

**BEFORE THE WASHINGTON
UTILITIES AND TRANSPORTATION COMMISSION**

In the Matter of the Petition of

PUGET SOUND ENERGY, INC.,
and NW ENERGY COALITION

For an Order Authorizing PSE To
Implement Electric and Natural Gas
Decoupling Mechanisms and To
Record Accounting Entries
Associated With the Mechanisms

DOCKETS UE-121697 and
UG-121705

REPLY OF ELECTRIC AND GAS
JOINT PARTIES TO COMMENTS
OF INDUSTRIAL CUSTOMERS OF
NORTHWEST UTILITIES AND
PUBLIC COUNSEL TO JOINT
RESPONSES TO PETITIONS FOR
RECONSIDERATION FILED BY
NWIGU, NUCOR AND KROGER

I. INTRODUCTION

1. Nucor Steel Seattle, Inc. (“Nucor”), The Kroger Co. (“Kroger”), Northwest Industrial Gas Users (“NWIGU”),¹ Commission Staff, and Puget Sound Energy, Inc. (“PSE” or the “Company”) respectfully submit this response to the opposition filed by Industrial Customers of Northwest Utilities (“ICNU”)² and the Response of Public Counsel on November 8, 2013³ addressing the November 1, 2013 Joint Response of Commission Staff, PSE, NW Energy Coalition (“NWECC”), NWIGU and Nucor (“Gas Joint Response”) (the gas parties collectively are the “Gas Joint Parties”) and the Joint Response of Commission Staff, PSE, NWECC and Kroger (“Electric Joint Response”) (the electric parties collectively are the “Electric Gas

¹ NWIGU and Nucor join only the arguments set forth in sections A and G below and take no position on the arguments set forth in sections B through F. NWIGU represents its members only with regard to natural gas issues and Nucor does not buy power from PSE.

² Industrial Customers of Northwest Utilities’ Comments in Opposition to Joint responses to Petition for Reconsideration. (“ICNU Comments”)

³ Public Counsel Response to Joint Responses and Joint Testimony of Northwest Industrial Gas Users, Nucor, Kroger, Northwest Energy Coalition, Commission Staff and Puget Sound Energy. (“Public Counsel Response”)

Parties”).⁴ In their collective Joint Responses, the Joint Gas and Electric Parties (“Joint Parties”) reported to the Commission that they had collectively developed proposed alternatives to decoupling for large industrial, non-residential gas customers and Schedules 26 and 31 non-residential electric customers. The Joint Parties stated that if the Commission chooses to adopt their recommended decoupling alternatives, Nucor and NWIGU’s petitions for reconsideration in the referenced docket would be considered satisfied and Nucor would drop its request for reconsideration of the issue of return on equity reduction. ICNU and Public Counsel subsequently filed responses in opposition to the proposed alternatives to decoupling set forth in the Gas and Electric Joint Responses.

II. BACKGROUND

2. The Gas and Electric Joint Responses offer a straightforward resolution of the question of whether a one size fits all decoupling plan is appropriate for all large, non-residential PSE gas and electric customers by recommending the adoption of alternative plans for Schedule 85, 85T, 87 and 87T gas customers and Schedule 26 and 31 electric customers. In Order 07 in this proceeding, the Commission acknowledged that there may be “alternatives for some, or all, non-residential customers that are better suited to meeting decoupling’s goals than are the current decoupling mechanisms.”⁵ The Commission also indicated its willingness to remain “open to hearing fully supported alternative proposals for fixed-cost recovery from the non-residential class of customers, or subsets of the class.”⁶ Following the July 15, 2013, Procedural Conference, which the Commission convened following petitions for reconsideration of Order 07 by Nucor, NWIGU, and Kroger, most of the parties met on at least six occasions, with the Joint

⁴ NWEC does not oppose this reply, but due to the short turnaround time, NWEC has not had an opportunity to fully review the reply with its members and therefore does not join in the reply.

⁵ Order 07, ¶ 129.

⁶ *Id.*

Parties eventually reaching agreement on alternative approaches to achieving the underlying goals and purposes of decoupling for large, non-residential gas and electric customers. These alternatives were submitted to the Commission on November 1, 2013 in the Gas and Electric Joint Responses. On November 8, ICNU and Public Counsel filed responses essentially opposing the solutions that emerged through the collaborative efforts of the Joint Parties.

