PSE*, Docket UE-0702300, Order 13, ¶ 9 (January 15, 2009).

¹⁰ *Id.* ¶ 11.

¹¹ Dockets UE-011570 and UG-011571, Appendix A Settlement Stipulation, C.11.

1 unexpected and acute volatility in power costs while generally
2 avoiding the trigger of surcharges or bill credits.¹²

3 **C. The Commission has Confirmed the Importance of the PCORC in a Prior**
4 **Proceeding**

5 **Q. Has the question of whether the PCORC should continue been presented to**
6 **the Commission in prior proceedings since the inception of the PCORC?**

7 A. Yes. In Docket UE-072300 Public Counsel and Industrial Customers of
8 Northwest Utilities (“ICNU”) recommended elimination of the PCORC.¹³ The
9 issue was ultimately referred to the Commission for a determination.

10 **Q. What was the outcome in that proceeding?**

11 A. The Commission concluded that the PCORC should be retained, but the process
12 by which filings are processed would be improved with specific changes.¹⁴ The
13 Commission commented in its order:

14 The PCORC has proven to be a useful mechanism that allows for
15 timely consideration of PSE’s major resource acquisitions, which
16 are part of an ongoing process to make the Company less dependent
17 on short- and intermediate-term power transactions in sometimes
18 volatile wholesale power markets. Furthermore, the PCORC and the
19 PCA mechanisms have worked together to provide for timely
20 updates to PSE’s power costs in rates and to adjust the Company’s
21 power cost baseline, which has prevented the accumulation of
22 unhealthy positive or negative imbalances in its power cost deferral
23 accounts. In short, the benefits of the PCORC outweigh the
24 arguments for its elimination.¹⁵

¹² *WUTC v. PSE*, Docket UE-072300 Order 13, ¶ 53 (January 15, 2009).

¹³ *Id.*, ¶ 20.

¹⁴ *Id.*, ¶ 59.

¹⁵ *Id.*, ¶ 25.

1 The Commission also said in that order:

2 Complementing the PCA’s purpose of addressing short-term,
3 significant imbalances between expected and actual power costs, the
4 PCORC was intended to adjust rates in response to long-term trends
5 in production-related costs. The PCORC was designed to allow for
6 adjustment of both fixed and variable power costs, and to allow for
7 the more timely inclusion of resource acquisitions in rates.¹⁶

8 **Q. Is there still a need for major resource acquisitions and reduced dependence**
9 **on short- and intermediate-term power transactions?**

10 A. Yes. Washington’s Clean Energy Transformation Act (“CETA”) requires PSE to
11 supply Washington customers with electricity that is 100 percent renewable or
12 non-emitting by 2045 and greenhouse gas (“GHG”) neutral by 2030, and to
13 eliminate coal-fired power by the end of 2025.¹⁷ CETA requires PSE to submit to
14 the Commission a Clean Energy Implementation Plan¹⁸ that is informed by its
15 Clean Energy Action Plan¹⁹ by January 1, 2022 and every four years thereafter.
16 As discussed in the Prefiled Direct Testimony of Joshua J. Jacobs, Exh. JJJ-1T,
17 PSE filed its final Clean Energy Implementation Plan with the Commission in
18 December 2021.

19 CETA requires a transformation of PSE’s resource base over the next several
20 years, and PSE’s 2021 Integrated Resource Plan (“IRP”) indicates a need of 3,838
21 MW of additional supply-side capacity in the next ten years to comply with

¹⁶ *Id.*, ¶ 10.

¹⁷ RCW 19.405.

¹⁸ RCW 19.405.060.

¹⁹ RCS 19.280.030.

1 CETA and meet resource adequacy requirements. This reality qualifies as a “long-
2 term trend in production-related costs.”²⁰

3 Please see the Prefiled Direct Testimony of Kyle C. Stewart, Exh. KCS-01CT, for
4 a discussion of market risk and the need to reduce dependence on market
5 transactions. As discussed in detail later in my testimony, PSE’s PCA under-
6 recoveries in the last three years have been large. They have been driven by
7 multiple factors, including price and load volatility and extreme weather and
8 market events. Developments since the Commission ordered the continuation of
9 the PCORC confirm the importance of the PCORC and provide no support for its
10 elimination.

11 **D. PSE Proposes a System of Annual Changes to the Variable Portion of the**
12 **Baseline Rate Beginning in January 2024**

13 **Q. Please describe PSE’s proposal for annual rate changes.**

14 A. With this proposal, the variable portion of the baseline rate would change
15 annually on January 1. The first rate change that results from the new process
16 would be on January 1, 2024, approximately one year after the effective date of
17 rates in this proceeding. There would also be a rate to collect from or credit to
18 customers the deferred costs that have been assigned to customers through the
19 sharing bands in the PCA mechanism. That rate would be in place as long as there

²⁰ See *WUTC v. PSE*, Dockets UE-072300 and UG-072301, Order 13, paragraph 10 (noting the PCORC was intended to adjust rates in response to long-term trends in production-related costs).

1 remains a balance in the customer deferral account and would change annually on
2 October 1. This routine is similar to the current purchased gas adjustment
3 (“PGA”) mechanism, in which rates are set based on estimated costs for the
4 upcoming year, and the surcharge or credit for deferred costs also changes
5 annually.

6 **E. Proposed Annual Filings Would Be Combined With the Current Annual**
7 **PCA Filing**

8 **Q. What annual procedure does PSE propose?**

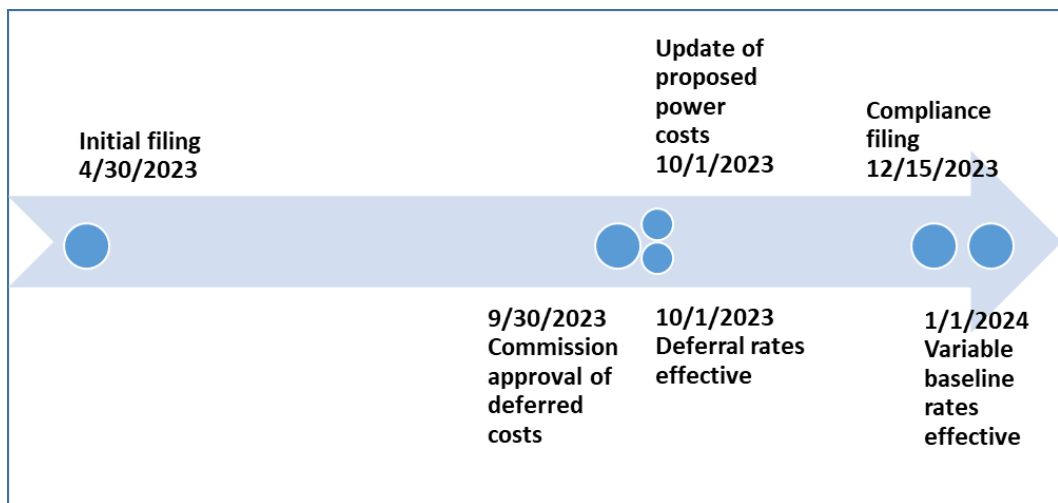
9 A. PSE requests that the Commission establish an annual schedule that combines the
10 existing PCA annual filing with annual changes to the variable portion of the
11 baseline rate. It would include the following timetable:

- 12 • Initial filing on April 30;
- 13 • Commission approval of deferred costs by September 30, consistent with
14 current practice;
- 15 • Deferral rate change effective October 1;
- 16 • Update of proposed power costs approximately October 1;
- 17 • Compliance filing approximately December 15; and
- 18 • Variable baseline rate effective January 1.

