

Rates and Regulatory Affairs
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December 3, 2008

VIA ELECTRONIC FILING

Public Utility Commission of Oregon
550 Capitol Street, N.E., Suite 215
P.O. Box 2148
Salem, Oregon 97308-2148

Attn: Filing Center

Re: OPUC Docket UM 1327
Application for Reauthorization to Defer Smart Energy Pilot Program
Communication Costs

Northwest Natural Gas Company, dba NW Natural ("NW Natural" or the "Company"), files herewith the above-referenced Application for Reauthorization to Defer Smart Energy Pilot Program communication costs. The application requests continued authorization to defer costs associated with educating customers about how to reduce their carbon footprint by reducing their gas consumption and offsetting their remaining usage with carbon offset products offered through the Smart Energy Pilot Program.

The 2007-2008 Smart Energy Annual Report filed with the Commission on October 30, 2008 is attached as Exhibit A. Also, a Certificate of Service stating that parties to UM 1327 have received notice of this filing is attached as Exhibit B.

Please call Jennifer Gross at (503)226-4211, extension 3590 if you have any questions.

Sincerely,

/s/ Inara K. Scott

Inara K. Scott, Manager
Regulatory Affairs

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**BEFORE THE PUBLIC UTILITY COMMISSION
OF OREGON**

UM 1327

**NORTHWEST NATURAL'S APPLICATION
FOR REAUTHORIZATION OF DEFERRED
ACCOUNTING**

In the Matter of the Application of
NORTHWEST NATURAL for an Order
Reauthorizing Deferred Accounting for
Smart Energy Program Communications
Costs

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8 Under ORS 757.259 and OAR 860-027-0300, Northwest Natural Gas Company
9 ("NW Natural" or the "Company") applies to the Oregon Public Utility Commission (the
10 "Commission") for an order reauthorizing the Company to defer certain unfunded
11 communications costs associated with NW Natural's Smart Energy pilot program incurred
12 January 1, 2009 through December 31, 2009.

13

I. INTRODUCTION

14 NW Natural's Smart Energy pilot program is a voluntary program that enables
15 residential and commercial customers to offset greenhouse gas emissions associated with
16 their natural gas use by purchasing high quality project-based emission reductions from
17 offset projects developed by The Climate Trust.¹ Although the 5-year pilot program is
18 funded almost entirely by the voluntary participants, the program's success—and related
19 benefits—depends on a portion of its communications costs being spread to all classes of
20 customers eligible for participation in the program.

21 On November 14, 2008, NW Natural presented the Portfolio Options Committee
22 (POC)² with a proposed budget of \$475,000 for communications that it believes are

23 ¹ For more information about the Climate Trust, see NWN Advice No. OPUC 07-
24 4/Miller/101/1-2 (filed June 29, 2007).

25 ² The POC is a committee formed to present recommendations to the Commission regarding
26 residential portfolio options per OAR 860-038-0220. Upon approval of the Smart Energy program in
2007, the POC recognized that the Company's carbon offset product was similar in nature to the
electric utilities' portfolio options. At its meeting on February 8, 2008, the POC unanimously approved

1 necessary in order to achieve continued success of the program. The POC approved a
2 motion to recommend that the Commission approve the Company's deferral request. The
3 Company herewith files this application with the support of the POC, for the deferral of no
4 more than \$475,000 for communications associated with the Smart Energy program.

5 **II. BACKGROUND**

6 NW Natural is committed to helping our customers reduce their carbon footprint by
7 using natural gas as efficiently as possible. Consistent with this, the Company has formed a
8 successful partnership with Energy Trust of Oregon, Inc. ("Energy Trust") to help customers
9 increase their energy efficiency and plans to continue to find new ways to work with Energy
10 Trust in the future. Additionally, NW Natural supports the enactment of federal climate
11 legislation to limit greenhouse gas emissions. Although legislation is not currently in place,
12 NW Natural believes it must continue taking steps to help its customers reduce their climate
13 impacts immediately—without waiting for this future regulatory program to take effect.