III. ARGUMENT

A. Approval of the Gas Joint Response does not unlawfully discriminate against non-residential electric customers, nor does it grant an undue and unreasonable preference to industrial customers, as claimed by ICNU.

3. The essence of ICNU's complaint with the proposal for large, non-residential gas customers contained in the Gas Joint Response is that its adoption would unlawfully discriminate and create unreasonable preferences between similarly situated customers. Nothing could be further from the truth.

4. ICNU did not file a petition for reconsideration of Order 07. Nucor and NWIGU, representing large, non-residential gas customers, and Kroger, representing certain large, non-residential electric users, set in motion the efforts to reach an alternative approach to decoupling. Through the efforts of these customers, ICNU was also given the opportunity to fashion its own alternative to decoupling in the subsequent negotiations. However, ICNU was not able to develop a proposal that garnered support from other parties.⁷ From the outset of this stage of the proceeding, natural gas and electric customers have proceeded as separate groups, not only in petitioning for reconsideration of Order 07, but in fashioning alternative approaches to

⁷ ICNU incorrectly states that "it advanced its own proposal to create an alternative decoupling mechanism for electric Schedule 40 customers, which was similar to the proposal adopted for Schedules 26 and 31, but for reasons that were never articulated, this proposal was rejected." ICNU Comments, ¶ 6. Commission Staff articulated concerns about proposed alternatives to decoupling for Schedule 40, in part due to a previous settlement agreement in PSE's 2011 general rate case in which the parties agreed to meet and review Schedule 40. Discussions of alternatives for decoupling for Schedule 40 can still take place in that larger Schedule 40 review.

decoupling. ICNU's opposition to the Gas Joint Response attempts to leverage the gas settlement to unrelated electric industry customers. It is an inappropriate objection to the terms of a proposal, in which it has no substantive interest

5. The erroneous basis for ICNU's position – that gas and electric customers are similarly situated – appears at the outset of ICNU's opposition: “[B]y exempting all industrial gas users from the current decoupling mechanism while keeping industrial electric customers subject to the same decoupling mechanism, the Gas and Electric Joint Responses discriminate against industrial electric users and grant an unreasonable preference to industrial gas users.”⁸ This statement is incorrect. Natural gas and electric customers buy different products and services and do so pursuant to an entirely distinct set of rates. The concepts of “discrimination” and “unreasonable preference” do not apply across different types of energy service. Gas and electric customers are not similarly situated and these terms are used incorrectly by ICNU and out of the context intended in RCW 80.28.90 and 80.28.100. The same logic holds true for ICNU's charges of impermissible rate discrimination and cost shifting. ICNU can point to no historical or judicial example where natural gas rates were found to discriminate against electric customers, nor where natural gas rates were found to impermissibly shift costs to electric utility customers. Natural gas and electric transmission and distribution systems developed entirely separately from one another, with their services and rates set accordingly.⁹

6. Washington courts have long held that rates are discriminatory only when similarly situated persons receiving the *same service* are charged different rates. Puget Sound

⁸ ICNU Comments, ¶ 2.

⁹ In addition to the obvious distinction that gas and electric customers buy different products and services, there are other distinctions between Gas Schedules 85, 85T, 87, and 87T and Electric Schedules 40 and 49. The gas schedules are primarily interruptible service, whereas Schedule 40 and 49 are fully firm service. As discussed below, customers in the excluded gas schedules primarily take unbundled service, whereas Schedules 40 and 49 only offer fully bundled service.

Elec. Ry. v. R.R. Comm'n of Washington, 65 Wash. 75, 96-97, 117 P. 739, 748 (1911) (“It makes no discrimination against persons or classes of persons by charging one a greater or less rate for the same service that is charged all other persons similarly situated.”) Gas customers and electric customers simply are not receiving the same service, no matter how analogous the rates may be.

7. When ICNU observes that “the Gas Joint Response proposes to exempt all industrial gas customers from decoupling entirely,”¹⁰ it is correct. The Gas Joint Response clearly states that “Schedules 85, 85T, 87 and 87T will not be subject to the decoupling mechanism but will be subject to the ‘rate plan’”¹¹ offered as an alternative to decoupling. However, what ICNU ignores is the fact that this approach was agreed to by the Gas Joint Parties because the vast majority of PSE’s fixed costs for customers on those schedules are already recovered and therefore decoupling is not necessary for those schedules. This does not discriminate or show undue preference to natural gas customers as opposed to electric customers, because those customers are not similarly situated. Natural gas has its own Commission-approved rates and costs and, if approved, its own alternative approach to decoupling for large industrial, non-residential natural gas customers.