19 When PSE files its case on April 30, the Commission would establish a
20 procedural schedule that includes specific dates and milestones that are typical in
21 a PCORC, such as a prehearing conference, discovery schedule, testimony
22 schedule, deadlines for briefs, and a hearing date. The schedule would allow for

1 involvement by Commission Staff, Public Counsel, and other parties who are
2 granted the right to intervene in the proceeding. It would include the opportunity
3 for PSE to provide a full update of the power costs in the variable baseline rate
4 during the proceeding at approximately October 1, and for a full or partial update
5 in a compliance filing. The proposed procedural schedule is depicted in Figure 1.

6 **Figure 1. Proposed Procedural Schedule for Annual Updates**



8 **Q. What would be the content of PSE’s April 30 filing?**

9 A. The annual filing would combine the current contents of the required PCA annual
10 filing with information that supports the proposed January 1 change to the
11 baseline rate and October 1 change to the deferral rate. Using the April 2023
12 filing for a January 2024 baseline rate change as an example, the April filing
13 would include the following:

- 14 1. A report on 2022 actual power costs and changes to the PCA
15 deferral balance in 2022, consistent with current practice.

- 1 2. A comparison of 2022 actual power costs with the projections that
2 were used to set the rates that were in effect during 2022,
3 consistent with current practice.
- 4 3. A current projection of all 2024 power costs in the variable
5 baseline rate.
- 6 4. A proposed baseline rate effective January 1, 2024.
- 7 5. An estimate of the deferral surcharge or credit effective October 1,
8 2023 reflecting the December 2022 deferral balance, contingent
9 upon Commission approval by September 30.
- 10 6. Testimony supporting all of these items as well as:
 - 11 (a) Prudence of new resources that affect power costs; and
 - 12 (b) Preliminary information on relatively straightforward and
13 small scale new resources that have not yet been finalized
14 but are expected to be finalized during the pendency of the
15 proceeding.

16 **Q. Why does PSE propose to include preliminary information on potential new**
17 **resources in its April filing?**

18 A. There may be circumstances when PSE is very close to finalizing a contract for a
19 new resource but has not finalized the transaction in time for the April filing. If a
20 transaction is expected to be finalized within the pendency of the case, it is
21 relatively minor and straightforward resource, and the resource is scheduled to be
22 operational during the rate effective period (calendar 2024 in this example), PSE
23 would like to seek a prudence determination for that resource and include the
24 costs in its October update. PSE understands that sufficient time is required to
25 allow parties and the Commission the opportunity to review the prudence of new
26 resources, and at some point in the proceeding it will be too late to introduce new

1 resources. The intention of providing preliminary information on resources that
2 are not yet finalized is to accommodate the need for meaningful review.

3 **Q. Would you provide an example of a relatively minor and straightforward**
4 **resource that PSE might propose to update during the course of the annual**
5 **proceeding?**

6 A. Yes. In July 2019 PSE purchased a 50 MW contract for long-term point-to-point
7 transmission service with Bonneville Power Administration (“BPA”) from Talen
8 Energy. Talen Energy had issued a request for proposals (“RFP”) to sell the
9 contract; PSE submitted a bid and was the successful bidder. PSE was prohibited
10 by the procedural schedule in the 2019 general rate case from adding the contract
11 during that proceeding, which was filed in June 2019, just one month before the
12 purchase PSE requested and was granted by the Commission a prudence
13 determination of the contract in the 2020 PCORC, Docket UE-200980. The cost
14 of the contract was included in rates effective July 1, 2021, eighteen months after
15 PSE began incurring costs. This contract was not controversial in the PCORC.
16 Opportunities to acquire resources like this arise periodically, and PSE pursues
17 them. PSE proposes that the annual update process provide opportunity for
18 inclusion of similar resources during the annual review process.

19 **Q. What does PSE propose to update during the course of the annual**
20 **proceeding?**

21 A. PSE proposes a full update to power costs in the variable baseline rate, with the
22 qualifications on new resources described above. Specifically, PSE proposes to

1 update the following items in the October update and in any other updates
2 required by the Commission or agreed to by the parties to the case.

3 Costs associated with Mid-C hydro contracts. PSE has long-term contracts with
4 three Public Utility Districts (“PUDs”) for hydroelectric energy – Grant, Chelan
5 and Douglas PUDs. PSE receives new information on these costs from Grant
6 three times per year, Chelan four times per year, and Douglas once per year. The
7 most current projections need to be included in rate year power costs.

8 Costs associated with upstream pipeline capacity. PSE takes service from
9 Northwest Pipeline, Westcoast Energy, Cascade Natural Gas, Nova Gas
10 Transmission, Foothills Pipeline and Gas Transmission Northwest. These service
11 providers update their tariffs periodically, and PSE’s costs change as a result. The
12 most current tariff rates need to be reflected in rate year power costs.

13 Outage schedules. PSE regularly updates its schedule of planned outages for its
14 resources. This outage information is an important input to the dispatch logic and
15 the most current information needs to be reflected in rate year power costs.

16 BPA rates. BPA rates change every other year on October 1. In years when BPA
17 rates change, BPA’s proposed rates will be available when PSE makes its initial
18 filing in April but final rates will not. However, a final record of decision will
19 become available during the course of PSE’s annual proceeding. These known
20 and measurable rate changes need to be included in rate year power costs.

1 Load forecast. PSE updates its long-term load forecast annually. The forecast
2 used in the April filing might not be current when rates take effect unless it is
3 updated. The most recent forecast incorporates the most recent historical data on
4 PSE load and customer counts and current input assumptions related to economic
5 and demographic data. PSE proposes to use the most recent load forecast in its
6 October update and any other updates during the course of the annual proceeding.

7 Input assumptions used in dispatch logic. PSE has a quarterly process for
8 updating its variable operation and maintenance (“O&M”) costs, and when PSE
9 calculates rate year power costs it uses the most recent estimates. Under this
10 proposal PSE would use the most recent version of variable operations and
11 maintenance costs when it updates power costs during the proceeding. Variable
12 O&M costs are not power costs, but they are important input assumptions to the
13 dispatch logic in the power cost model.

14 Hedges and physical supply contracts. PSE’s Energy Supply Merchant (“ESM”)
15 department purchases and sells power and natural gas in the marketplace every
16 day, with all transactions compliant with the Energy Supply Transaction and
17 Hedging Procedures Manual and Energy Risk Policy as discussed in the Prefiled
18 Direct Testimony of Kyle C. Stewart, Exh. KCS-1CT. Currently, power cost
19 updates include incorporating all these transactions up to a certain cut-off date
20 before the Aurora model is run. PSE’s proposal for annual power cost updates
21 includes this process of updating hedges and physical supply contracts during the
22 proceeding and at the compliance filing.

1 Natural gas prices. Forward natural gas prices are a necessary input to the Aurora
2 model and are used to forecast some out of model power costs. Currently, power
3 cost updates include incorporating three-month average forward natural gas prices
4 as of the same cut-off date used for hedges and physical supply contracts. PSE's
5 proposal for annual power cost updates would include this process of updating
6 natural gas prices during the proceeding and at the compliance filing.

7 Changes to terms of current resources. Sometimes terms change. For example,
8 during the course of the 2019 general rate case there was a change to the price for
9 the contract serving Point Roberts because the term expired. Sometimes volumes
10 in contracts change, such as the Centralia contract. These types of changes need to
11 be included during the annual proceeding.

12 Limited new and updated resources. Some new resources are relatively small in
13 terms of rate year power cost and noncontroversial. Examples include new
14 Schedule 91 contracts, and a transmission contract acquired from a third party as
15 discussed above.

16 **Q. How often does PSE propose to rerun its power cost model during the annual**
17 **process?**

18 A. PSE proposes to run Aurora to estimate rate year power costs for its April filing,
19 again for the October update to power costs, and for a compliance filing made in
20 response to the Commission's order. Other reasons PSE would rerun its power
21 cost model would be a request from the Commission or agreement among the
22 parties at the prehearing conference.

