Puget Sound Energy
P.O. Box 97034
Bellevue, WA 98009-9734
PSE.com

Received
Records Management
04/30/19 16:42
State Of WASH.
UTIL. AND TRANSP.
COMMISSION

April 30, 2019

Filed Via Web Portal

Mark L. Johnson, Executive Director and Secretary
Washington Utilities and Transportation Commission
P.O. Box 47250
1300 S. Evergreen Park Drive S.W.
Olympia, Washington 98504-7250

Re: Docket U-180907: Comments of Puget Sound Energy in Response to Notice of Opportunity to File Written Comments on adequacy of the current regulatory framework employed by the Commission in addressing developing industry trends, new technologies, and public policy affecting the utility sector

Dear Mr. Johnson:

Puget Sound Energy (PSE) appreciates the Commission's effort to solicit feedback in order to craft policy guidance and a potential framework for considering expedited rate filings (ERFs) in the future. PSE submits the following responses to the Commission's questions raised in the Notice of Opportunity To File Written Comments issued on March 21, 2019 (notice). As described in the notice, PSE's experience in its most recent ERF (Dockets UE-180899 & UG-180900) demonstrated a need for a clear policy framework for considering ERFs so that all parties have a consistent understanding of an ERF's parameters and rules. An ERF has the potential to be one of many useful tools in responding to the transformation of the energy industry and addressing regulatory lag, but its success as a mechanism depends on having clear and defined rules. In particular, parameters around (i) the procedural schedule, (ii) the ratemaking methodology and (iii) prudence determinations are important. Based on PSE's most recent experience, the company would be more inclined to proceed with a more established process like a general rate case (GRC) rather than proceed with another ERF until a stronger and more definitive policy framework is established. PSE appreciates the Commission's efforts to establish that framework under a docket focused on aligning customer and utility incentives in a changing utility regulatory landscape.

<u>Policy Issues</u>

1. Regulatory lag

a. Are ERFs an important tool to address regulatory lag?

PSE Response: Yes, ERFs have the potential to be an important tool to address regulatory lag provided that the procedural schedule allows for a truly *expedited* proceeding. To PSE, expedited means a procedural schedule of four or less months from the filing date to rate effective date. Otherwise, the utility is incentivized to file a GRC, which allows for the use of pro forma adjustments (that are not allowed in ERFs) and more liberal use of annualizing adjustments.

b. Do ERFs effectively and efficiently remedy regulatory lag?

PSE Response: Based on PSE's most recent experience, the answer is no. However, an ERF framework with clearer rules that support a truly expedited process would allow the mechanism to reduce lag. The efficiency of an ERF mechanism in reducing regulatory lag depends on certain elements of the policy framework. Examples of elements that could make an ERF more effective and efficient include a four-month procedural schedule (from filing date to rate effective date), a common understanding of threshold issues, clearer guidance on prudence requirements and a streamlined ratemaking and reporting methodology. The current policy framework is not clear, marginally effective and not efficient in addressing regulatory lag.

c. Are there other non-ERF solutions that would more effectively or efficiently resolve regulatory lag?

PSE Response: Yes. Fundamentally, all forms of regulatory lag could be addressed in a GRC if the regulatory lag is handled in a more holistic fashion (e.g., through some form of future test year or attrition adjustment). From there, a properly constructed multi-year rate plan could extend that effective treatment of lag several more years. Absent such a holistic approach, other types of solutions may be more efficient and effective in addressing specific causes of regulatory lag. These solutions could include decoupling (for load-based attrition), trackers (which address single-sources of cost-based attrition), deferred accounting treatment for investments and depreciation (which are effective at treating attrition for investments in shorter-lived assets), or more extensive pro-forma adjustments. Formula rates, such as the one used by PSE for setting rates for wholesale transmission service through its Open Access Transmission Tariff, is another example.

d. If regulatory lag is cited as a reason for serial general rate cases, and ERFs alleviate regulatory lag, to what extent should the filing of an ERF be tied to the commitment to file fewer rate cases?

