BEFORE THE WASHINGTON UTILTIES AND TRANSPORTATION COMMISSION

AIR LIQUIDE AMERICA CORPORATION, AIR PRODUCTS AND CHEMICALS, INC., THE BOEING COMPANY, CNC CONTAINERS, EQUILON ENTERPRISES, LLC, GEORGIA-PACIFIC WEST, INC., AND TESORO NORTHWEST COMPANY Complainants, v. PUGET SOUND ENERGY, INC. Respondent.	Docket No. UE-001952 (consolidated) PUBLIC COUNSEL PREHEARING MEMORANDUM
IN RE: PETITION OF PUGET SOUND ENERGY, INC. FOR AN ORDER REALLOCATING LOST REVENUES RELATED TO ANY REDUCTION IN THE SCHEDULE 48 OR G-P SPECIAL CONTRACT RATES	Docket No. UE- 001959 (consolidated)

I. INTRODUCTION

1. Public Counsel does not address all the legal issues listed in the Commission's December 18, 2000, Prehearing Conference Order,[1] but will instead focus in this memorandum on the issues of particular importance to Puget Sound Energy's (PSE's) core customers. [2] Those issues are: (1) May the Commission approve any relief for the Schedule 48 and special contract customers which shifts cost recovery responsibility to "core customers?"; (2) Is the PSE petition for deferred accounting consistent with the Schedule 48 order or the merger rate plan?; (3) Does the Commission have the authority to adopt a rate cap proposal for Schedule 48 customers?; (4) Should the Commission grant the complainants' request that they be allowed to return to a

[1] Order Consolidating Proceedings; Prehearing Conference Order and Notice of Hearing, December 18, 2000, pp. 3-4.

[2] While not set out in precisely the same form, Public Counsel believes the issues addressed are within the scope of those listed in the prehearing order, the industrial customers' complaint and the PSE petition.

Office of the Attorney General
Public Counsel Section
900 4th Ave. Suite 2000
Seattle, WA 98164
(206) 464-7744

tariffed rate such as Schedule 49?; and (5) What is the minimum action the Commission should take to address the situation, in the event it finds that an emergency exists?

II. DISCUSSION

A. The Schedule 48 Order Provides A Guarantee Against Cost Shifting to Core Customers.

2. The complainants in this case, with the exception of Georgia-Pacific, which is served by a special contract, receive service from PSE under the terms of Schedule 48. The adoption of Schedule 48 was integrally related to the merger between Puget Sound Power & Light (Puget) and Washington Natural Gas and was initially proposed by Puget as a part of a "market transition plan" intended to provide customers with the option of accessing competitively-priced supplies of electric energy.[3]

3. Public Counsel opposed approval of Schedule 48 at open meeting, recommending instead that the Commission suspend the filing and conduct hearings on a number of issues including economic viability of the bypass threat; the costs and benefits associated with Schedule 48 and open access generally; and the cost based pricing of Schedule 48.[4]

4. At its October 9, 1996 open meeting, the Commission approved Schedule 48 with seven conditions developed by Commission Staff in consultation with Puget. The first condition related to cost shifting, and stated in its entirety:

> (1) No cost shifting – The revenue difference between Schedule 48 rates and the effective tariff rates that would otherwise be applicable to current Schedules 31, 46, 49, or special contract customers (*i.e.*, lost revenues), shall not be shifted to other customer classes and shall be borne by shareholders until a future Commission determination regarding allocation of costs and cost savings, and then on a prospective basis only.[5]

The company expressed concurrence with the conditions at the open meeting. The import of this provision was further clarified and emphasized in the order. The Commission expressly

[3] *Washington Utilities and Transportation Commission v. Puget Sound Power & Light Company*, Docket No. UE-960696, Commission Order Approving Schedule 48 With Conditions (October 30, 1996), p. 1 ("Schedule 48 Order").

[4] Id., p. 4, n. 3.

[5] Schedule 48 Order, p. 5.