1 **Q. Does PSE propose to include potential updates to its methods for projecting**
2 **rate year power costs in its annual April filings, if there are any proposed**
3 **changes?**

4 A. PSE has used a combination of Aurora and Excel to model its power costs for
5 many years, but the approach has evolved over time. PSE could potentially
6 propose modifications to its methods in its April filing.

7 **Q. Will PSE's proposal comply with RCW 80.28.425(3)(e) which requires an**
8 **update to power costs in the third rate year of a multiyear rate plan?**

9 A. Yes. The law requires a power cost update in the third rate year of a multiyear rate
10 plan but it does not prohibit more frequent power cost updates, as PSE is
11 proposing. Given PSE's proposal to update power costs annually, the annual
12 filing in 2024 for a rate change effective January 1, 2025 would fulfill the
13 requirement of the law.

14 **Q. How will variable power costs be treated in future general rate cases?**

15 A. PSE proposes that the ratemaking process for variable power costs be included
16 entirely in the annual update process described herein, beginning with a filing in
17 April 2023 that results in a deferral rate change in October 2023 and a variable
18 baseline rate change in January 2024. With this process in place, it will be
19 unnecessary to include variable power costs in future general rate cases.

1 **Q. How will updating the variable baseline rate in annual updates instead of**
2 **general rate cases impact PSE's tariffs?**

3 A. PSE proposes to establish a tariff that corresponds with the variable baseline rate.
4 This schedule would be effective January 1, 2024 and the rates would be updated
5 annually on January 1. Please see the Prefiled Direct Testimony of Jon A. Piliaris,
6 Exh. JAP-1T, for a discussion of these tariff changes.

7 **F. The PCORC Would Continue to Facilitate Updates to Fixed Production**
8 **Costs**

9 **Q. How does PSE propose to use the PCORC in the future?**

10 A. PSE proposes to continue use of the PCORC for updating fixed production costs
11 on an as-needed basis. If the Commission approves PSE's proposal for annual
12 power cost updates, PSE proposes to amend the PCORC so that it is limited to
13 updating fixed production costs, which flow through the fixed portion of the PCA
14 baseline rate. If the Commission declines to approve annual power cost updates,
15 PSE proposes that the PCORC continue in its current form to allow updates to
16 both fixed and variable portions of the baseline rate.

17 As discussed in more detail below, PSE's IRP indicates a need for the addition of
18 3,132 MW of new resources in the next ten years. If any of these resource
19 additions include the acquisition or construction of physical plant, they will
20 impact PSE's rate base and O&M costs. These costs are recovered through the
21 fixed portion of the baseline rate, and PSE would utilize the PCORC and general
22 rate case processes to add these resources to its rates.

1 **III. PCORCS AND ANNUAL CHANGES TO POWER COSTS AND THE**
2 **VARIABLE PORTION OF THE BASELINE RATE ARE NECESSARY**

3 **A. Overview of Reasons for PCORC and Annual Rate Changes**

4 **Q. Why is the PCORC necessary?**

5 A. The PCORC is necessary because 1) PSE is required by law and resource
6 adequacy requirements to add large amounts of generation capacity to its portfolio
7 in the next ten years, 2) customers need proper price signals so they can make
8 informed decisions about energy consumption and conservation, and 3) the
9 general rate case process is too lengthy to bring new resources into customer rates
10 on a timely basis as they become operational and to keep the costs of existing
11 resources current, particularly when the general rate case is paired with a
12 multiyear rate plan. The upcoming resource additions will impact production-
13 related capital O&M costs as well as power costs, and the PCORC is an important
14 tool for updating rates, although as I discuss below, it too has limitations in terms
15 of providing for timely inclusion of all new resources and updates to existing
16 resources.

17 **Q. Can the rate base and O&M costs associated with new resources be included**
18 **in PSE's multiyear rate plan projections?**

19 A. The multiyear rate plan includes annual rate changes for other components of
20 PSE's rates. Production costs are uncertain and therefore difficult to accurately
21 estimate multiple years in advance to meet the Commission's known and
22 measurable standard, particularly when new resources are anticipated. The

1 PCORC is the most expedient tool in the current ratemaking toolkit to update
2 fixed production costs so that customer rates align with actual production costs.

3 **Q. Why are annual updates to the variable baseline rate necessary?**

4 A. Annual updates to the variable baseline rate are necessary for the same reasons
5 the PCORC is necessary. Even though the PCORC process is more streamlined
6 than the general rate case process, it does not provide for timely inclusion of all
7 new resources and updates to existing resources. Annual baseline rate updates
8 would improve the alignment of customer rates with resource costs. Recent PCA
9 imbalances provide evidence that the current system is inadequate for aligning
10 costs charged to customers with actual power costs.

11 **Q. Would the Commission's approval of an annual power cost update remove
12 the need for the PCORC?**

13 A. No. There would still be a need for the PCORC to update the fixed portion of the
14 baseline rate, especially when PSE acquires or constructs new physical plant, as I
15 discussed previously in my testimony.

16 **B. PSE's 2021 Integrated Resource Plan Indicates that PSE Needs to Add New**
17 **Resources in the Next Few Years to Meet its Capacity and Renewable Energy**
18 **Needs**

19 **Q. What changes to PSE's resource portfolio are anticipated in the next few
20 years?**

21 A. The Clean Energy Action Plan in PSE's 2021 IRP presents a ten-year preferred
22 portfolio that includes 706 MW of distributed energy resources, 1,898 MW of

1 renewable resources, 255 MW of peaking capacity using biodiesel fuel, and 979
2 MW of firm resource adequacy qualifying capacity contracts between 2022 and
3 2031. This is a total of 3,838 MW of supply-side capacity additions over 10
4 years.²¹ The IRP also identifies a need for 7,634,092 MWh of renewable and
5 non-emitting resources per year by 2030 to meet PSE's obligation required by
6 CETA (net of conservation and before demand-side resources).²²

7 **Q. How significant are these resource additions to PSE's portfolio?**

8 A. The capacity of PSE's owned assets currently totals 3,332 MW. PSE has an
9 additional 1,475 MW of contracts. The additional 3,838 MW of supply-side
10 resources called for over the next ten years in the IRP is 115 percent of the
11 capacity of PSE's current owned generating assets. The magnitude of the new
12 resources in terms of capacity relative to historical capacity additions is illustrated
13 in Exh. JKP-3. By 2031, total new additions will be ten times the capacity that
14 was added in 2021. The 1,898 MW of planned renewable capacity called for by
15 2031 in the 2021 IRP is approximately five times the capacity of Colstrip Units 3
16 and 4, which PSE will no longer use to serve customers in Washington after 2025.
17 The 7,634,092 MWh of incremental energy required to fulfill PSE's CETA
18 obligation represents approximately 34 percent of PSE's projected retail electric
19 sales in 2030.

²¹ 2021 PSE Integrated Resource Plan, Figure 2-1 including demand response. Figure 2-1 also includes 696 MW of demand-side resources.

²² Final PSE 2021 IRP, Figure 8-4.

1 **Q. Have there been modifications to the preferred portfolio identified in the**
2 **IRP?**

3 A. Yes. PSE's 2021 Clean Energy Implementation Plan is based on the IRP but
4 updated for recent resource additions and costs. The Clean Energy
5 Implementation Plan indicates a plan to add the following resources:

- 6 • 200 MW of wind generation in 2024 and 300 MW of wind in 2025 instead
7 of the 400 MW of wind in 2025 identified in the IRP;
- 8 • 200 MW of solar in 2024 and 100 MW of solar in 2025;
- 9 • 25 MW of battery storage in 2024 and another 25 MW of battery storage
10 in 2025;²³
- 11 • 80 MW of distributed energy resource ("DER") solar in total installed
12 between 2022 and 2025; and
- 13 • 25 MW of DER battery storage in total installed between 2022 and
14 2025.²⁴

15 **Q. How will the CETA requirement to eliminate coal-fired resources impact**
16 **PSE's power costs?**

17 A. The fuel costs from Colstrip are power costs, and when PSE ceases to serve
18 customers with Colstrip Units 3 and 4 after 2025, those fuel costs will no longer
19 be in PSE's power costs.