8. ICNU illustrates the weakness of its position when it states that “the Gas and Electric Joint Responses would raise rates for non-residential customers that remain subject to the original decoupling mechanism.”¹² The *Gas* Joint Response, if implemented, will patently not raise or otherwise impact rates for *electric* customers. It cannot. Public Counsel addresses this issue along similar lines, but correctly limits comments to the impact the *Gas* Joint Response

¹⁰ ICNU Comments, ¶7.

¹¹ Gas Joint Response, ¶ 9.

¹² ICNU Comments, ¶7.

might have on other non-residential *gas* customers.¹³ However, the issue needs to be placed in context. The only possible rate impact that the Gas Joint Response projects might occur is on gas rates and then only to unwind the rate impacts that were due to the application of decoupling. Moreover, there is no immediate rate impact as a result of the proposal in the Gas Joint Response. There is only a projection that the rates for other non-residential gas customers may increase slightly in 2014 as a result of the unwinding of cross subsidization that occurred as a result of the Commission approved decoupling mechanism.

9. ICNU's legal argument is based almost entirely on the prohibition in RCW 80.28.100 against discrimination and unreasonable preferences "between similarly situated customers." ICNU is on perilously weak ground here, because changes in gas rates do not affect electric rates. Gas and electric customers are entirely different. They buy different products and do so pursuant to an entirely distinct set of rates. Choosing to ignore this distinction, ICNU attempts to connect gas and electric customers through decoupling itself: "Industrial gas customers and industrial electric customers are no different from each other with regard to the cost impacts decoupling has on them, as well as with regard to their role in effectuating the 'underlying purposes and goals of decoupling'."¹⁴ However, RCW 80.28.100, on its face, clearly intends to protect similarly situated customers from discrimination and unreasonable preferences for "doing a like or contemporaneous service with respect thereto under the same or substantially similar circumstances or conditions." The section is not meant to apply across different types of service, such as gas service versus electric service.

10. ICNU's fallback is RCW 80.28.090, which generally prohibits "any undue or unreasonable prejudice or disadvantage to any person, corporation, or locality, or any particular

¹³ Public Counsel Response, ¶5.

¹⁴ ICNU Comments, ¶8.

description of service. . . .” Again, natural gas and electric service are different products with different rates that account for different costs of separate systems. Rates and standards applying to natural gas have always been separate from those applied to electric service. ICNU’s reliance on Cole v. Wash. Utils. & Transp. Comm’n, 79 Wn.2d 302 (1971) does not support ICNU’s position. In that case, the Commission found no discrimination in offering lower natural gas rates to new home builders, which had the effect of incentivizing the use of natural gas in new construction. Cole had complained that this discriminated against established residential natural gas customers, but the Court recognized a difference between offering temporary service to new construction, as opposed to continuing service to established customers. In Cole, the Court was willing to draw a narrow distinction among what looked like, at least at first blush, similarly situated customers. Cole does not further ICNU’s argument in this case. ICNU asks the Commission to equate natural gas and electric service – a much broader leap than equating natural gas service for homes under construction with natural gas service for homes already occupied, which the Court refused to do.

11. The Court addressed this issue more recently and more directly in Willman v. Wash. Utils. & Transp. Comm’n, 122 Wn. App. 194, 211-12, 93 P.3d 909, 917 (2004), *aff’d*, 154 Wn.2d 801, 117 P.3d 343 (2005):

The petitioners contend first that the revised tariffs grant an undue or unreasonable preference to members of the Nation, because nonmembers receive no benefits from and do not have a voice in the tribal government. They misperceive the purpose of RCW 80.28.090, which is to assure that customers who receive the *same service* pay the same rates. [citation omitted] Under the revised tariffs here, all of the utilities’ customers within the boundaries of the reservation will receive the *same service* at the same rates. The tariffs thus do not violate RCW 80.28.090

In short, RCW 80.28.090 applies only to customers receiving the same service.