14 In 2007, the Company launched its Smart Energy Pilot program.³ The Company
15 believes its Smart Energy Pilot program is a prudent, proactive approach to future carbon
16 legislation. This program will provide the Company with knowledge and experience with
17 carbon legislation that may reduce future compliance costs and allow the Company to
18 search now for low-cost mitigation opportunities that may be more difficult to access in a
19 fully developed compliance market.

20 **A. 2007 and 2008 Program Costs**

21 Residential Smart Energy participants pay a flat amount of \$6 per month or a rate of
22 \$0.10486 per therm. Commercial participants may select a flat amount of their choosing
23 (not less than \$10 per month). This rate is designed to fund the cost of carbon offsets

24 a motion to recommend that the Commission include the Smart Energy program under the POC's
25 oversight and that the Company be invited to serve on the POC. See Order No. 08-278, approving
this motion.

26 ³ See Order No. 07-383; Advice No. 07-4.

1 estimated at the time of this filing and the ongoing administrative costs associated with the
2 program. The Smart Energy program rate was not designed to cover the costs associated
3 with program start-up costs incurred in 2007 or the communications costs expected in 2008
4 and 2009 because the Company's market research suggested the program's rates are near
5 the top end of the price customers will pay for a product of this kind. Moving above these
6 rates would likely result in substantially fewer customer signups, and ultimately, an
7 unsuccessful program.

8 In 2007, the Company agreed to pay all start-up costs associated with the program,
9 which were approximately \$270,000. The Company also agreed it would absorb the capital
10 expenditures associated with development of the project until the Company's next rate case.
11 In 2008, the Company was granted authorization to defer up to \$622,000 for start-up and
12 program education costs as forecasted in Appendix A to Order No. 07-383.

13 **B. 2009 Communication Cost Forecast**

14 Appendix A to Order No. 07-383 shows that the Company estimated needing to
15 request deferral of \$268,000 for communication costs in 2009. Learnings gained during the
16 first program year have altered this forecast. The Company has found that Smart Energy is
17 a difficult product to communicate to customers, and increasing or even maintaining
18 program enrollment requires the delivery of repeated messages through multiple media
19 channels.

20 Beyond gaining a better understanding of how to successfully communicate about
21 Smart Energy to customers, the Company has also realized that its revenue forecast was
22 not sufficiently detailed. The Company did not build in a half-year convention or other lag
23 factor, and thus the model reflected revenues based on a 12-month collection of the \$6 flat
24 fee, whereas in reality, customers do not all sign up in January.

25 According to the refined program forecast, the Company now recognizes a need to
26 defer approximately \$475,000, which it expects to incur for its 2009 Smart Energy

1 **A. Description of Utility Revenue or Expense.**

2 This application addresses NW Natural's unfunded program communication
3 expenses. As explained above, the success of the program relies in part on the program
4 rate not exceeding a level that customers are willing and able to pay. Consequently, the
5 program rate does not cover all the related program costs.

6 NW Natural shareholders committed to pay all start-up operating costs incurred in
7 2007, which was approximately \$270,000. In addition, NW Natural's shareholders absorbed
8 all related capital costs until the Company's next general rate case. In 2008, the Company
9 deferred approximately \$621,000 in additional start-up and educational costs. Now, the
10 Company expects to incur approximately \$475,000 in program communication costs during
11 the 12 months covered by this deferral application.

12 Table 1 below itemizes the Company's proposed 2009 Smart Energy communication
13 budget and compares it with the program costs deferred in 2008. The 2008 column
14 represents actual costs through October 2008 and two pending invoices totaling \$50,000
15 from The Climate Trust.