²³ See Exh. JJJ-3, at 28, Table 2-8.

²⁴ *Id.*, at 7, Figure 1-4.

1 **Q. How will the new resources identified in PSE’s 2021 IRP and Clean Energy**
2 **Implementation Plan impact PSE’s power costs?**

3 A. As described in the Prefiled Direct Testimony of Paul K. Wetherbee, Exh. PKW-
4 1-CT, PSE’s power costs include the costs of purchased power, fuel for
5 generation resources and third-party transmission. All power purchase agreements
6 (“PPA”) that PSE executes will be included as power costs when they are
7 effective. If physical assets are added to the portfolio, the fuel cost associated with
8 them will be included in power costs, although renewable resources such as wind
9 typically do not include fuel costs. New transmission contracts to deliver power to
10 PSE’s system will also be included in power costs. New resources also impact
11 PSE’s power costs because they change operating reserve requirements and the
12 cost of balancing generation with load.

13 **Q. Why can’t PSE simply defer the cost of these new resources as allowed by**
14 **RCW 80.28.410?**

15 A. Mr. Kazi Hasan discusses the limitations of deferrals in his testimony, specifically
16 that deferrals do not provide the cash flows necessary for maintaining financial
17 strength. Please see the Prefiled Direct Testimony of Kazi K. Hasan, Exh. KKH-
18 1CT, for additional detail on the limitations of deferring new resources.

1 **Q. Is it necessary to update power costs annually when the PCORC allows for**
2 **periodic updates to all production costs?**

3 A. Yes, PSE believes it is. As discussed above, PCORCs alone do not provide for
4 sufficiently timely updates to power costs given the magnitude of resource
5 changes coming and the limited updates to power costs that recently have been
6 allowed during the proceeding. While PCORCs are important to bring in fixed
7 production costs associated with new resources, the PCORC alone will not send
8 proper price signals to customers. Given the massive changes that lie ahead for
9 PSE's portfolio and market, a process that provides a timelier update to power
10 costs is needed.

11 **C. Customers Need Proper Price Signals so they can Make Informed Decisions**
12 **about their Energy Consumption and Conservation**

13 **Q. Why are proper price signals important?**

14 A. One of the principles of utility ratemaking described by James Bonbright, et al. in
15 their book Principles of Public Utility Rates²⁵ is efficiency. Effective utility rates
16 should promote efficient use of energy and competing products and services. One
17 of the primary objectives of a sound rate structure as described by Bonbright is

18 the consumer-rationing objective, under which the rates are
19 designed to discourage the wasteful use of public utility services
20 while promoting all use that is economically justified in view of the

²⁵ Principles of Public Utility Rates, by James C. Bonbright, Albert L. Danielsen and David R. Kamerschen, Public Utilities Reports, Inc., 1988.

1 relationships between the private and social costs incurred and
2 benefits received.²⁶

3 Throughout the economy, customers rely on the price of goods and services to
4 determine how much of a given product or service to consume and when to
5 purchase it. If prices charged to customers for energy are not consistent with the
6 cost to provide that energy, customers do not have the right information to make
7 decisions about their energy consumption.

8 Another primary objective of a sound rate structure described by Bonbright is the

9 fair-cost apportionment objective, which invokes the principle that
10 the burden of meeting total revenue requirements must be
11 distributed *fairly* and without arbitrariness, capriciousness, and
12 inequities among the beneficiaries of the service and so as, if
13 possible, to avoid undue discrimination.²⁷

14 The rates customers pay should align with the benefits they receive. Customers
15 move in and out of PSE's service territory constantly. If rates charged to
16 customers today are not adequate to pay for the service those customers receive,
17 customers who leave PSE's service area never pay the full cost of the benefits
18 they receive, but new customers who join PSE's system later pay the deferred cost
19 of service that was received by previous customers. If costs are deferred for later
20 recovery from customers, rather than having rates accurately reflect costs, then
21 costs do not align with benefits received.

²⁶ *Id.*, page 385.

²⁷ *Id.*

1 **Q. How does PSE’s proposal to continue the PCORC and implement annual**
2 **rate changes improve customer price signals?**

3 A. The proposed system of annual rate changes in combination with the PCORC is
4 better than the current system with respect to both the efficiency and fairness
5 principles of ratemaking. Annual updates to the variable baseline rate would result
6 in customer rates that are based on the best information about the actual cost of
7 the energy that customers consume and would align charges to customers with the
8 benefits customers receive rather than pushing costs to future customers. Removal
9 of the PCORC and reliance on changes only through the general rate case process
10 would exacerbate the inconsistency between rates customers pay and the costs to
11 serve those customers. This violates the ratemaking principles of efficiency and
12 fairness.

13 **D. The Current Regulatory Framework Does Not Provide for Timely Inclusion**
14 **of New Resources or Changing Costs of Existing Resources**

15 **Q. What are the limitations of the current system of changing the variable**
16 **baseline rate in general rate cases and PCORCs?**

17 A. The current process does not provide for timely inclusion of new resources,
18 timely updates to the costs of existing resources, the most recent fuel prices, or the
19 best projections of load in determining rate year power costs and calculating the
20 variable baseline rate. Given the length of time a general rate case requires, it is
21 not practical to file general rate cases fast enough to incorporate all new
22 resources. Some new resources are large in capacity and cost, and some are

1 relatively small, but all need to be included in the baseline rate. In addition, some
2 of the existing costs listed above change frequently, so for rates to reflect true
3 costs the rates need to be updated more frequently than can be achieved with a
4 general rate case.

5 **Q. Why does the current process not allow for timely inclusion of the cost of new**
6 **resources in the baseline rate?**

7 A. When PSE files a general rate case, power costs are estimated approximately
8 thirteen months in advance of the rate effective date. PSE files its case eleven
9 months before the effective date, and PSE cuts off data inputs approximately two
10 months prior to that to allow time to complete the analysis and incorporate results
11 into revenue requirement, cost of service and rate design calculations and
12 testimony. When PSE files a PCORC, power costs are estimated approximately
13 eight months in advance of the start of the rate year. General rate cases and
14 PCORCs provide time for prudence reviews of new resources, but if PSE
15 executes a new contract after finalizing its proposed power costs, that new
16 resource does not get reviewed and put into rates until the next general rate case
17 or PCORC. This can result in a gap between the effective date of a new resource
18 and the date when it is included in rates. New resources that become effective
19 during the rate year or after the rate year but when rates are still in effect are
20 excluded from the baseline rate until the next rate case cycle. This works in both
21 directions. When a resource ceases to provide service to PSE, its costs and energy
22 are not removed from the revenue requirement used to establish the baseline rate

1 until the rate effective date associated with the next general rate case or PCORC.
2 This lag contributes to the PCA imbalance.

3 **Q. Please provide an example.**

4 A. The 2020 PCORC was filed on December 9, 2020 and had a rate effective date of
5 July 1, 2021. During the proceeding, in March 2021, PSE executed an extension
6 of the contract with Douglas County PUD for the Colville slice of the Wells
7 Hydroelectric Project effective October 1, 2021. Also in March 2021, PSE
8 executed a contract with Chelan County PUD for a five percent slice of the Rock
9 Island and Rocky Reach Hydroelectric Projects effective January 1, 2022.

10 Because these contracts were executed after PSE filed its initial case in the 2020
11 PCORC, the net impact of the contracts was not included in the rates effective on
12 July 1, 2021. They will not be included in the baseline rate until the rate effective
13 date in this proceeding, which is expected to be in January 2023. This means the
14 rates currently in place do not accurately represent these known and measurable
15 resources for fifteen months for the Colville slice and for a year for the Rocky
16 Reach and Rock Island slice, from October 2021 through December 2022.