PSE Response: While an ERF could ameliorate or delay the need to file a GRC, there are multiple sources of regulatory lag (as noted above) and some of those sources may not be addressed by an ERF (depending on how one defines it). For example, return on equity has so far been excluded from ERF filings before the Commission. If cost of capital were to make a

significant turn upwards, this could put the utility at a material disadvantage for earning relative to what it may otherwise earn if it were allowed to request a higher return. Power costs are another factor to consider. It may be that sources of attrition come from both the production/sale of energy and its delivery. While it's possible in PSE's case that it could file a power cost only-rate case, it is unclear how parties to that case would respond to a simultaneous ERF filing. It would seem reasonable to expect, with such a broad array of sources of regulatory lag, that the utility should instead file a full GRC. Moreover, if a utility feels the need to file a GRC so soon after an ERF, it may be an indication that the ERF truly wasn't effective in addressing regulatory lag in the first place. For all of the above reasons, conditioning the approval of ERFs on fewer GRCs may be unwarranted and, indeed, may be counterproductive if it leads to reluctance by utilities to file ERFs at all.

2. Responsiveness to change

a. Are companies, ratepayers, and the Commission responding fast enough to the changing energy landscape? If not, how can ERFs be used to help companies, ratepayers, and the Commission respond?

PSE Response: No. PSE believes the traditional model of cost recovery in Washington State does not sufficiently support the pace and scale of utility adoption of advanced technologies necessary to respond to customer expectations and new public policy requirements. ERFs can be one of many tools to help respond to a changing utility landscape, but an ERF's effectiveness depends on its framework, procedural schedule and application. As mentioned earlier, ERFs with a truly expedited procedural schedule and clear definitions of threshold requirements for filing could be used to reduce overall regulatory lag or address the depreciation expenses on shorter-lived technology investments that are becoming more fundamental to providing the utility service that customers and policymakers increasingly expect.

3. Other policy issues

a. Are there other policy issues that ERFs could address?

PSE Response: Yes, by helping to address associated regulatory lag, a well-designed ERF can simultaneously help address other policy issues. For example, public policy mandates to integrate more carbon-free energy into the utility energy supply mix will require increased investment in building (or buying the output from) renewable energy projects and the necessary infrastructure to integrate and deliver that energy to load centers. Increasingly, these investments have shorter useful lives or may be outright expenses. A well-designed and predictable ERF process, along with the use of power cost only rate cases for new resources, could help address the lag in recovering the investments and related expenses necessary for building (or buying) and delivering renewable infrastructure.

Through its effect on regulatory lag, a well-designed ERF could also help support market transformation projects. Commission policy has recognized that utilities play a necessary role in transforming certain markets such as electric vehicles or battery storage. Reduced regulatory lag for investments in market transforming pilots, programs, services and infrastructure could provide more certainty to utilities and potentially lead to more rapid market transformation.

b. How do ERFs effectively and efficiently address these additional policy issues?

PSE Response: Similar to PSE's response to question 1(a), an ERF is only effective and efficient in addressing these policy issues when its framework truly differentiates this mechanism from a general rate case. PSE proposes a procedural schedule of four months (or less) as one element of that differentiation.

c. Are there non-ERF solutions that would more effectively or efficiently resolve these policy issues?

PSE Response: Yes, but it also depends on how those mechanisms are designed. Again, PSE believes the preferred approach should be better regulatory treatment in a GRC. Absent that, the following solutions could be more effective and efficient to address these policy issues: trackers, deferred accounting treatment for investments and depreciation, and the use of PCORCs to allow for power cost updates and the inclusion of new clean energy investments into PSE's portfolio.

Threshold Criteria

1. Under what circumstances is an ERF appropriate?

PSE Response: At least as traditionally constructed, ERFs are most appropriate as a tool to mitigate the effects of regulatory lag shortly after a GRC where the principal cause of that lag is increasing delivery system costs related to rate base or expenses. As originally envisioned, this would be a straight-forward administrative filing where these costs were simply trued up to a more recent period of time and all other factors normally adjudicated in a GRC were purposely excluded.

2. What should be the standard to demonstrate the need for expedited rate relief?

PSE Response: An important standard to demonstrate the need for an ERF should be that the company can demonstrate a revenue deficiency based on a commission basis report (CBR) with allowed annualizing adjustments. It is important that a utility be able to include designated annualizing adjustments in demonstrating its need for an ERF. A historical CBR alone does not provide an up-to-date snapshot of the company's financial picture and current need for rate relief.