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Table 1

Communication Expenses - Smart Energy Deferral Account		
	2008	2009 (proposed)
The Climate Trust	\$100,000.00	0
Costs to start up Smart Energy Pilot Program		
Education	\$355,604.47	\$331,000.00
Customer communications, advertising, media outreach		
Interaction	\$111,679.60	\$105,000.00
Direct mail, email, community outreach, events, sponsorships		
Professional Services	\$13,495.00	\$10,000.00
Creative production, fees		
Promotional	\$35,970.71	\$20,000.00
give-away items, incentives, promotional activities		
Miscellaneous	\$3,810.16	\$9,000.00
Postage, materials, etc.		
Total	\$620,559.94	\$475,000.00

As Table 1 suggests, the Company intends to employ a similar communications strategy in 2009 as was used in 2008. The Company's 2009 efforts will be scaled back slightly but will still be at a level necessary to be relevant among the communities served. The Company's 2009 educational materials will build on the awareness garnered in 2008. The majority of the 2009 costs will be spent on education about climate change and the need to reduce greenhouse gas emissions, as well as additional messaging about biodigester projects and the benefits they provide. The Company will continue to leverage the same communication channels, as they proved to be effective.

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1 **B. Reasons for Deferral.**

2 ORS 757.259(2)(e) allows the deferral of utility revenues where necessary to match
3 appropriately the costs borne by and benefits received by ratepayers. By deferring the
4 communication costs associated with the Smart Energy program and spreading those costs
5 to all customers eligible to participate in the program, this request seeks to align the costs
6 NW Natural will incur for its Smart Energy program with the broad benefits customers
7 receive.

8 **1. The Smart Energy Program Offers Broad Benefits.**

9 The Smart Energy program provides a broad array of benefits for all NW Natural
10 customers, whether or not they enroll in the program. First, the program provides real and
11 measurable greenhouse gas benefits. While these offset benefits will be retired by The
12 Climate Trust for the participants, the environmental benefits of these actions accrue to all.
13 Second, the program allows all NW Natural customers an opportunity to learn about their
14 “carbon footprint” and the specific steps they can take to reduce it. As our state and country
15 move toward carbon regulation, it will become more important that all customers make the
16 connection between their energy use and their carbon impacts. Third, the Smart Energy
17 program will provide an opportunity for the State of Oregon, Public Utility Commission, and
18 NW Natural to develop and hone policy tools that will be critical in the upcoming regulation
19 of greenhouse gases. Finally, it is appropriate to collect program educational costs from all
20 customers because the program creates opportunities for all customers to participate. The
21 existence of the program, and its availability to all customers, is of value for all and thus
22 justifies spreading some costs to all NW Natural customers.

23 These broad benefits for customers are valued and expected by NW Natural
24 customers. In a March 2007 survey, 81% of respondents said they “strongly favored” or

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1 “somewhat favored” NW Natural offering a program for customers that helps reduce carbon
2 dioxide emissions⁴.

3 **2. Program Success Depends on Effective Education.**

4 A utility carbon offset program is a relatively unknown product that brings with it
5 some complex issues. While concern about climate change is growing, customers are not
6 yet fluent with concepts such as a “carbon footprint,” and with the idea of balancing
7 emissions from one activity with “offsets” from another. A successful program pilot requires
8 a steady delivery of broad education about how customers’ gas use produces carbon
9 dioxide, the connection between carbon emissions and climate change, and the concept of
10 carbon offsets.

11 **3. Support from All Customers Will Be Modest.**

12 The effect on an average residential customer bill is estimated to be approximately
13 4.8 cents per month for 12-months (an annual total of 58 cents). This estimate equates to a
14 0.06% change over current residential billing rates.

15 **4. NW Natural Shareholders Contribution to the Smart Energy
16 Demonstrates the Company’s Commitment to the Success of this
17 program pilot.**

18 NW Natural paid all the start-up costs incurred in 2007, which were approximately
19 \$270,000. In addition, NW Natural absorbed the capital costs for the necessary
20 programming of customer information and phone systems. Finally, NW Natural
21 shareholders purchased the first blocks of Smart Energy offsets at the time the tariff was
22 approved. NW Natural provided a fixed contribution of \$77,000, which represents a total
23 offset of the natural gas used to heat its offices, service centers and shops for the entire
24 five-year period of the pilot program.