17 Some new resources are developed in a relatively short period of time because
18 suppliers issue RFPs, and PSE must act quickly to acquire the resource in accord
19 with the schedule of the supplier. As a result, the impact of these contracts on
20 power costs may not be reflected in rates for over a year simply due to timing. For
21 example, as indicated in the testimony of Paul Wetherbee in PSE's 2020 PCORC,
22 Energy Keepers, Inc. issued a request for offers to purchase carbon-free energy

1 from its hydroelectric project in October 2019. The start date of the PPA that PSE
2 ultimately negotiated with Energy Keepers was March 1, 2020.²⁸ This resource
3 came to PSE's awareness after the 2019 general rate case was in process, and PSE
4 was not able to seek a prudence determination until the 2020 PCORC even though
5 the resource start date was March 1, 2020. This resulted in a 16-month lag from
6 the resource start date to the date it was fully included in customer rates.

7 There are other inconsistencies between costs and rates related to timing. A new
8 resource is included in rate year power costs beginning with the month that
9 resource is scheduled to start. If a resource starts in the twelfth month of the rate
10 year, only one month of costs are included in rates. Those rates are typically in
11 place beyond the initial rate year after the resource is in the portfolio, but only one
12 month worth of costs is included in rates.

13 Exh. JKP-4 presents a summary of new resources in PSE's last four rate cases,
14 with the resource start date, rate case when it was presented to the Commission,
15 rate effective date, and months of lag between start date and rate effective date.

16 Exh. JKP-4 also presents resources that have ended with their termination dates
17 and the dates they were removed from rates. This exhibit illustrates that there are
18 typically several months to more than two years of lag between the start or
19 termination of a resource and the date that change is represented in the baseline
20 rate. In some cases when a resource is included in the baseline rate without lag, it

²⁸ Docket UE-200980 Exh. PKW-1CT pages 10-12.

1 is only partially included because resource start or termination dates do not align
2 with the start of a rate year.

3 **Q. Are new resources included in allowable power costs in the PCA?**

4 A. Yes they are, but inclusion in allowable costs in the PCA does not constitute
5 collection of revenue to recover those costs. In simple terms, the PCA imbalance
6 is calculated as the difference between allowable costs and baseline rate revenue,
7 with baseline rate revenue determined by multiplying actual load in MWh by the
8 variable baseline rate in dollars per MWh. Putting new resource costs into
9 allowable power costs provides for sharing of those costs with customers (in the
10 form of a deferral) if the imbalance is outside of the dead band. That is not the
11 same as including costs in the baseline rate, which provides an opportunity for full
12 recovery and further provides that current customers are paying the current cost of
13 power supplied by PSE. The PCA is not a substitute for cost recovery of
14 prudently-incurred costs through the baseline rate.

15 **Q. Does that work in both directions?**

16 A. Yes, it does. If an existing PPA expires in the middle of a rate year, its cost is
17 included for only the months it is still in existence, but the rates could extend
18 beyond that rate year. The proposed annual updates would account for all changes
19 to resources, whether they be new resources joining the portfolio or existing
20 resources expiring.

1 **Q. Why does the current process not allow for timely updates to the costs of**
2 **current resources when calculating the baseline rate?**

3 A. Some contracts have periodic rate changes, with new information becoming
4 available during the course of the proceeding. For example, PSE's contracts with
5 Grant, Douglas and Chelan PUDs allow for regular cost changes. When PSE
6 estimates its power costs for its initial general rate case or PCORC filing, PSE
7 uses the most current information, but that information changes during the course
8 of the proceeding.

9 **Q. What costs change frequently and warrant updating?**

10 A. All of the items listed above in Section II.E change routinely or periodically and
11 warrant updating during a proceeding.

12 **Q. Does PSE have an established process for updating its load forecast?**

13 A. Yes. PSE updates its load forecast on an annual basis. The annual update to the
14 load forecast allows inclusion of the most recent historical data on customer
15 counts and energy consumption when projecting future energy consumption. The
16 annual update also includes the most recent economic and demographic data to
17 inform the forecast.

1 **Q. Do PSE's rate proceedings include the best projections of load when**
2 **calculating the baseline rate?**

3 A. No. Typically, a new forecast is developed during the course of a rate proceeding,
4 but PSE continues to use the load forecast it used in the initial filing throughout
5 the proceeding even though it is not the most current information.

6 **Q. Why is updating to the most recent load forecast important for calculating**
7 **the variable portion of the baseline rate?**

8 A. The variable portion of the baseline rate is calculated by dividing power costs by
9 megawatt hours. Load is an input to projected costs, and the denominator in
10 determining the rate to be charged to customers. An old load forecast results in
11 outdated cost projections and resulting rates.

12 **Q. Does PSE update power costs for new resources, changes to existing**
13 **resources, and a new load forecast in the course of a general rate case or**
14 **PCORC?**

15 A. Historically, PSE has made updates during proceedings. In recent proceedings
16 Commission Staff have been reluctant to consider updates other than limited
17 updates during the course of the proceeding. For example, Appendix B to Order
18 03 in Dockets UE-190529 and UG-190530 explicitly limited the items that could
19 be updated in that proceeding to only gas prices and short-term contracts for
20 power and natural gas. PSE ultimately agreed to that limitation during protracted
21 discussions over the procedural schedule, but the limitation was driven by the

1 reluctance of Commission Staff to consider other items to be updated, or more
2 than one update process, during the course of that proceeding. In Paul
3 Wetherbee's rebuttal testimony in that proceeding he illustrated that several other
4 costs had changed or been added during the course of the proceeding but were not
5 included because of the limitation in Order 03. At the time Mr. Wetherbee
6 quantified the omission of those items as an inaccuracy of \$14.9 million in rate
7 year power costs.²⁹

8 This opposition to mid-proceeding updates means that supplemental, rebuttal and
9 compliance filings have afforded only limited opportunity to update information
10 during a proceeding.

11 **Q. Have these obstacles to updating during a proceeding always been present?**

12 A. No. Until recently, it was routinely expected that PSE would update power costs
13 at least once during the course of a rate proceeding, with the possibility of
14 updating power costs again for the compliance filing. Exh. JKP-5 presents a list of
15 standard power cost items and indicates when they were updated in all of PSE's
16 rate cases dating back to 2004. This list indicates that updates in a supplemental
17 or rebuttal filing and sometimes both were standard prior to the 2019 general rate
18 case. Items that were updated include gas prices, hedges and physical supply
19 contracts, the load forecast, Mid-C hydro costs, BPA transmission rates, resource
20 outage schedules, coal costs, pipeline contracts and costs, and PPA prices.

²⁹ Dockets UE-190529 & UG-190530, Exh. PKW-34CT, pages 30-31.

1 **Q. Why is the PCORC still necessary if annual power cost updates are**
2 **approved?**

3 A. PSE's proposal for annual power cost updates would address the need to align the
4 variable portion of the baseline rate with power costs. It would not address the
5 need to align the fixed portion of the baseline rate with fixed production costs.
6 Upcoming resource additions driven by CETA and resource adequacy
7 requirements could take the form of PPAs, which would flow through power costs
8 and the variable portion of the baseline rate, or physical assets, which would have
9 capital and O&M costs that require recovery through the fixed portion of the
10 baseline rate.

11 The ratemaking principles of efficiency and fairness apply to all components of
12 rates including fixed production costs, and removal of the PCORC would reduce
13 rather than improve alignment with these principles.