3. In the context of an ERF, what is the appropriate basis for determining whether a company's current rates are or are not fair, just, reasonable, and sufficient? Is the basis different than the standard for a general rate case (GRC)?

PSE Response: No. The basis for determining fair, just reasonable, and sufficient rates should not differ much between an ERF and GRC. The standard should be that the utility can demonstrate a revenue deficiency based on a CBR with allowed annualizing adjustments. There should not be a higher threshold such as a showing of "extraordinary under-earnings" or "extraordinary circumstances." The standard should remain for either a GRC or ERF that a utility must demonstrate its rates are not fair, just, reasonable, or sufficient.

That being said, there is a related issue that the Commission should address in this context. The Commission should make clear its standard for determining that the rates it *approves* in an ERF filing are fair, just, reasonable and sufficient. In PSE's most recent ERF filing it was unclear whether the approved ERF rates must take into consideration the totality of the company's earnings after the approval of the ERF rates. Using a very simple example, if the utility is slightly over-recovering its variable power costs, should that over-recovery be factored into the overall level of rates approved for the recovery of delivery costs through the ERF filing? If so, could this possibly imply that any form of single-issue rate filing (e.g., the recovery of conservation costs) also need to first explore the impact of the approved rate change on the totality of the utility's earnings? These are issues that must be addressed as part of any Commission policy guidance or rules surrounding ERF filings.

<u>Methodology</u>

1. What is the appropriate conceptual framework for an ERF?

PSE Response: An ERF proceeding should strive for a balance of speed, accuracy and simplicity. The best way to achieve that balance is to align the ERF framework with existing utility processes to the extent practicable. An ERF should be completed in four months or less (from filing date to rate effective date), filed within two years of a GRC, and include up-to-date, transparent and accurate information. To achieve these ERF policy objectives, major elements from the previous GRC should remain unchanged such as ROE, rate design, cost of service, etc. It is also important for an ERF to use a new test period because it is current, more accurate, re-establishes the revenue, expense and rate base relationship and better aligns with established utility and stakeholder experience with constructing and evaluating test years.

2. Should an ERF use a new test year or should an ERF use the test year from a recently completed general rate case and merely extend the pro forma period? If the pro forma period is extended, should an ERF only include those capital additions that were not included in pro forma adjustments of the last GRC?

PSE Response: An ERF should use a new test year. A new test year is more current, accurate, cleaner and simpler than extending a pro forma period. A new test year appropriately re-establishes the revenue, expense and rate base relationship[1]. Utilities are experienced at preparing test year results and stakeholders are experienced at evaluating them. A new test year will match the utility's audited or reviewed books. There is not much benefit to have an ERF be an extension of the previously completed GRC as it would be more challenging and contentious to match revenues and expenses through pro forma adjustments than using a more up to date test period.

There will be minimal or no benefit to the utility if an ERF uses the test year from the recently completed GRC and "merely extend[s] the pro forma period." Generally, pro forma adjustments

---

[1] *WUTC v. PSE,* Dockets UE-111048 and UG-111049, Prefiled Response Testimony of Kenneth L. Elgin, Exh. KLE-1T, p. 80:15 -81:7.

must qualify as major projects and only capture a small fraction of the overall utility cost structure. Therefore, limiting a utility to only pro forma adjustments from a previous test year would result in the utility failing to recover much of the plant that was put in service and the utility would be incentivized to quickly file a general rate case rather than an ERF to recover this excluded plant in service.

3. Should an ERF include all new plant in service, or just major investments? Should it exclude revenue-producing plant?

PSE Response: An ERF should include all plant in service including revenue producing plant and not be limited to "major investments." As stated above, it is PSE's belief that a new test year should be established in an ERF. Therefore, inclusion of revenue producing plant would be matched with revenues in the newly established test year.

4. How should plant additions be treated in an ERF if parties do not have the time to perform a thorough prudence review? Should ERF rates be subject to refund if prudence determinations for investments cannot be completed?