Office of the Attorney General
Public Counsel Section
900 4th Ave. Suite 2000
Seattle, WA 98164
(206) 464-7744

referenced Puget's written comments in the proceeding which had addressed Public Counsel's concern about cost shifting:

> Public Counsel states that 'if some classes get reduced rates, the clear implication is that others will be asked to pay more.' Public Counsel's conclusion is not correct. As noted in our initial comments, we *guarantee* that other classes will not pay more as a result of Schedule 48. [quoting Puget July 29, 1996, letter, p. 6][6]

The Commission expressly concurred in this interpretation of the schedule's effect, stating:

> Public Counsel believes this commitment is what the Company and the Commission Staff have agreed upon, and that both parties believe that this commitment is captured in the language of condition "(1)" above. *We concur with this assessment and affirm the reading of the language of condition (1), and accept the Company's "guarantee."*[7]

There is simply no room for doubt or ambiguity. When Schedule 48 was adopted, residential and other core customers of Puget were given a "guarantee" that they would not be responsible for any revenues lost to the Company as a result of the adoption of the schedule.[8] Accordingly, the Commission may not adopt or approve in this proceeding any relief for industrial customers which results in any shift of revenue responsibility to PSE's general body of ratepayers. As noted above, the order expressly states, in the first "condition" that lost revenues shall be borne by shareholders.

5. Later in the order, discussing pricing, the Commission again affirmed the protection afforded core customers:

> Such pricing [Schedule 48 rates based on market prices] does not harm other customers so long as the prohibition against cost shifting in condition "(1)" above is preserved. Schedule 48, as long as it remains compensatory, keeps the companies largest volume customers on its system and contributing to joint costs.[9]

More recently, the Commission reaffirmed this protection in its order approving a settlement of a Schedule 48 dispute, stating:

---

[6] Id., p. 7.
[7] Id. (emphasis added).
[8] The Schedule 48 order makes clear that this guarantee also applies to special contract customers such as Georgia Pacific.
[9] Schedule 48 Order, p. 10.

Office of the Attorney General
Public Counsel Section
900 4th Ave. Suite 2000
Seattle, WA 98164
(206) 464-7744

> We emphasize that this condition [no cost shifting], along with the others established by the Commission's order approving Schedule 48, remains effective.[10]

As a first principle in this case, therefore, the Commission must continue to preserve as fully effective the prohibition against cost shifting.

6. Finally, it is worth remembering that the concern over lost revenues at the time Schedule 48 was approved arose from "the revenue difference between Schedule 48 rates and the effective tariff rates that would otherwise be applicable[.][11] It was anticipated that Schedule 48 customers might be able to acquire power at rates lower than these tariffed rates, as in fact they did in the early years, saving millions of dollars, and depriving PSE of revenues. That was a risk to Puget and a benefit to Schedule 48 customers. Conversely, there was also a risk that the industrial customers would pay more in the market than they would have under tariff. This was a risk to the Schedule 48 customers but a *benefit* to Puget. Under current circumstances, therefore, we are nowhere even within hailing distance of the "lost revenue" scenario feared in the initial order. Instead we are at the other end of the spectrum where Puget is gaining revenue, and indeed revenues far greater than anticipated. The industrial customers are paying far more than tariffed rates, so there is effectively no "lost revenue" to be shifted so long as PSE Schedule 48 rates cover PSE's cost to serve the industrial customers.

7. Under Schedule 48 Puget accepted risk; the Schedule 48 customers accepted risk. The level of risk to the customers (and benefit to Puget) turned out to be vastly different than was anticipated at the time of the adoption of Schedule 48. We concur with Complainant's assertion that the "expected" range of power costs was less than ten cents per kilowatt-hour.

B. The Deferred Accounting Mechanism Sought In The PSE Petition Violates Both The Schedule 48 Guarantee And The Rate Plan. Deferred Accounting Should Not Be Approved Unless It Expressly Insulates Core Ratepayers From Any Revenue Recovery.