14 **E. Recent Under-recoveries Provide Evidence that New Resources and Changes**
15 **to the Costs of Existing Resources are not Being Put into Rates Fast Enough**

16 **Q. What have PCA imbalances been over the years?**

17 A. From the inception of the PCA in July 2002 until 2018, annual imbalances ranged
18 from \$39.6 million under-recovered in 2014 to \$38.0 million over-recovered in
19 2013, but the average annual imbalance was \$1.1 million under-recovered. During
20 this period the cumulative imbalance ranged from \$62.7 million under-recovered
21 to \$35.8 million over-recovered, with an average of \$16.0 million under-
22 recovered. Only a portion of the imbalance is assigned to customers. A return of

1 deferred over-recoveries was never triggered, and PSE never sought recovery of
2 deferred under-recoveries during that period. Things changed in 2019. PSE under-
3 recovered PCA power costs by \$67 million in 2019, \$76 million in 2020, and \$68
4 million in 2021. As of December 2021, the cumulative imbalance since July 2002
5 would have been \$229.0 million under-recovered if not for \$83.5 million of
6 receivables for under-recovered costs being recovered from customers, excluding
7 interest. Exh. JKP-6 provides a summary of historical PCA imbalances. As
8 indicated in Exh. JKP-6, under-recoveries have jumped dramatically in the last
9 three years.

10 PSE implemented a surcharge to recover deferred costs from customers starting
11 December 2020 for the first time. That request resulted in recovery of \$41.7
12 million of deferred costs including interest.³⁰ In PSE's 2020 annual PCA filing
13 the Commission approved a request to recover an additional \$46.0 million of
14 deferred costs.³¹ In total, \$87.7 million is being recovered from customers via
15 surcharges for costs dating through 2020. However, as discussed above and
16 indicated in Exh. JKP-6, under-recoveries have continued in 2021.

17 **Q. What have been the drivers of under-recoveries in recent years?**

18 A. PSE has provided explanations of under-recoveries in its annual PCA filings. In
19 general terms, they have been driven by load below the forecast used to set rates,

³⁰ Docket UE-200893, Advice No. 2020-39 and Commission staff memo. Excluding gross-up for revenue sensitive items.

³¹ Docket UE-210300, Exh. SEF-1 Tr page 9 line 6 and Order 01 paragraph 23. Excluding gross-up for revenue sensitive items.

1 new resources not in rates, changes to prices of long-term contracts, wind and
2 hydro generation variances from the levels assumed when setting rates, increases
3 to rates charged by upstream gas pipeline and transmission providers, and price
4 and load volatility partially related to extreme weather and market events.³² In
5 2019 specifically, there was an extreme event in February and March that
6 involved cold weather and multiple supply constraints.³³ Under-recoveries in
7 2019 also reflected cost escalation on long-term contracts, a transmission rate
8 increase, low wind and hydro generation, and load below forecast.³⁴ Table 1
9 below provides a comparison of 2019 power costs relative to those included in
10 rates by resource type, and the impact of load variance on baseline rate revenue.

³² Docket UE-200398 Exh. PKW-1CT and Docket UE-210300 Exh. PKW-1CT.

³³ Docket UE-200398 Exh. PKW-1CT page 12.

³⁴ Docket UE-200398 Exh. PKW-1CT pages 16-20.

Table 1: 2019 PCA Period Cost Recovery Summary	
Cost above / (below) 2017 General Rate Case	\$M
Coal ³⁵	22.2
Natural Gas Fuel and Transportation ³⁶	(77.4)
Long Term Contracts ³⁷	(1.6)
Market Purchases and Sales ³⁸	95.0
Transmission ³⁹	9.0
Other	8.5
Total Costs	55.6
Revenue (above) / below 2017 General Rate Case	
Load ⁴⁰	11.6
Total Revenue	11.6
Total under / (over) - recovery	67.2

1 In 2020 specifically, under-recoveries were related to the introduction of new
2 contracts that had not yet been included in rates, increases to transmission and gas
3 pipeline rates, and load below forecast, partially offset by higher than normal
4 wind and hydro generation.⁴¹ Table 2 below provides a comparison of 2020
5 power costs relative to those included in rates by resource type, and the impact of
6 load variance on baseline rate revenue.

³⁵ Variable coal fuel cost was higher than the amount included in rates due to fuel contract cost escalation. Docket UE-200398 Exh. PKW-1CT pages 17-18.

³⁶ During a February and March market event when market heat rates were low, PSE sold previously purchased gas and bought power in the market. Docket UE-200398 Exh. PKW-1CT page 18.

³⁷ Docket UE-200398 Exh. PKW-1CT page 18.

³⁸ During the February and March market event when market heat rates were low, PSE sold previously purchased gas and bought power in the market. Hydro and wind generation were below levels included in rates and contributed to higher market purchases. Docket UE-200398 Exh. PKW-1CT page 19.

³⁹ Cost of third-party transmission was higher than the amount included in rates due to rate increases that occurred after rates were established. Docket UE-200398 Exh. PKW-1CT page 20.

⁴⁰ Delivered load was below the level assumed when rates were established, contributing to the under-recovery. Docket UE-200398 Exh. PKW-1CT page 16.

⁴¹ Docket UE-210300 Exh. PKW-1CT pages 17-20.

Table 2: 2020 PCA Period Cost Recovery Summary	
Cost above / (below) rates	\$M
Coal ⁴²	(24.4)
Natural Gas Fuel and Transportation ⁴³	7.1
Long Term Contracts ⁴⁴	48.4
Market Purchases and Sales ⁴⁵	(4.6)
Transmission ⁴⁶	10.1
Other	4.4
Total Costs	41.0
Revenue (above) / below rates	
Load ⁴⁷	35.2
Total Revenue	35.2
Total under / (over) – recovery	76.1

1
2
3
4
5
6

Q. What new resources contributed to under-recoveries in 2020?

A. In the PCA annual filing for 2020, PSE attributed approximately \$14.0 million of 2020 under-recoveries to the new Energy Keepers PPA,⁴⁸ which had not yet been put into rates. Another \$26.1 million of under-recoveries was attributed to new contracts with Douglas PUD for output from the Wells hydroelectric project.⁴⁹

⁴² Closure of Colstrip Units 1 and 2 was not captured in 2017 general rate case rates, which were in effect for majority of 2020 PCA period. Docket UE-210300 Exh. PKW-1CT pages 16-17.

⁴³ Docket UE-210300 Exh. PKW-1CT page 17.

⁴⁴ Mid-C hydro fixed costs were significantly higher than amount included in rates. Addition of Energy Keepers PPA and contract rate escalation of Centralia PPA also contributed to the under-recovery. Docket UE-210300 Exh. PKW-1CT page 18.

⁴⁵ Docket UE-210300 Exh. PKW-1CT pages 19-20. Hydro and wind generation were above levels included in rates and contributed to lower market purchases.

⁴⁶ Cost of third-party transmission was higher than the amount included in rates due to rate increases that occurred after rates were established and additional 50 MW BPA transmission contract not captured in rates. Docket UE-210300 Exh. PKW-1CT page 20.

⁴⁷ Delivered load was 5% below level assumed in rates, contributing to the under-recovery. Docket UE-210300 Exh. PKW-1CT page 14.

⁴⁸ Docket UE-210300 workpaper NEW-PSE-PKW-WP 2020 PCA Variance Summary (C).xlsx / Contracts (C).

⁴⁹ Docket UE-210300 Exh. PKW-1CT pages 18-19.

1 **Q. What contract rate changes contributed to under-recoveries in 2019 and**
2 **2020?**

3 A. The Centralia coal PPA includes annual rate changes, but the baseline rate that
4 PSE charges to customers does not change annually. In the PCA annual filing for
5 2020 PSE attributed \$7.0 million of under-recoveries to this misalignment.⁵⁰ In
6 2019, a similar misalignment between the Centralia cost increase and baseline rate
7 changes resulted in a \$4.1 million under-recovery.⁵¹ In that case the cost increase
8 was more than offset by higher volumes associated with other contracts. As
9 discussed above, the PUDs update their projections of Mid-C contract costs
10 routinely, and variances between the actual costs and the levels assumed when the
11 baseline rate was established contributed to imbalances in both 2019 and 2020.

