

**EXHIBIT NO. \_\_\_\_ (GSS-1T)  
DOCKET UE-161123  
PSE SCHEDULE 451  
WITNESS: GARY S. SALEBA**

**BEFORE THE  
WASHINGTON UTILITIES AND TRANSPORTATION COMMISSION**

**WASHINGTON UTILITIES AND  
TRANSPORTATION COMMISSION,**

**Complainant,**

**Docket No. UE-161123**

**v.**

**PUGET SOUND ENERGY,**

**Respondent.**

**PREFILED DIRECT TESTIMONY OF GARY S. SALEBA  
ON BEHALF OF MICROSOFT CORPORATION**

**October 12, 2016**

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1 **I. INTRODUCTION**

2 **Q. Please state your name and business address.**

3 A. My name is Gary S. Saleba. I am the CEO and President of EES Consulting, Inc.  
4 My business address is 570 Kirkland Way, Suite 100, Kirkland, Washington  
5 98033.

6 **Q. Please describe your background and experience.**

7 A. I hold an MBA in Finance from Butler University and a BA in Economics and  
8 Mathematics from Franklin College. I am a founder of EES Consulting, Inc.  
9 (EES). I have over 30 years of experience working in the utility industry and  
10 have managed projects related to resource planning, contract negotiations,  
11 mergers and acquisitions, financing, rates studies, operational prudence and  
12 strategic planning. I have considerable experience appearing as a subject matter  
13 expert in various jurisdictions that include numerous utility commissions and  
14 provincial tribunals, the Federal Energy Regulatory Commission, National Energy  
15 Board and numerous courts of law. I have testified over 100 times as a subject  
16 matter expert on utility matters. A further description of my educational  
17 background and work experience can be found in Exhibit (GSS-2) attached to this  
18 testimony.

19 **Q. On whose behalf are you appearing in this proceeding?**

20 A. I am testifying on behalf of Microsoft Corporation (Microsoft).

21 **Q. What is the purpose of your testimony?**

22 A. Microsoft desires to purchase its power supply from a third party vendor and no  
23 longer take power supply service from Puget Sound Energy (PSE). As outlined

1 by Witness Irene Plenefisch, Microsoft and PSE have agreed to an arrangement to  
2 facilitate the transfer of Microsoft’s power supply service to a non-PSE supplier  
3 with the understanding that Microsoft will (1) pay an “exit fee” to PSE and its  
4 remaining customers in the amount of about \$23.7 million; and (2) continue to  
5 pay PSE for the transmission and distribution services provided to Microsoft by  
6 PSE under PSE’s Schedule 451. *See* Exhibit No. \_\_\_(IP-1T). My testimony  
7 opines on the reasonableness of this \$23.7 million exit fee payment.

8 **Q. How is your testimony organized?**

9 A. My testimony is organized as follows:

- 10 • Background on exit fees
- 11 • Precedents for exit fees
- 12 • Summary of PSE’s proposed exit fee
- 13 • Critique of PSE’s proposed exit fee
- 14 • Impacts of using a more standard exit fee construct
- 15 • Summary observations and conclusions

16 Each of these major sections is discussed below.

17 **II. BACKGROUND ON EXIT FEES**

18 **Q. What is an “exit fee”?**

19 A. An exit fee is a term of art in utility regulation which has been defined and refined  
20 over the past three decades.

21 With the advent of open access and customer choice within the utility industry,  
22 there are often times options for an existing customer to no longer take power

1 supply service from the incumbent utility and to begin purchasing power supply  
2 from a third-party vendor. Under this arrangement, the incumbent utility  
3 continues to provide transmission and distribution services to the customer but  
4 allows the customer to purchase its power supply services from another supplier.  
5 As part of the regulatory construct which allows power purchases from a third  
6 party, the incumbent utility collects or credits the departing customer an “exit fee”  
7 in an amount that keeps the remaining customers financially indifferent or “held  
8 harmless” from the actions of a customer taking power supply from a non-  
9 incumbent supplier. This payment or credit is set so that the remaining customers  
10 will be no better off and no worse off with respect to the costs of supporting the  
11 incumbent utility’s existing power supply assets when a customer elects to no  
12 longer take power supply service from the incumbent utility.