B. Approval of the Electric Joint Responses without also exempting electric Schedules 40 and 49 from decoupling does not discriminate against customers in Schedules 40 and 49 and does not grant an undue or unreasonable preference to Schedule 26 and 31 customers.

12. ICNU argues that the “customers effectively pay PSE through the decoupling mechanism to increase conservation efforts” and that “these conservation efforts should be viewed as a ‘service rendered’ by PSE to its customers.”¹⁵ ICNU goes on to argue that adopting the alternative decoupling provision proposed for Schedule 26 and 31 constitutes undue preference for those customers.

13. As an initial matter, ICNU’s contention that customers pay PSE to increase conservation efforts though the decoupling mechanism is factually incorrect. Decoupling adjustments are not a payment for services rendered (conservation or otherwise), but rather a ratemaking mechanism that can take the form of either a charge or a credit. This ratemaking mechanism is intended to maintain a targeted level of fixed cost recovery for PSE’s delivery service on a per-customer basis. The proposed alternative decoupling mechanism for Schedule 26 and 31 customers would simply subject said customers to an alternative mechanism for calculating targeted revenues per customer -- they would not somehow be provided the service of “conservation” on terms that are different from those afforded any other customers. ICNU’s contention that adoption of a modified decoupling mechanism for Schedules 26 and 31 constitutes an undue preference should be rejected.

14. ICNU’s argument fails to address the fact that the currently authorized decoupling mechanism already exempts Electric Retail Wheeling customers (Schedule 449) from decoupling. Because the Electric Retail Wheeling rate schedule is generally comprised of PSE’s largest industrial customers, a significant proportion of industrial customers are already exempt

¹⁵ ICNU Comments, ¶9.

from electric decoupling, and thus enjoy the very status that ICNU claims to be seeking for “industrial customers.” Not surprisingly, in its direct case in this proceeding, ICNU did not raise the argument that it raises here, namely, that exemption of certain electric customers (e.g., Electric Retail Wheeling customers) should be denied unless the exemption is extended to all other industrial customers such as those on Schedule 40. ICNU’s allegations regarding discrimination should be rejected as selective, self-serving and inaccurate.

15. Because decoupling is fundamentally a ratemaking mechanism, it has a clear nexus to PSE’s existing rate schedules; indeed, the determination of whether PSE’s targeted revenues per customer are adequately recovered is a function of the delivery service revenues that are recovered pursuant to the Company’s rate schedules. By their very terms, PSE’s existing rate schedules differentiate among customers in a manner that has been found to be just and reasonable and thus not unduly discriminatory. The differentiation of rates among customers in this manner makes it perfectly plausible that decoupling may be unnecessary for certain rate schedules or more expertly implemented through an alternative mechanism for other rate schedules. Indeed, the joint testimony presented in support of the Joint Responses to Petitions for Reconsideration demonstrates that this is the case for the rate schedules that the Joint Parties propose for exemption or alternative treatment. Moreover, it is commonplace for Commissions that have adopted decoupling to differentiate among rate schedules in its application.¹⁶

C. By its terms Schedule 40 differentiates the rates paid by its customers relative to Schedules 26 and 31.

16. Schedule 40 was established pursuant to a settlement agreement that was approved by the Commission in PSE’s 2004 general rate case. Schedule 40 was initially populated with customers that had previously been on Schedules 25, 26 and 31, but which

¹⁶ See Exhibit No. KCH-1T at 26:8-28:17.

concentrated load on a non-dedicated distribution feeder.¹⁷ The very creation of Schedule 40 is *prima facie* evidence that its customers have characteristics that differentiate them from customers on Schedules 26 and 31, i.e., they are not similarly situated, otherwise Schedule 40 customers would be paying the same rates as Schedule 26 and 31 customers. To underscore this point, the Schedule 40 rate structure is very different from that of Schedules 26 and 31. Indeed, the Schedule 40 rates for distribution service (a major component of decoupling-eligible revenues) are uniquely determined for each Schedule 40 customer. Naturally, the modifications to the decoupling mechanism that may be workable for Schedules 26 and 31 are not necessarily applicable to Schedule 40. While a modified approach to decoupling for Schedule 40 may still be reasonable, it has not at this time been achieved through negotiation. The failure to develop a consensus solution for Schedule 40 is not reasonable grounds to stymie the progress the Joint Parties have made in identifying reasonable alternatives for Schedules 26 and 31 (or Gas Schedules 85, 85T, 87, and 87T).