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26 ⁴ See NWN Advice No. OPUC 07-4/Miller/101/1-2.

1 It should be noted that the Smart Energy program poses shareholder risks unique to
2 the natural gas industry. Unlike the educational component of an electric renewable
3 program, which enhances the “clean-energy” image of electricity, the educational
4 component of this program entails educating customers about how their natural gas use
5 emits carbon dioxide associated with climate change. This very important education
6 presents a significant business risk to NW Natural.⁵ In light of this risk, and the broad
7 customer benefits provided as described above, NW Natural’s proposed deferred
8 accounting treatment, for later inclusion in rates, represents an appropriate sharing of costs
9 among the Company, program participants and eligible customers.

10 **C. Proposed Accounting.**

11 During the period of deferral, NW Natural proposes to account for the deferred
12 expenses related to the Smart Energy program by recording the deferral in a sub-account of
13 Account 186 (Miscellaneous Deferred Debits). In the absence of deferred accounting, the
14 Company would record Smart Energy program educational expenses in the appropriate
15 sub-account of FERC Account 401. Ratemaking treatment of deferred amounts will be
16 addressed in a future rate proceeding.

17 **D. Estimate of Amounts.**

18 The Company estimates the amount to be recorded in the deferred account for the
19 upcoming 12 month period will be approximately \$475,000, as detailed in Table 1.

20 **E. Entries Deferred under UM 1327 to-date**

21 In 2008, the Company deferred \$621,000 for start up and communications costs as
22 detailed in Table 1.

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26 ⁵ See NWN Advice No. OPUC 07-4/Miller/100/6-7.

1 **F. Reason for Continued Deferred Accounting**

2 The Company requests continued authorization to defer accounting for Smart Energy
3 as outlined in Table 1 so that the Company can recover the costs associated with
4 successfully communicating its Smart Energy Pilot Program. The Company's first program
5 year was successful, having enrolled 1% of residential customers and 0.1% of commercial
6 customers. The successes and accomplishments of Smart Energy's first program year are
7 best summarized in its 2007-2008 Annual Report which was filed on October 30, 2008. A
8 copy of this report is attached to this application as Exhibit A. NW Natural seeks the
9 continued success of this program – meaning customers will continue to be educated on
10 climate change, how to effect a change in their carbon footprint through reduced usage and
11 the availability to offset their remaining usage through the purchase of a carbon offset
12 product. Success also means the Company will continue to gain an understanding of
13 carbon offset project development in this interim before carbon legislation is enacted. The
14 Company believes that approval for reauthorization of deferred accounting will allow the
15 Company to continue the conversation with customers about climate change and Smart
16 Energy, and will strengthen the program's chances of being self-funding by the end of the
17 five year pilot program.

18 **V. CONCLUSION**

19 NW Natural respectfully requests that, in accordance with ORS 757.259, the
20 Commission authorize the Company to defer the expenses described in this Application.

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DATED: December 3, 2008.

NW NATURAL GAS COMPANY

/s/ Inara K. Scott

Inara K. Scott
Manager, Regulatory Affairs
220 NW Second Ave
Portland, OR 97209

OPUC DOCKET UM 1327

EXHIBIT A



SMART  **ENERGY™** *Presented by NW Natural*

**NW Natural Annual Report on the
2007-08 Smart Energy™ Program Year**

INTRODUCTION

NW Natural is proud to be the first stand alone gas utility in the United States to offer its customers the opportunity to offset their environmental footprint through the purchase of carbon offsets. The Smart Energy™ program was launched September 1, 2007, under the Company's Schedule 400. Under this Schedule, residential and commercial customers may choose to purchase high quality carbon offsets. These offsets are acquired through the development of regional biogas projects. The Company has partnered with the Climate Trust, a nationally recognized leader in the carbon offset industry, which will quantify, verify and retire each carbon offset.