13 **Q. Why is an exit fee being paid by Microsoft?**

14 A. PSE has determined that Microsoft buying its power supply from a non-PSE  
15 supplier will result in net costs to remaining PSE customers of approximately  
16 \$23.7 million over the first 5 years of this transition as the result of foregone  
17 revenue that Microsoft would have contributed to supporting PSE’s current costs  
18 of supplying power, which is in excess of PSE’s reduced costs. In order to hold  
19 harmless PSE’s remaining customers over these first 5 years, PSE proposes  
20 Microsoft should pay this \$23.7 million net cost as an exit fee.

21 **Q. After Microsoft begins purchasing its power supply from a non-PSE source,**  
22 **will Microsoft pay other charges to PSE?**

1 A. Yes. Microsoft will continue to pay PSE under Schedule 451 – Large Customer  
2 Retail Wheeling. Under Schedule 451, Microsoft will pay PSE for all of the costs  
3 associated with using PSE’s transmission and distribution facilities plus riders that  
4 cover such things as conservation services, low income programs, property taxes,  
5 expedited rate filings and revenue decoupling adjustments.

6 **Q. Have you been involved in the calculation of exit fees before?**

7 A. Yes. I have actively participated in calculating appropriate exit fees in numerous  
8 jurisdictions over the past three decades representing both departing customers  
9 and the incumbent utilities.

10 **III. PRECEDENT FOR EXIT FEES**

11 **Q. Is there regulatory precedent for calculating exit fees?**

12 A. Yes. Many state, federal and provincial utility regulators that allow customers to  
13 purchase power supply services from a third-party or offer “open access” have  
14 gone through the exercise of calculating exit fees. These jurisdictions have  
15 adjudicated exit fees for customers that wish to purchase their power supply  
16 service from a supplier other than the incumbent utility.

17 **Q. Are there specific regulatory forums that are well known for the calculation**  
18 **of an exit fee?**

19 A. Yes. The western states have been front-runners in this exercise including  
20 California, Nevada, and Oregon. The Federal Energy Regulatory Commission  
21 (FERC) has also been a lead in calculating exit fees. The FERC Order 888-A is  
22 considered by most as providing appropriate guidance in the calculation of these  
23 exit fees.

24 **Q. Is there a standard method for calculating exit fees?**

1 A. No. Exit fees are always situation-specific but they all generally embrace the  
2 higher principle of holding harmless remaining customers from the financial and  
3 rate impacts of departing customers who no longer take power supply services  
4 from the incumbent utility and will therefore no longer contribute to costs  
5 associated with the utility's existing power supply assets, which were acquired by  
6 the utility to serve the larger (pre-departure) customer load.

#### 7 IV. SUMMARY OF PSE'S PROPOSED EXIT FEE

8 **Q. What is your understanding of PSE's proposed exit fee if Microsoft**  
9 **purchases its power supply from a non-PSE source?**

10 A. The details of PSE's proposed exit fee for Microsoft are contained in Witness Jon  
11 A. Piliaris's testimony. In summary, PSE proposes to collect the net present value  
12 (NPV) of the difference between (a) the power supply revenues PSE would have  
13 collected from Microsoft if Microsoft continued to purchase power supply service  
14 from PSE and (b) the amount of reduced PSE power supply expenses that are  
15 realized by not having to provide Microsoft with this power supply service. This  
16 NPV is aggregated over the first five years after Microsoft begins purchasing  
17 power supply from a non-PSE source. The end result of this PSE proposal is an  
18 exit fee for Microsoft of approximately \$23.7 million.

#### 19 V. CRITIQUE of PSE'S PROPOSED EXIT FEE

20 **Q. Have you reviewed the input assumptions associated with PSE's proposed**  
21 **exit fee for Microsoft?**

22 A. Yes. I have.

23 **Q. Is it your opinion that PSE's proposed exit fee is the amount necessary to**  
24 **hold remaining ratepayers harmless?**

1 A. No. My review of PSE's proposed exit fee reveals that it is in excess of the  
2 amount needed to hold PSE's remaining customers harmless if Microsoft  
3 purchases its power supply from a non-PSE source.

4 **Q. Why do you opine that PSE's proposed exit fee is in excess of what is needed**  
5 **to hold PSE's remaining customers harmless?**

6 A. I find two assumptions that are in conflict with the principle that the proposed exit  
7 fee's objective is to hold PSE's remaining customers financially harmless. These  
8 inappropriate assumptions are:

- 9 • The analysis period should extend beyond five years for the forecast of the  
10 NPV difference in rate revenues from Microsoft and the reduced PSE  
11 power supply expenses.
- 12 • The assumed value of reduced PSE power supply costs attributable to  
13 Microsoft taking power from a non-PSE supplier is too low.