8. PSE may not, through a deferred accounting mechanism, seek to recover from core ratepayers those revenues lost as a result of relief granted to Schedule 48 customers. As set forth

[10] *WUTC v. Puget Sound Energy*, Docket No. UE 981238, Seventh Supplemental Order, p. 5.
[11] Schedule 48 Order, p. 5, condition (1).

Office of the Attorney General
Public Counsel Section
900 4th Ave. Suite 2000
Seattle, WA 98164
(206) 464-7744

above, the approval of such a mechanism with the express or implied possibility of later recovery from core ratepayers would be directly at odds with the foundation of the first condition for the adoption of Schedule 48 – no cost shifting. The first "condition," by its express terms, precludes retroactive recovery of lost revenue, stating that lost revenue is to be borne by shareholders "until a future Commission determination regarding allocation of costs and cost savings, *and then on a prospective basis only*."[12] Presumably, PSE's intent is that amounts would be booked to the deferred account on an ongoing basis and that at some future date, those amounts would be allocated to the appropriate customer class. Any shift of costs, however, must be based only upon a finding that revenue *loss* to PSE is unavoidable, and then only allow *future* revenue loss to be recovered from other classes. Since there is no revenue loss here, only a possible constraint of revenue gain, there is no loss to reassign.

9. More importantly, and equally unambiguously, Puget's deferred accounting proposal also runs afoul of the rate plan adopted in the settlement of the Puget/Washington Natural Gas Merger.[13] If a deferred account is created, any recovery from core customers of amounts booked to that account during the period of the rate plan would have the effect, retroactively, of increasing the core customers' rates above the plan level. The rate plan fixes core customer tariffed rates to a set schedule of changes through the year 2001.[14] As the stipulation states:

> Commencing on the date of merger approval and continuing through December 31, 2001 (the "Rate Plan Period"), changes in PSE's electric and natural gas rates *shall only be as provided in Section III.A [Rate Plan] herein.*[15]

The only exceptions or "carve outs" are expressly named. Nowhere in the body of the Commission's order[16] or in the underlying stipulation which it approved[17] is there provision for a "carve out" to the agreed rates based on deferred accounting for unspecified future events.

---

[12] Id., p. 5 (emphasis added).

[13] *In the Matter of the Application of Puget Sound Power & Light Company and Washington Natural Gas Company for An Order Authorizing Merger*, UE-951270, UE 960195 (consolidated), Fourteenth Supplemental Order Accepting Stipulation; Approving Merger, February 5, 1997 ("Merger Order").

[14] Id., Appendix A (Stipulation), Exhibit A (Summary of Electric Rate Changes).

[15] Id, p. 4 (emphasis added).

[16] Merger Order, pp. 21-23

[17] Merger Order, Appendix A (Stipulation), pp. 4-11.

Office of the Attorney General
Public Counsel Section
900 4th Ave. Suite 2000
Seattle, WA 98164
(206) 464-7744

10. For these reasons, PSE's petition, as framed, cannot be granted. The Commission may only approve a deferred accounting mechanism if it makes clear that any amounts deferred under this mechanism cannot be recovered from core ratepayers.

C. The Commission Has The Requisite Authority To Adopt The "Soft Cap" Proposed By Public Counsel.

11. In its Initial Response filed in these dockets, Public Counsel proposed a rate cap of some reasonable level, to be imposed in the event that the Commission was persuaded that an emergency existed that warranted immediate relief. In its outline form, the proposal provided that, in order to avoid accruing potential liabilities for other ratepayers, or unduly harming PSE, such a cap would be in place during times when PSE was not actually purchasing energy in the wholesale market. At times when PSE could demonstrate it actually faced generation or market prices above the cap, it would be allowed to pass those prices on to Complainants on a pro rata basis of their loads to PSE purchase.[18] It is Public Counsel's understanding that Commission Staff is also planning to present a "soft cap" proposal along with its January 4 legal memorandum. Public Counsel expects to support the proposal.