D. The adoption of the alternative decoupling mechanism for Schedules 26 and 31 will not arbitrarily increase rates for industrial electric customers as ICNU claims.

17. As explained in the Electric Joint Testimony, the alternative decoupling mechanism for Schedules 26 and 31 is projected to result in a *de minimis* rate impact of 0.07 percent to other non-residential customers. This projected negligible impact is a consequence of removing Schedule 26 and 31 customers from the larger group. This projected rate impact, minor as it is, is not arbitrary at all, but is simply the projected rate impact of those other customers bearing their own decoupling costs. Moreover, the segregation of Schedule 26 and 31 decoupling costs is not being pursued for the purpose of unwinding cross subsidies as suggested

¹⁷ Docket Nos. UE-040641 and UG-040640, Joint testimony of Joelle Steward, Donald Schoenbeck, Kevin C. Higgins, James A. Heidell, and Jim Lazar, pp. 11-12.

by ICNU (although that is a minor effect) but for the purpose of applying the decoupling mechanism to the specific revenues collected from the Schedule 26 and 31 demand charges, consistent with the design of the alternative mechanism.

18. Ironically, ICNU overlooks the fact that the creation of Schedule 40 in 2005 increased rates for each of the rate schedules from which Schedule 40 customers migrated: 0.017% for Schedule 25, 0.207% for Schedule 26, and 1.159% for Schedule 31.¹⁸ These rate increases occurred because the customers remaining on those rate schedules were required to bear their own costs without the revenues from the departing Schedule 40 customers. Just as the rate increases experienced by other rate schedules by the establishment of Schedule 40 was in the public interest, so is the projected minor rate impact to the remaining non-residential customers when Schedule 26 and 31 customers are provided a separate decoupling mechanism. ICNU cannot have it both ways in its advocacy for Schedule 40.¹⁹

E. Public Counsel's conjectures on rate design for large customers should not derail the adoption of an alternative decoupling mechanism for Schedule 26 and 31 customers.

19. Public Counsel attempts to undermine the alternative decoupling mechanism developed for Schedules 26 and 31 by conjecturing that the accompanying adjustment to the rate design could create a disincentive to invest in energy conservation (even though reducing a customer's billing demand through energy efficiency would save the customer money). The Joint Parties, while of differing opinions as to whether such a concern is bona fide, have addressed this matter head on by agreeing that PSE would analyze this very question.

¹⁸ *Id.* p. 13, lines 1-6.

¹⁹ ICNU alleges, without support, that "Schedule 26 and 31 customers are essentially subsidizing other non-residential customers" and "[t]he same is true for Schedule 40 customers." ICNU Comments, ¶18. There is no evidence in the record supporting ICNU's hypothesis that Schedule 40 customers are subsidizing other non-residential customers. In fact, the opposite may be true--other non-residential customers may be subsidizing Schedule 40 customers.

Specifically, the Joint Response provides for an examination of whether and how the change to rate design for Schedule 26 and 31 affects conservation achievement by these customers. The evaluation will examine whether there is conclusive evidence that the change had an appreciable effect on customers' energy efficiency achievements, including but not limited to achievements made through customer participation in PSE's energy efficiency programs.

20. Moreover, it is worth noting that Schedule 26 and 31 customers are starting from rates that are 103 - 104 percent of cost of service, based on the cost-of-service analysis presented by PSE in its last general rate case.²⁰ These above-cost rates provide an added price incentive for these customers to conserve and the proposed rate design change will not change the revenue requirement for these rate schedules. Consequently, they will continue to have the added incentive to conserve energy that comes with paying rates that are above parity.

21. Finally, while it is true that the alternative proposal for Schedules 26 and 31 shifts recovery of costs from energy charges to demand charges, approximately 70 percent of revenue from Schedules 26 and 31 (\$182 million vs. \$262 million) will continue to be recovered through volumetric charges. Thus, there continues to be ample incentive for customers to conserve.

F. Contrary to Public Counsel's claims, there is ample evidence in the record to support the alternative decoupling proposal for Schedules 26 and 31.