14 Taken in total, correction of these two inappropriate assumptions will result in a  
15 net benefit to PSE's remaining customers if Microsoft purchases its power supply  
16 from a non-PSE source.

17 **Q. Can you explain why the forecast period should be beyond five-years?**

18 A. Yes. The theory behind an exit fee is that the net costs/benefits associated with an  
19 existing customer taking power supply service from a third party should be  
20 analyzed over the remaining useful lives of the assets at issue. Once the affected  
21 assets at issue are fully depreciated or obsolete, the costs/benefits associated with  
22 a departing load on these assets become a moot issue. In this case, the assets at  
23 issue are only PSE's power supply assets as all costs related to PSE transmission



1 and distribution assets are covered under the rates paid to PSE by Microsoft under  
2 Schedule 451.

3 In reviewing the PSE power supply assets, the remaining useful lives of these  
4 assets are much more than five years. Based on data included in PSE's 2015  
5 FERC Form 1, dated April 14, 2016, the average remaining useful life of PSE's  
6 generating assets is at least 20 years. Additionally, an initial review of PSE's  
7 power supply portfolio indicates that they have roughly 20 years of depreciation  
8 associated with them. As such, the remaining useful lives for these same power  
9 supply assets are at least 15-20 years, and a 15 – 20-year period of analysis of the  
10 relative costs/benefits of Microsoft no longer taking power supply service from  
11 PSE is a much more appropriate period of analysis.

12 **Q. What effect does extending the period of analysis for the calculation of a**  
13 **Microsoft exit fee have on PSE's proposed exit fee?**

14 A. Based upon its most recently filed Integrated Resource Plan (IRP), PSE is power  
15 supply surplus until Colstrip 1 and 2 are retired. Once Colstrip 1 and 2 are retired,  
16 PSE goes power supply deficit and must replace this lost generation output with  
17 more expensive power supply options. By terminating power supply service from  
18 PSE, Microsoft's procurement of power from a non-PSE source allows PSE to  
19 avoid purchasing or building a corresponding amount of new power supply  
20 resources which saves the remaining PSE customers a considerable amount of  
21 money. For example, termination of Colstrip 1 and 2 costs PSE at least \$20  
22 million per year in power supply expense. These savings continue through the  
23 term of the exit fee analysis. Thus, extending the exit fee analysis period to match

1 the remaining useful life of PSE's current power supply resources more  
2 accurately and fairly calculates the value to remaining PSE customers of  
3 Microsoft taking power supply service from a non-PSE source and results in net  
4 benefits to the fully-bundled PSE customers remaining after Microsoft has moved  
5 its Schedule 40 load onto Schedule 451.

6 **Q. What is the next assumption made in the proposed PSE exit fee calculation**  
7 **for Microsoft that you find inappropriate?**

8 A. The next assumption which is inappropriate is the value to PSE of Microsoft not  
9 taking PSE power supply services. In its exit fee analysis, PSE assumes that the  
10 power supply freed up by Microsoft's use of Schedule 451 will be used to reduce  
11 PSE's purchases of power supply for its remaining customers. However, the  
12 Schedule 40 power supply product purchased by Microsoft from PSE is a firm,  
13 load-following product with all the necessary ancillary services (i.e., schedule,  
14 dispatch, balancing and reactive power services). If PSE sold the power freed up  
15 by Microsoft on the open market as a firm load-following product, PSE would  
16 realize a price for that power that exceeds the value to PSE of reducing its  
17 purchases of power supply by an equivalent amount. As such, PSE should  
18 assume a higher value for the power not being sold to Microsoft. It would be  
19 more appropriate to assume this product's wholesale market value equals a 50  
20 MW block of a load-following product with all ancillary services. A description  
21 of the BPA Tier 1 product, which would be a low cost proxy for such a power  
22 supply product, can be found in Exhibit No. \_\_\_(GSS-3) attached to this  
23 testimony. My initial research indicates a 4-year load following power supply

1 product such as the BPA Tier 1 product would garner a value near 35 percent  
2 higher than the value PSE has attributed to this surplus power supply in the  
3 calculation of PSE's exit fee.