12. A "soft cap" is a permissible form of relief in the event that the Commission determines that an emergency exists which warrants some relief under RCW 34.05.479. The underlying complaint asks the Commission to establish a fair, just and reasonable rate for complainants. The Commission has general authority to entertain such complaints, RCW 80.28.020, and has a general duty under its enabling act to establish fair rates. RCW 80.01.040(3). Thus, it is within the Commission's authority, after a full complaint proceeding, to establish a rate for service to the industrial customers to be calculated in the manner proposed by Staff and Public Counsel. In an emergency adjudicative proceeding under RCW 34.05.479, therefore, the Commission may grant the same relief, so long as it makes a brief statement of its factual findings and conclusions of law, as well as the basis of its determination that an emergency exists. RCW 34.05.479(3). Following the grant of emergency relief, the Commission would then proceed as quickly as

[18] Initial Response of Public Counsel, pp. 3-4.

Office of the Attorney General
Public Counsel Section
900 4th Ave. Suite 2000
Seattle, WA 98164
(206) 464-7744

feasible to complete a full complaint proceeding. RCW 34.05.479(5). Likewise, as to the issue of sufficiency of the rate under RCW 80.28.020, the Commission can make a preliminary finding on that issue in the emergency hearing, and examine the question in more detail subsequently in the full complaint case.

13. Neither does the "soft cap" proposal violate the terms of the merger rate plan. As discussed above, the merger rate plan applies to core customer tariffed rates. The text of the stipulation describes the "general rate changes" permitted, the schedules and customer classes affected and the manner in which the adjustments will be collected. The only reference to Schedule 48 is in the provision that annual adjustments will be collected from the "non-energy portion of Schedule 48."[19] Exhibit A to the Stipulation, Appendix A to the Merger Order, contains a table showing all the tariff schedules which are subject to the rate plan, together with the agreed rate changes over the life of the plan. Schedule 48 is not listed on the exhibit. Schedule 48 rates for non-core customers are outside the ambit of the plan. This makes sense. The purpose of the rate plan was to provide a five-year period of certainty to core customers and to allow the company an opportunity to achieve merger savings.[20]

14. Moreover, in approving Schedule 48, the Commission observed that "so long as [Schedule 48] remains compensatory" it preserves other customers from harm, keeps the largest customers on the system, and contributes to joint costs.[21] In supporting adoption of Schedule 48, PSE maintained that Schedule 48 rates are compensatory, covering the fully embedded cost of non-power services as well as the costs of incremental non-firm market priced energy. There is nothing in the "soft cap" proposal of Public Counsel that would render the Schedule 48 rate non-compensatory.

[19] Merger Order, Appendix A (Stipulation), p. 6.

[20] Id., App. A, p. 4. Public Counsel, in the early stages of the merger, had expressed concern that reductions in industrial rates *below* tariffed levels would drive up residential rates. Id., p. 9. The rate plan addressed that concern.

[21] Id., p. 10.

Office of the Attorney General
Public Counsel Section
900 4th Ave. Suite 2000
Seattle, WA 98164
(206) 464-7744

15. Finally, it is worth noting that the rate plan does not leave PSE completely exposed to financial risk. The rate plan makes express provision that should the necessity arise, the company can avail itself of the right to request interim rate relief:

> During the Rate Plan Period, PSE may seek, under appropriate circumstances, interim rate relief. The Commission adopted a six-part standard for interim rate relief in *WUTC v. Pacific Northwest Bell Telephone Company,* Cause No. U-72-30, Second Supplemental Order (October 1972). The *Pacific Northwest Bell* standard has been consistently reaffirmed in several Commission decisions since 1972.[22]

The stipulation goes on to describe the procedure for seeking interim relief. Thus, while Public Counsel does not believe that the "soft cap" would place PSE in such a position, the rate plan does provide a mechanism for PSE to obtain relief if circumstances warrant. Public Counsel recognizes the risk of interim relief and proposes that any interim relief ordered during the rate plan period apply initially to Schedule 48 customers, until their rates are equal to those under the current form of Schedule 48, and only if that level of relief is not sufficient to meet the financial needs of the Company, then to all customers.