The Smart Energy™ campaign educates customers that it is environmentally responsible to reduce natural gas use when possible and to offset the rest. This is a bold and wise message that will ultimately serve Oregon well and prepare us for future carbon legislation. The Company credits the Commission and its Staff for establishing the framework through decoupling which allows the Company to present this message of efficient and sensible gas usage.

According to the terms and conditions of Schedule 400, NW Natural is annually required to present the participation details, an analysis of the funds collected and expenditures related to the product, and a review of the offset expenditures by The Climate Trust, all of which are contained herein.

HIGHLIGHTS

- NW Natural set an ambitious goal of enrolling 0.75% residential and 0.05% commercial of our customers. While it took tremendous effort we succeeded in meeting our enrollment goals.
- We contracted with The Climate Trust, one of only two U.S. based companies recognized as a provider of quality carbon offsets in a 2006 international study produced by Trexler Climate + Energy Services, Inc. for the non-profit organization Clean Air Cool Planet.
- To demonstrate commitment to this program's message, NW Natural invested enough to offset five years of its total carbon emissions from natural gas used in heating our facilities.
- We hired a full time Smart Energy™ Program Manager.
- The Company partnered with Energy Trust of Oregon (Energy Trust) on a community challenge in Corvallis where we educated the community on the need to both reduce and offset energy use. We are on track to meet the one year goal of homeowners and businesses offsetting 3% of natural gas consumed in Corvallis by March 2009.
- The Company engaged numerous farmers in productive discussions and plans to break ground by the end of the year with its first biodigester, in part funded by Smart Energy™ participants.

TOTAL ACTIVE ENROLLMENTS

Enrollment in the Smart Energy™ program is detailed in Table I. As of August 31, 2008, we met our first-year enrollment goal for both residential and commercial customers. A total of 5,853 customers have enrolled in Smart Energy™. When the program was being developed in late 2006, we expected our customer base to grow more than it has. Nevertheless, we have surpassed our enrollment goal of 0.75% of residential customers and 0.05% of commercial customers. The total enrollment of 5,853 participants is made up of 5,783 residential customers and 70 commercial customers. Of the 5,783 residential customers enrolled, 3,092 or 53% have selected the volumetric option.

Table I demonstrates enrollments as of August 31, 2008.

Table I – Enrollment

	GOAL			Actual		
	# Customers	% of Customers	Enrollments	# Customers	% of Customers	Enrollments
Residential	608,800	0.75%	4,566	592,702	0.98%	5,783
Commercial	62,000	0.05%	31	61,639	0.11%	70

CARBON REDUCTION

Total carbon reduction for our first program year will be approximately 13,733 tons when offsets are purchased and retired.

THE CLIMATE TRUST

OFFSET FUNDS

As of August 31, 2008

All offset funds transferred to The Climate Trust to date are unspent and kept in a separate interest bearing money market account with ShoreBank Pacific.

The total amount transferred to the program account managed by The Climate Trust this program year is \$171,659, which includes offset purchases for program participants and NW Natural. This total is itemized in Table 2.

Table 2 – Carbon Offsets in cost and tons

Offsets	Dollars	Offsets (tons)
NWN Shareholders	\$77,000	6,160
Smart Energy™ Participants	\$94,659	7,573
	\$171,659	13,733

ACTIVITIES

The Climate Trust accomplished the following:

- Negotiated and signed an agreement with NW Natural for the procurement of high quality offsets for Smart Energy™ customers
- Established accounting procedures to ensure proper tracking of Smart Energy™ funds
- Developed a tool to approximate potential greenhouse gas emissions reductions acquired from projects
- Met with potential biodigester developers and stakeholders including Energy Trust of Oregon, Oregon Department of Agriculture and individual farmers
- Worked with the NW Natural employees to assess development opportunities
- Provided NW Natural with expert assistance on offset valuation and communications
- Reviewed and assessed methodologies from Clean Development Mechanism (CDM), California Climate Action Registry (CCAR), Regional Greenhouse Gas Initiative (RGGI), and Environmental Protection Agency (EPA) Climate Leaders

COMMUNICATION AND CUSTOMER EDUCATION

Given the complexity and relative unknown nature of carbon offset programs, our communication efforts focused on broadly educating customers about global warming and the need to reduce greenhouse gas emissions. We used advertising and public relations to establish a general awareness. Later, we tried to obtain enrollments using direct communications such as traditional mail and email channels, customer communications in the bill, and community outreach and events.