4 **VI. FINANCIAL IMPACTS OF USING A MORE**  
5 **STANDARD EXIT FEE CONSTRUCT**

6 **Q. Have you estimated the financial impacts of making your appropriate changes to the**  
7 **proposed PSE exit fee for Microsoft?**

8 A. Yes. I have.

9 **Q. Can you estimate the impacts of using a 15-20 year forecast of net benefits/costs on**  
10 **PSE's proposed exit fee for Microsoft?**

11 A. Yes. PSE Exhibit No. \_\_\_(JAP-03) shows the benefits/costs of Microsoft  
12 terminating PSE power supply service. By referencing this exhibit, the basis for  
13 the \$23.7 million exit fee over a five-year forecast is displayed. As reflected in  
14 Exhibit No. \_\_\_(GSS-4) attached to this testimony, if the PSE forecast period is  
15 properly extended to 15 years, which is a conservative time period (i.e., relatively  
16 short when compared to resource planning periods and power supply asset useful  
17 lives), the net benefit to PSE remaining customers is roughly \$15.4 million. In  
18 other words, using a 15-year period of analysis, Microsoft would theoretically  
19 receive a payment from PSE of \$15.4 million, instead of having to pay over \$23.7  
20 million. Extending the period of analysis thus would result in a swing of about  
21 \$39 million of net benefit. PSE's proposal to have Microsoft pay a \$23.7 million  
22 exit fee is obviously highly protective of the remaining PSE customers.

1 **Q. Did you estimate the effect on PSE's exit fee proposal if an appropriate**  
2 **market value for the surplus Microsoft power is assumed?**

3 A. Yes. A firm load following product with ancillary services and a 4-year term  
4 should be used as the assumed value of the Microsoft-related surplus power. As  
5 shown in Exhibit No. \_\_\_(GSS-3) attached to this testimony, the value of this  
6 type of power supply product greater than the avoided power supply expenses  
7 assumed by PSE even when using this low cost BPA Tier 2 product for  
8 comparison. Based upon this, the PSE stranded cost proposal would decrease to  
9 \$7.8 million if a 5-year forecast period is used and become a net benefit of \$35.2  
10 million if a 15-year forecast is used. The basis for these calculations can be  
11 referenced on Exhibit No. \_\_\_(GSS-5).

12 **VII. SUMMARY OBSERVATIONS AND CONCLUSIONS**

13 **Q. In your opinion, is PSE's proposed exit fee of \$23.7 million calculated based**  
14 **upon generally-accepted exit fee principles?**

15 A. No. PSE's proposed exit fee for Microsoft is not in keeping with generally-  
16 accepted rate setting principles as they apply to the calculation of a fair, just and  
17 reasonable exit fee.

18 **Q. If the higher principle associated with exit fees to hold remaining customers**  
19 **harmless is the objective, would PSE's proposed exit fee meet this standard?**

20 A. No. The proposed PSE exit fee for Microsoft is far in excess of the amount  
21 needed to hold remaining PSE customers harmless. This proposed \$23.7 million  
22 exit fee would make PSE customers better off than they would have been if  
23 Microsoft had remained a full service customer of PSE.

1 **Q. In your opinion, how should the exit fee for Microsoft be calculated?**

2 A. An exit fee in this circumstance should be calculated over a forecast period of at  
3 least 15 years and be predicated on the highest and best use of the surplus PSE  
4 power supply created by Microsoft taking power supply services from a non-PSE  
5 source.

6 **Q. Have you estimated what a fair, equitable, non-discriminatory and adequate**  
7 **exit fee should be for Microsoft?**

8 A. Yes. Using generally-accepted rate setting standards and the factual basis noted  
9 above, Microsoft should receive a payment from PSE for not using PSE's power  
10 supply sources of between \$15.4 million and \$35.2 million.

11 **Q. Based upon your aforementioned analysis, is PSE's proposed exit fee for**  
12 **Microsoft of \$23.7 million in the public interest of the remaining PSE**  
13 **customers?**

14 A. Yes. This level of exit fee payment is significantly in excess of what regulatory  
15 precedent would dictate, in excess of what is needed to hold the remaining PSE  
16 customers harmless and is more than generous on the part of Microsoft.

17 **Q. Does this conclude your testimony?**

18 A. Yes. It does.