D. The Complainants May Not Return To Tariffed Rates.

16. Complainants' request that they be allowed to return to tariffed rates such as Schedule 49 as at least an interim solution. Public Counsel opposes this proposed remedy. Schedule 48 does not make provision for the Complainants to return to tariffed service at this time. The schedule states:

> At the expiration of the term of the Service Agreement, Customer may commence taking service under any retail tariff providing firm service; however, the Customer understands and acknowledges that such service may be subject to payment by such Customer of any long-run resource costs and any incremental capacity costs (which costs are not intended by the Company and Customer to constitute an exit fee) incurred by the Company to provide service. (Original Tariff Sheet 48-E)

The term of Schedule 48 is not yet complete, thus there is no mechanism in place by which the customers can return to Schedule 49, or indeed any tariff. Should the Commission consider such

[22] Id., Appendix A, pp. 10-11.

Office of the Attorney General
Public Counsel Section
900 4th Ave. Suite 2000
Seattle, WA 98164
(206) 464-7744

a mechanism in these proceedings, it should include compensatory payments sufficient to ensure that there is no harm to other customers.

17. Returning to tariffed rates has other problems. As we noted in our Initial Response, Schedule 49, the standard industrial tariff which these customers abaondoned, is below cost. As of the time of PSE's last general rate case, UE-921262, Schedule 49 provided only 88% of its allocated revenue requirement. (PSE Response to Bench Request 515E, UE-921262). There is no reason to believe that this situation has changed. Such a below-cost rate cannot be employed as a safe-haven for Complainants without increasing the risk to all ratepayers of cost-shifting. Puget's other customers should not subsidize those industrial customers who chose to leave the tariffed rate. In ordering emergency relief under this complaint, the Commission is required by RCW 80.28.020 to make a finding that the interim rate is sufficient, as well as fair, just and reasonable. It is unlikely the record would support such a finding here if these industrial customers were placed on Schedule 49.

E. The Minimum Action The Commission Must Take To Address The Emergency Situation.

18. In the event the Commission determines that an emergency exists pursuant to RCW 34.05.479, the statute limits the agency to "only such action as is necessary to prevent or avoid the immediate danger[.]" RCW 34.05.479(2). The primary alternatives before the Commission are the complainants requested return to tariffed rates and the proposed rate caps. Public Counsel would suggest that, as between the two, the rate cap is the minimally intrusive approach. While the "soft cap" proposal moderates the impact of the indexed rates, in overall structure it continues to adhere to the general framework of Schedule 48. Its primary impact is to attempt to eliminate the worst effects of the unprecedented volatility of wholesale market. It continues to allow PSE to earn significant net revenues from Schedule 48 customers, over and above the cost of providing service. While it limits the exposure of the industrial customers, it does not simply put them back on tariffed rates, but continues to subject to them to a degree of risk as originally contemplated by Schedule 48. The Commission may also observe the limitation expressed in the

Office of the Attorney General
Public Counsel Section
900 4th Ave. Suite 2000
Seattle, WA 98164
(206) 464-7744

statute by imposing any emergency remedy for a limited time period only, on an interim basis, pending further proceedings in the docket.

III. CONCLUSION

19. For the foregoing reasons, Public Counsel urges the Commission to preserve the Schedule 48 guarantee and refrain from approving any relief for the Schedule 48 and special contract customers which shifts cost recovery responsibility to "core customers". In the event that the Commission determines that any emergency relief is warranted, Public Counsel recommends that the Commission consider imposition of the "soft cap" to be proposed in more detail at the evidentiary hearing. We believe this mechanism will address any emergency the Commission determines may exist, and will prevent deterioration of Puget's financial condition below acceptable levels.

Dated this 4th day of January, 2001.

CHRISTINE GREGOIRE
Attorney General of Washington

_____
Simon J. ffitch
Assistant Attorney General
Public Counsel

Office of the Attorney General
Public Counsel Section
900 4th Ave. Suite 2000
Seattle, WA 98164
(206) 464-7744