22. The rationale for focusing on rate design and demand charges to meet the objectives of decoupling is fully addressed in the record of this case.²¹ Although the Commission was unwilling to adopt Kroger's decoupling recommendations over the objections of the Joint Parties, it is critical to appreciate that a more comprehensive discussion has since occurred among the Joint Parties which has allowed them to support a *compromise* that blends

²⁰ Exhibit JAP-1T, p. 10.

²¹ See Exhibit No. ___ (JPE-1T) 14:11-15:12; Exhibit No. KCH-1T at 24:10-31.

some of the elements advocated by Kroger with the fundamental decoupling mechanism approved by the Commission. Public Counsel seeks to use the Commission's statement that alternative proposals "*should be supported by a detailed cost of service study and such other evidence as may be needed to protect both the Company and its customers*"²² to block adoption of the alternative mechanism, but Public Counsel's arguments are misplaced. First, the projected impact on other customers is presented in the record, and it is *de minimis*. Second, with a Joint Response in hand, it is not necessary for the Commission to "*protect the Company*" with respect to the alternative proposal because the Company is a signatory to the alternative proposal. PSE sees the merit in the proposal it helped to negotiate and is in agreement with it. Third, as there are no cost shifts as a result of the alternative proposal, the Joint Parties can reasonably rely on the same cost of service study that supports the Commission's decision to adopt decoupling in the first instance, namely the cost-of-service study performed in support of PSE's last general rate case. To require a new cost of service study for the alternative proposal – when there are no cost shifts and a new cost-of-service study was not required for the currently approved decoupling mechanism – would be to require an asymmetric and unreasonable burden of proof.

G. Adoption of the proposals offered in the Gas and Electric Joint Responses would not be unduly complex or administratively burdensome.

23. Public Counsel's specific complaint with the Gas Joint Proposal deals with the projected impact it will have on rates for other non-residential gas customers, which Public Counsel claims would be 3.6 percent, as opposed to the 3.0 percent calculated by the Joint Parties.²³ This issue was addressed above at pages 4-5.²⁴

²² Order 07, ¶ 128.

²³ Public Counsel Response, ¶5.

24. The only projected rate impact that the Gas Joint Response has is on gas rates and then only to unwind the rate impacts that were due to the application of decoupling. By definition, if the application of decoupling causes rates to go in one direction, unwinding or unapplying decoupling will cause rates to go back the other way. The new settlement will at least reduce the number of classes in each group to reduce the amount of cross-class subsidization that Public Counsel acknowledges will happen through decoupling.

25. Public Counsel's secondary complaint is that an alternative to a decoupling mechanism "appear[s] to increase the administrative complexity and burden rather than reduce it."²⁵ There is no authority offered for this statement, other than Commission Staff's discussion in another case of whether system-wide decoupling is simpler than class-by-class decoupling,²⁶ which is not evidence in this present proceeding. In principle, however, there is no requirement that procedural efficiency should trump administrative robustness, and nothing in the record establishes this standard. Moreover, since all industrial customers are granted an exemption in the Gas Joint Response, complexity is actually reduced.

26. Public Counsel overlooks record evidence that other utilities in the Western United States have exempted large non-residential customers from decoupling, apparently with no undue administrative effects. Kroger's expert witness, Kevin C. Higgins, noted that the only two major electric utilities in the Western states that have adopted full revenue decoupling, Idaho Power and Portland General Electric, chose not to apply revenue decoupling to all non-residential customers.²⁷

²⁴ It is important to keep in mind that all of these rate impacts are projections and are expected to change over time as new information becomes available. Public Counsel's concern about the change in projected rate impacts must be viewed in this context.

²⁵ Public Counsel Response, ¶13.

²⁶ Public Counsel Response, ¶13 n.16.

²⁷ See Exhibit No. KCH-1T at 26:8-28:17.

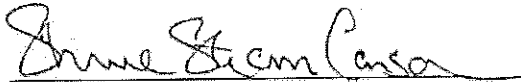
IV. CONCLUSION

27. The proposal set forth in the Gas Joint Response offers a reasonable alternative to the standard decoupling mechanism and should be adopted. The arguments to the contrary submitted by ICNU and Public Counsel are not supported by law and the facts and should be rejected. The Electric and Natural Gas Joint Parties respectfully request the Commission to adopt the alternatives proposed in the Gas Joint Response.

DATED this 15th day of November, 2013.

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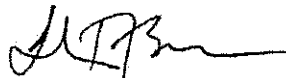
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