12 **Q. What changes to transmission and gas pipeline transportation rates**
13 **contributed to under-recoveries in 2019 and 2020?**

14 A. In the PCA annual filing for 2019, PSE indicated that third-party transmission
15 costs were \$4.1 million higher than the costs included in rates.⁵² In the PCA
16 annual filing for 2020, PSE indicated that purchased transmission costs were
17 \$10.1 million higher than the costs included in rates. Approximately \$7.9 million
18 of this variance was related to transmission rate increases, and \$2.2 million was
19 related to a new transmission contract that was not yet included in the baseline

⁵⁰ Docket UE-210300 Exh. PKW-1CT page 18.

⁵¹ Docket UE-200398 workpaper PKW-WP 2019 Variance Summary (C).xlsx.

⁵² Docket UE-200398 Exh. PKW-1CT page 20.

1 rate.⁵³ Increases in costs of upstream pipeline capacity related to pipeline rate
2 increases also contributed \$13.4 million of variances between actual costs and the
3 amount in rates in 2020.⁵⁴

4 **Q. How do load variances relative to forecast impact PCA imbalances?**

5 A. Load variances impact the PCA under- and over-recoveries in two ways, through
6 power costs and baseline rate revenue. If load is higher than projected, costs are
7 generally higher because more energy is required, and if load is lower than
8 projected costs are lower. At the same time, higher load results in more revenue
9 because the baseline rate is applied to higher retail sales volume, and the opposite
10 is true if load is below forecast. However, the cost and revenue variances do not
11 perfectly offset each other because the incremental cost associated with serving
12 more or less load depends on multiple factors, including market power and gas
13 prices, whereas the incremental revenue is simply the product of incremental load
14 times the variable baseline rate.

15 As indicated in the PCA annual filing for 2019 and presented in Table 1, the
16 variance in delivered load relative to the load forecast that was used to establish
17 the baseline rate contributed \$11.6 million of under-recoveries.⁵⁵ As indicated in
18 the PCA annual filing for 2020 and presented in Table 2, the variance in delivered

⁵³ Docket UE-210300 Exh. PKW-1CT page 20.

⁵⁴ Docket UE-210300 Exh. PKW-1CT page 17.

⁵⁵ Docket UE-200398 Exh. PKW-1CT page 16.

1 load relative to the load forecast that was used to establish the baseline rate
2 contributed \$35.2 million of under-recoveries.⁵⁶

3 **Q. How would PSE's proposed annual rate changes address the PCA under-**
4 **and over- recoveries that are related to load variances relative to forecast?**

5 A. The proposed annual rate changes would not address the impact of load variances
6 on power supply costs. The annual rate changes, as proposed, would address only
7 a portion of the revenue impact of load variances. The revenue impact can be
8 separated into two categories. One category is variances related to load forecast
9 error and the other is related to external factors such as weather. PSE updates its
10 load forecast annually. The proposed annual rate changes would allow for updates
11 to the most current load forecast during the annual process, and this would
12 mitigate the impacts of load forecast error on baseline rate revenue and therefore
13 PCA imbalances. The annual rate changes would not address the impact of
14 external factors such as weather on baseline rate revenue, and these impacts
15 would continue to flow through the PCA bands as originally intended.

16 **Q. Which of the other drivers of recent under-recoveries would be managed**
17 **with the proposed process for annual rate changes?**

18 A. Power cost under- and over-recoveries result from the interplay of multiple
19 factors relative to the costs that were projected when the baseline rate was
20 established. Some of the changes that produce variances are known in advance,

⁵⁶ Docket UE-210300 Exh. PKW-1CT page 13.

1 e.g., predetermined rate increases for the Centralia coal PPA. Some costs change
2 routinely even though the specifics might not be known in advance, e.g., fixed
3 costs of Mid-C hydro contracts and transmission rate increases. Some variances
4 result from the timing of new resources, e.g., the Energy Keepers PPA, which
5 started on March 1, 2020 but was not included in the costs that established the
6 baseline rate until July 1, 2021. Others are by their nature unpredictable and
7 dependent on market forces and weather, e.g., the costs of market purchases of
8 power and gas. The proposed process of annual changes to the variable baseline
9 rate would incorporate changes to the first three categories (variances that are
10 known in advance, routine, and timing-related) more quickly than the current
11 system does. The annual process would not eliminate under- and over-recoveries
12 that result from unpredictable weather and market forces that result in variances
13 related to load, power prices and gas prices relative to the costs included in the
14 variable baseline rate. However, the frequent updates allowed by the annual
15 process would mean that the forward natural gas prices used to project power
16 costs would be closer to the rate effective period, and the load forecast would
17 represent the most current load projections.

18 Markets and PSE's portfolio have changed since the inception of the PCA, and
19 the impacts of these changes are reflected in PCA imbalances. Annual rate
20 changes are needed so that costs are recovered through a baseline rate that
21 provides a reasonable estimate of costs rather than partially through customer
22 deferrals after the fact.

1 **IV. THE PROPOSED ANNUAL POWER COST UPDATE IS BETTER THAN**
2 **THE CURRENT SYSTEM**

3 **A. Annual Updates are Consistent with Practices in Neighboring States**

4 **Q. Do other states have similar processes to the annual power cost updates**
5 **proposed by PSE?**

6 A. Yes. Electric utilities regulated by the Oregon Public Utilities Commission
7 (“OPUC”) and the Idaho Public Utilities Commission (“IPUC”) have annual
8 update processes similar to that proposed by PSE.

9 In 2004, OPUC adopted an interim transition adjustment mechanism (“TAM”) for
10 PacifiCorp by Order No. 04-516, docketed as UM 1081.⁵⁷ The TAM is an annual
11 filing to update net variable power costs in rates and to set the transition
12 adjustments for customers who choose direct access during the open enrollment
13 window.⁵⁸

14 PacifiCorp filed an application with OPUC in 2012, docketed as UE 246, seeking
15 approval for a Power Cost Adjustment Mechanism (“PCAM”) to operate in
16 conjunction with the utility’s TAM, to collect or credit the differences between
17 actual net power costs and the forecasted net power costs approved in the TAM
18 and recovered in rates.⁵⁹ The Commission granted PacifiCorp’s request for a
19 PCAM with modification by Order No. 12-493.⁶⁰

⁵⁷ OPUC Order No. 07-446, p. 1, <https://apps.puc.state.or.us/orders/2007ords/07-446.pdf>.

⁵⁸ *Id.*

⁵⁹ OPUC Order No. 12-493, p. 8, <https://apps.puc.state.or.us/orders/2012ords/12-493.pdf>.

⁶⁰ OPUC Order No. 12-493, p. 1, <https://apps.puc.state.or.us/orders/2012ords/12-493.pdf>.

1 In 2006, Portland General Electric Company (“PGE”) filed an application with
2 OPUC for revised tariff schedules, docketed as UE 180. The application sought,
3 among other things, approval of an Annual Update tariff and an Annual Variance
4 tariff (also referred to as Power Cost Variance).⁶¹ By Order No. 07-015, the
5 OPUC adopted the Annual Update proposed by PGE with some exceptions,
6 stating “(I)t is important to update the forecast of power costs included in rates to
7 account for new information, e.g., on expected market prices for electricity and
8 natural gas, and for new PGE purchase power contracts.”⁶² Since 2006, PGE has
9 submitted annual PCAM forecasts through Annual Update tariff filings and
10 annual PCAM true-ups through Power Cost Variance filings.⁶³

11 In 1993, the IPUC approved Idaho Power’s implementation of an annual power
12 cost adjustment procedure in order to provide consistency and stability to rates by
13 Order No. 24806 issued in Case No. IPC-E-92-25.⁶⁴ An annual PCA application
14 includes the forecast of projected power costs based upon the most recent
15 Operating Plan; a true-up of last year’s forecasted costs to reflect actual costs; and
16 reconciliation of the prior PCA year true-up.⁶⁵

⁶¹ OPUC Order No. 07-015, p. 3, <https://apps.puc.state.or.us/orders/2007ords/07-015.pdf>.