Our paid media strategy was designed to garner a large reach during the April through September time period. The Company's goal was to touch our highest density service territories through multiple vehicles (radio, print, transit, online). Through this strategy, we focused on two key messages to encourage enrollment: *Reduce What You Use, Offset the Rest* speaks to promoting energy efficiency and offsets; *Fight Global Warming One Cow Pie at a Time* is accompanied with an explanation of the environmental benefits of Smart Energy™.

The paid media campaign was as follows:

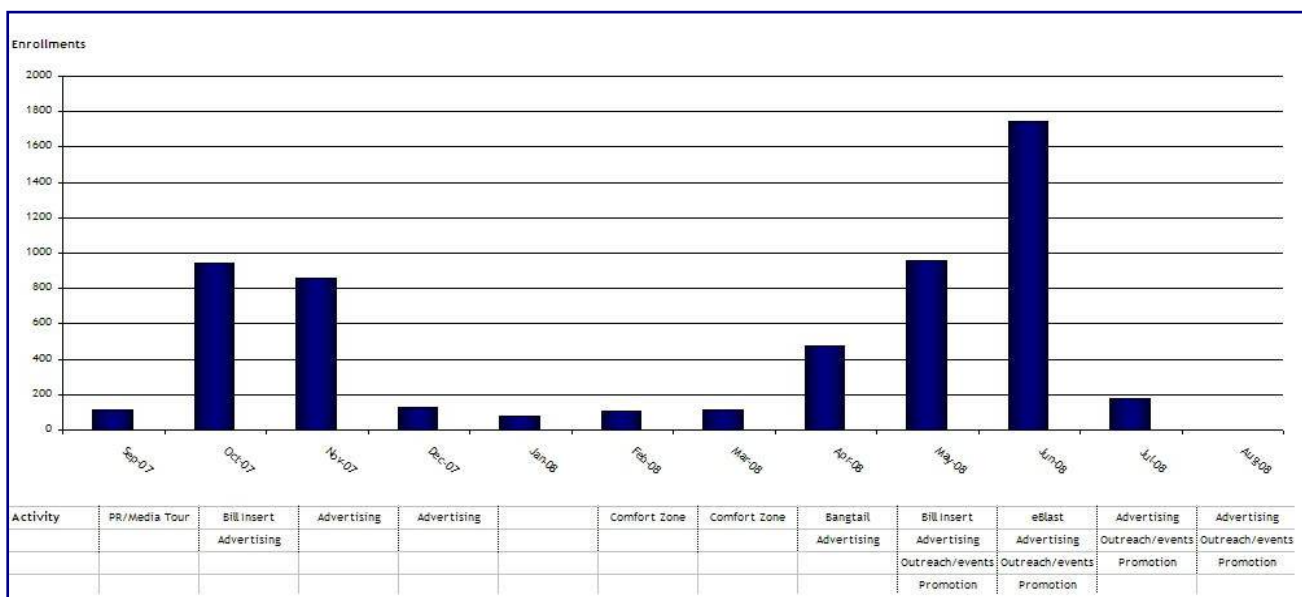
- Radio 2,400,000 impressions
- Print 3,901,220 impressions
- Transit/Outdoor 19,071,320 impressions
- Online 5,000,000 + impressions
- Customer communications 3,000,000 + impressions

Our paid efforts were supported through earned media outreach and Public Relations. These efforts produced:

- Broadcast 562,593 impressions
- Print 24,759,307 + impressions

These communication efforts were effective at increasing customer participation. As represented in the chart below, when multiple communication vehicles were employed during the same month, we experienced more enrollments. The opposite is also true. That is, when we are not delivering messages to our customers, we have fewer sign-ups. In 2009, we plan to strategize program messaging based on what we have learned in this first program year.