PSE Response: It is absolutely critical that the Commission provide clear guidance on its expectations regarding prudence in the context of an ERF filing. PSE believes that a higher prudence bar in an ERF filing will likely result in more time being required to adjudicate this type of filing and, in turn, the less likely that utilities will find an ERF useful for addressing regulatory lag. For an ERF to work as intended, the prudence bar must be set as low as possible to ensure the ERF is a simple and streamlined administrative process. Ideally, there would be no prudence review, and the ERF would be a simple exercise in addressing whether the plant included in rates is "used and useful." In exchange, the utility would carry its prudence burden for these investments into its next filed GRC where all parties have sufficient time to examine prudence of all investments made since the time of the utility's last GRC.

The question of whether ERF rates should be subject to refund is tied directly to the issue of prudence review. To the extent that the Commission accepts a proposal similar to the one put forth above, where there is little to no prudence review, then setting rates subject to refund is an appropriate customer protection. However, if and to the extent prudence review is required, it would be appropriate to exclude such costs from such a refund condition through a later re-examination in a future GRC proceeding.

An alternative to what PSE proposes above could be to construct the ERF as a two-part process, whereby interim rates would be allowed to go into effect, subject to refund, within three-to-four months of filing subject to verification that plant being recovered in rates was deemed "used and useful". The ERF filing would then enter a prudence phase, where all costs included in the filing were subject to the Commission's standard prudence review over another 6 month period. If any costs were deemed imprudent, then the portion of the interim rates allowed to go into effect tied to that plant would be subject to refund. This is admittedly a more cumbersome process for the Commission, utilities and intervenors. However, it would provide parties most concerned with a

more contemporaneous review of prudence an opportunity to have their review while providing utilities some degree of relief from regulatory lag.

5. How should expenses be handled in an ERF? Should expenses update to actuals or should they remain tied to the previous GRC?
PSE Response: Expenses should be updated to actuals for the ERF test year. This will allow for a more current and accurate representation of company expenses and matching of revenues, expenses and rate base as discussed in PSE's response to question 2 above.

<u>General Considerations</u>
1. What are the benefits and drawbacks of an ERF relative to a GRC?
PSE Response: The answers depend on whether the policy framework for ERFs truly differentiates the mechanism from a GRC. A well-designed ERF would allow rates to go into effect within four months from initial filing, and include a common understanding of threshold issues and methodology. Based on PSE's most recent experience—its 2018 ERF—the procedural schedule for a fully litigated ERF would have allowed for rates to go into effect approximately six to seven months after the ERF filing, which would not provide sufficient benefits to replace a GRC. One reason for this is that a utility can include pro forma and annualizing adjustments in a GRC, whereas pro forma adjustments have not been permitted and annualizing adjustments have been limited in an ERF. If the utility is to forgo these adjustments, the ERF must provide for a truly expedited schedule of no more than four months otherwise it holds no benefits over a GRC.

Also, there must be certainty on the threshold for filing an ERF and the procedural requirements for the proceeding. PSE's June 2018 ERF was withdrawn due to disagreements with Staff over the format and threshold issues for the filing, even though PSE had followed the format used in its 2013 ERF. If uncertainties on these issues continue, PSE sees no advantage in filing an ERF rather than a GRC, as there is insufficient time in an ERF to litigate its threshold or procedural requirements.

As for the potential drawback of an ERF relative to a GRC, the opportunity for adequate prudence review within a very tight timeline is paramount. However, it isn't insurmountable. PSE has proposed two alternatives above to address this concern and would be open to exploring others.

2. In what ways does an ERF create or relieve administrative or process burdens for responding parties?
PSE Response: Again, the answers depend on the policy framework for ERFs, particularly as it relates to prudence. In PSE's preferred handling of prudence discussed earlier, the ERF process could be exceedingly efficient and have a very low administrative burden. Beyond prudence, the clearer (and firmer) the guidance on the issues outlined above, the less burdensome the process will be in administering an ERF filing.

Thanks again for the opportunity to provide comments. Please contact Nate Hill at (425) 457-5524 or nate.hill@pse.com for additional information or questions regarding this filing. If you have any other questions, please contact me at (425) 456-2142.

Sincerely,

/s/ Jon Piliaris

Jon Piliaris
Director, Regulatory Affairs
Puget Sound Energy
PO Box 97034, EST-07W
Bellevue, WA 98009-9734
425-456-2142
Jon.Piliaris@pse.com

cc: Lisa Gafken, Public Counsel
Sheree Strom Carson, Perkins Coie