⁶² OPUC Order No. 07-015, p. 18, <https://apps.puc.state.or.us/orders/2007ords/07-015.pdf>.

⁶³ See “Annual Rate Adjustments”, <https://www.oregon.gov/puc/filing-center/Pages/Key-Cases.aspx>.

⁶⁴ Idaho Power Application for IPUC Case IPC-E-20-21, p. 2, https://docs.idahopower.com/pdfs/AboutUs/RatesRegulatory/Filings/Application_PCA2020.pdf.

⁶⁵ IPUC Order No. 32552, p. 3, https://puc.idaho.gov/Fileroom/PublicFiles/ELEC/IPC/IPCE1217/OrdNotc/20120531final_order_no_32552.pdf.

1 **B. Annual Power Cost Updates are Consistent with the Implementation of**
2 **Annual Rate Changes in the Multiyear Rate Plan**

3 **Q. Is the plan to update power cost rates annually consistent with the multiyear**
4 **rate plan PSE proposes in this proceeding?**

5 A. Yes. The multiyear rate plan includes annual rate changes for other components
6 of PSE's rates, and the proposal for annual power cost updates is consistent with
7 that plan. The difference is that power costs are very dynamic and therefore
8 require frequent updates as the resource portfolio and market conditions change.
9 Please see the Prefiled Direct Testimony of Dr. Mark Newton Lowry, Exh. MNL-
10 1T, for a discussion of the use of multiyear rate plans in conjunction with
11 mechanisms for energy cost recovery.

12 **C. The Proposed Process Allows More Time for Review than Provided by the**
13 **PCORC Process**

14 **Q. How much time for review by parties would be allowed in PSE's proposed**
15 **annual schedule?**

16 A. PSE proposes to file its annual power costs by April 30 of each year and have a
17 rate effective date of January 1 of the following year. This provides eight months
18 for the Commission and other parties to review the proposed power costs. This is
19 more time than is allowed in the current PCORC process, which typically has a
20 six-month window from filing to rate effective date. It is less time than the eleven
21 months in the current general rate case process. However, in a general rate case,
22 parties have much more information to review because it is a full case including

1 the revenue requirement and rates for both electric and gas operations including
2 the cost of capital. The proposed eight-month window provides a reasonable
3 amount of time for a full review. Review of power costs for the purpose of
4 updating the baseline rate needs to be part of an annual routine.

5 **D. The PCA was Intended to Address Volatility in Load and Markets**

6 **Q. What will the role of the PCA be given PSE's proposed annual power cost**
7 **updates?**

8 A. The PCA will continue to serve the purpose for which it was originally intended
9 as described above:

- 10 • achieve an appropriate balance between risks to customers and
11 risks to utility shareholders;
- 12 • provide PSE incentives to control power costs;
- 13 • promote rate stability; and
- 14 • enhance PSE's financial stability by addressing concerns
15 associated with potentially volatile wholesale power markets and
16 fluctuations in hydropower availability due to uncertain weather
17 conditions.

18 In contrast, the PCA would not be used to absorb the costs of new resources that
19 have been placed in service but not yet gone through prudence review, known and
20 measurable changes to existing resources that have not made it into the baseline
21 rate due to unfortunate timing, or known changes to other variables that could
22 have been incorporated into the baseline rate with more timely power cost
23 updates.

1 **E. PSE would Still Have Incentive to Effectively Manage its Power Costs**

2 **Q. Would the proposed annual rate changes eliminate the need for the PCA?**

3 A. No. There will still be volatility in weather and markets, and the impacts of this
4 volatility will continue to flow through the PCA. PSE's ability to manage its
5 power costs in the face of this volatility will impact PSE's earnings.

6 **Q. Which costs belong in the PCA bands and which belong in the baseline rate?**

7 A. PSE needs to return to using the PCA for its intended purpose, to share with
8 customers the impacts of weather and market related variability of power costs,
9 and get away from using the PCA for sharing with customers the cost of new
10 resources or known and measurable changes to the costs of existing resources.

11 **V. SUMMARY OF PSE'S PROPOSAL**

12 **Q. What is PSE's proposal in this proceeding?**

13 A. PSE proposes that the PCORC be amended to provide for updates to the costs that
14 are included in the fixed portion of the PCA baseline rate, and that it be
15 complemented with a system of annual updates to the costs that are included in
16 the variable portion of the baseline rate. This limit on the PCORC would be
17 implemented only if the Commission approves the system of annual power cost
18 updates. The annual updates would result in annual January 1 changes to the
19 variable portion of the baseline rate and annual changes to the deferral rate on
20 October 1. PSE would file PCORCs when updates to fixed production costs
21 require rate changes.

1 **Q. Please summarize why these two mechanisms are necessary.**

2 A. These mechanisms are necessary because 1) PSE is required by law and resource
3 adequacy requirements to add large amounts of generation capacity to its portfolio
4 in the next ten years, 2) customers need proper price signals so they can make
5 informed decisions about energy consumption and conservation, and 3) the
6 general rate case process is too lengthy to allow for new resources to be included
7 in customer rates when they become operational and for known and measurable
8 updates to existing costs to be timely included in customer rates.

9 **Q. What other evidence supports PSE's proposal?**

10 A. The Commission has already ruled that the PCORC should be retained for reasons
11 that are even more relevant today than they were when that order was issued in
12 2009—timely consideration of new resources and reduction of market reliance.
13 Neighboring states recognize the challenges of aligning customer rates with
14 power costs and have had similar processes for annual rate changes in place for
15 several years.

16 As indicated earlier in my testimony, the Commission has stated that “one
17 objective of a new resource proceeding is to have the new Power Cost Rate in
18 effect by the time the new resource would go into service.” The Commission has
19 also established the precedent that power costs in rates should be set as closely as
20 possible to costs that are reasonably expected to be actually incurred:

21 We resolve the philosophical question raised by ICNU in favor of
22 the practical conclusion that power costs determined in general rate

1 proceedings and in PCORC proceedings should be set as closely as
2 possible to costs that are reasonably expected to be actually incurred
3 during short and intermediate periods following the conclusion of
4 such proceedings.⁶⁶

5 The recent PCA under-recoveries and the misalignment of resource additions and
6 expirations illustrated above provide evidence that the current system is
7 inadequate to comply with these Commission directives to align customer rates
8 with actual prudently-incurred costs, especially in light of future resource
9 changes.

10 **Q. What is the benefit to customers of PSE's proposal?**

11 A. PSE customers and residents of Washington have made it clear with the passage
12 of CETA that they expect clean energy. The plans to acquire additional non-
13 emitting resources presented in PSE's IRP and Clean Energy Implementation Plan
14 signify PSE's commitment to complying with those customer expectations and
15 the law. PSE's proposal for a comprehensive process to incorporate the changing
16 resource portfolio into both the fixed and variable portions of the baseline rate
17 aligns customer charges with the service customers expect.

18 **Q. If the Commission declines to approve PSE's proposed process of annual rate**
19 **changes, what alternative do you recommend?**

20 A. Should the Commission decline to approve PSE's proposal for a system of annual
21 baseline rate changes to complement use of the PCORC for fixed production

⁶⁶ *WUTC v. Puget Sound Energy*, Dockets UE-111048 & UG-111049, Order 08 (May 7, 2012) at n. 303.

1 costs, the existing PCORC option should remain in place as it exists today for
2 both fixed production costs and variable power costs, for all of the reasons
3 presented above.

4 **VI. CONCLUSION**

5 **Q. Does that conclude your prefiled direct testimony?**

6 A. Yes, it does.