Chart I – Communication and Enrollment



THE SMART ENERGY™ PROGRAM YEAR SPENDING

The charts below demonstrate the costs associated with Smart Energy's™ first program year. This first program year included non-recurring start-up costs for program development, capital improvements to the Company's information and phone systems made to accommodate the program, and initial educational materials. All of the 2007 one-time costs were paid for by NW Natural shareholders.

Chart 2 – Costs: Education

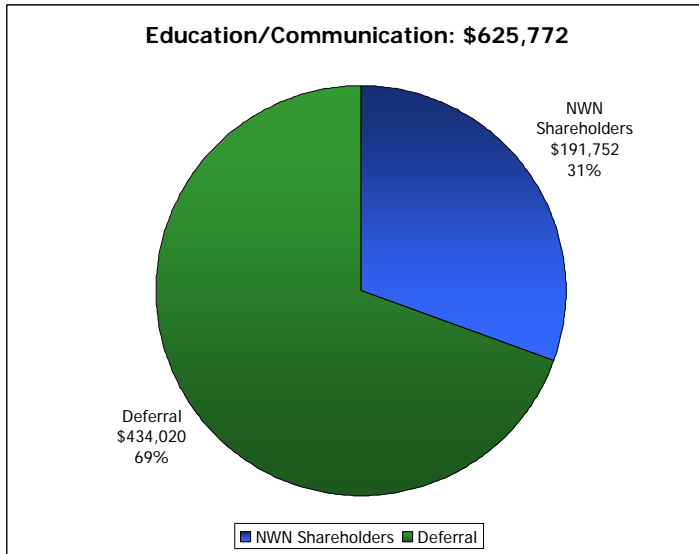


Chart 3 – Costs: The Climate Trust Fees

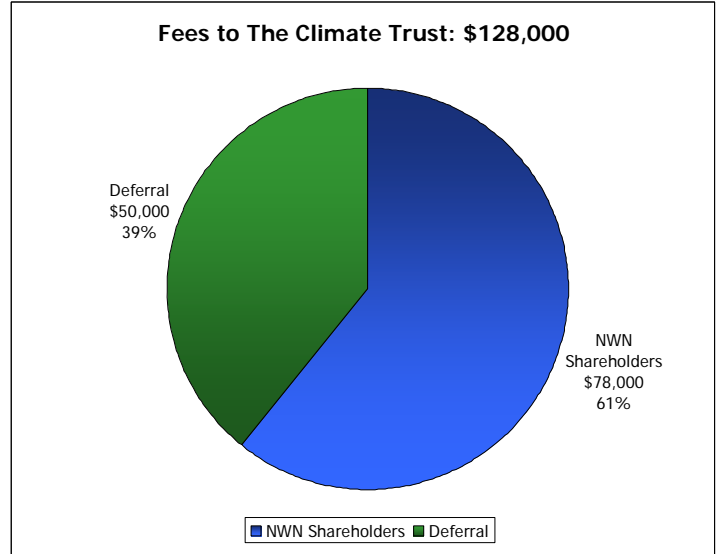


Chart 4 – Carbon Offsets

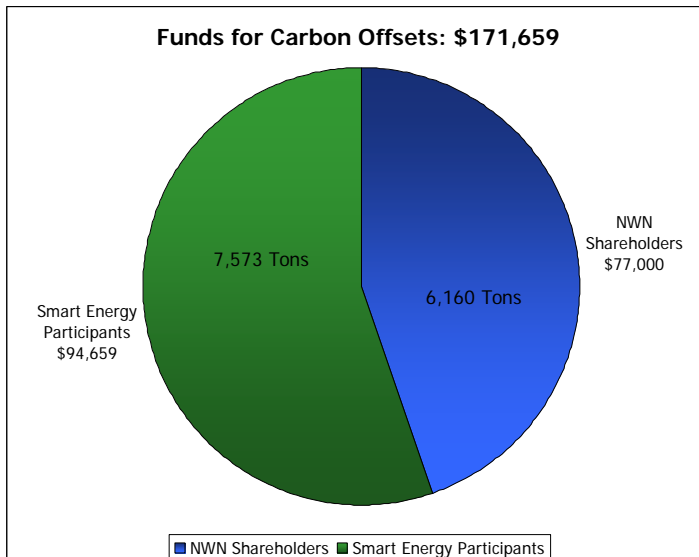


Chart 5 – Total Expenditures

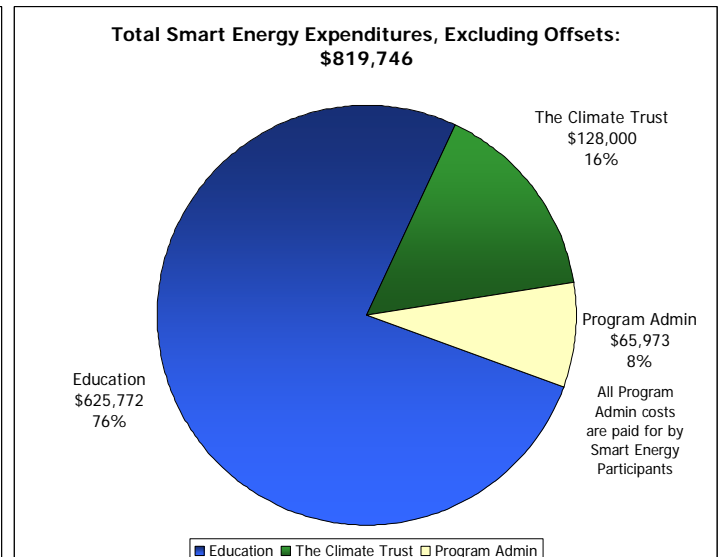


Chart 2 illustrates that the costs spent on customer communications and education totaled \$625,772 and were shared between customers and shareholders. Currently, the costs shared with customers are deferred for later inclusion in general rates.

Chart 3 provides an analysis of fees paid to The Climate Trust during the program year. Per the agreement between the Company and The Climate Trust, a total of \$100,000 for the program implementation will be

paid in 2008 calendar year. The Climate Trust invoices the Company quarterly for \$25,000. As of August 31st, the end of the program year, the Company has been invoiced for \$50,000. This expense has been deferred for later inclusion in general rates. Company shareholders paid the 2007 implementation fees of \$78,000.

Chart 4 details the funds sent to The Climate Trust for the purchase and retirement of offsets and the resulting tons offset. Smart Energy™ participants have funded \$94,659 towards the offset of 7,573 tons of carbon emissions. In addition, NWN Natural shareholders have contributed \$77,000 to offset 6,160 tons representing a total offset of the natural gas used to heat our offices, services centers and shops for the five-year period of the Smart Energy™ pilot program. Additional detail is provided above in Table 2.

Chart 5 summarizes all costs related to the program excluding the funds for offsets. A total of \$819,746 was spent for the communication and education of customers, Climate Trust fees and program administration. 76% of all costs were for customer education and communication. Program administration costs of \$65,973, 8% of total costs, were funded totally by program participants. Additional breakdown of these costs are provided in Table 3.

Table 3 – Expenses by type and source

<u>Expenses</u>	NWN Shareholders	Deferral	Smart Energy™ Participants	Total
Education	\$191,752	\$434,020	\$0	\$625,772
The Climate Trust	\$78,000	\$50,000	\$0	\$128,000
Program Admin	\$0	\$0	\$65,973	\$65,973
Total	\$269,752	\$484,020	\$65,973	\$819,746

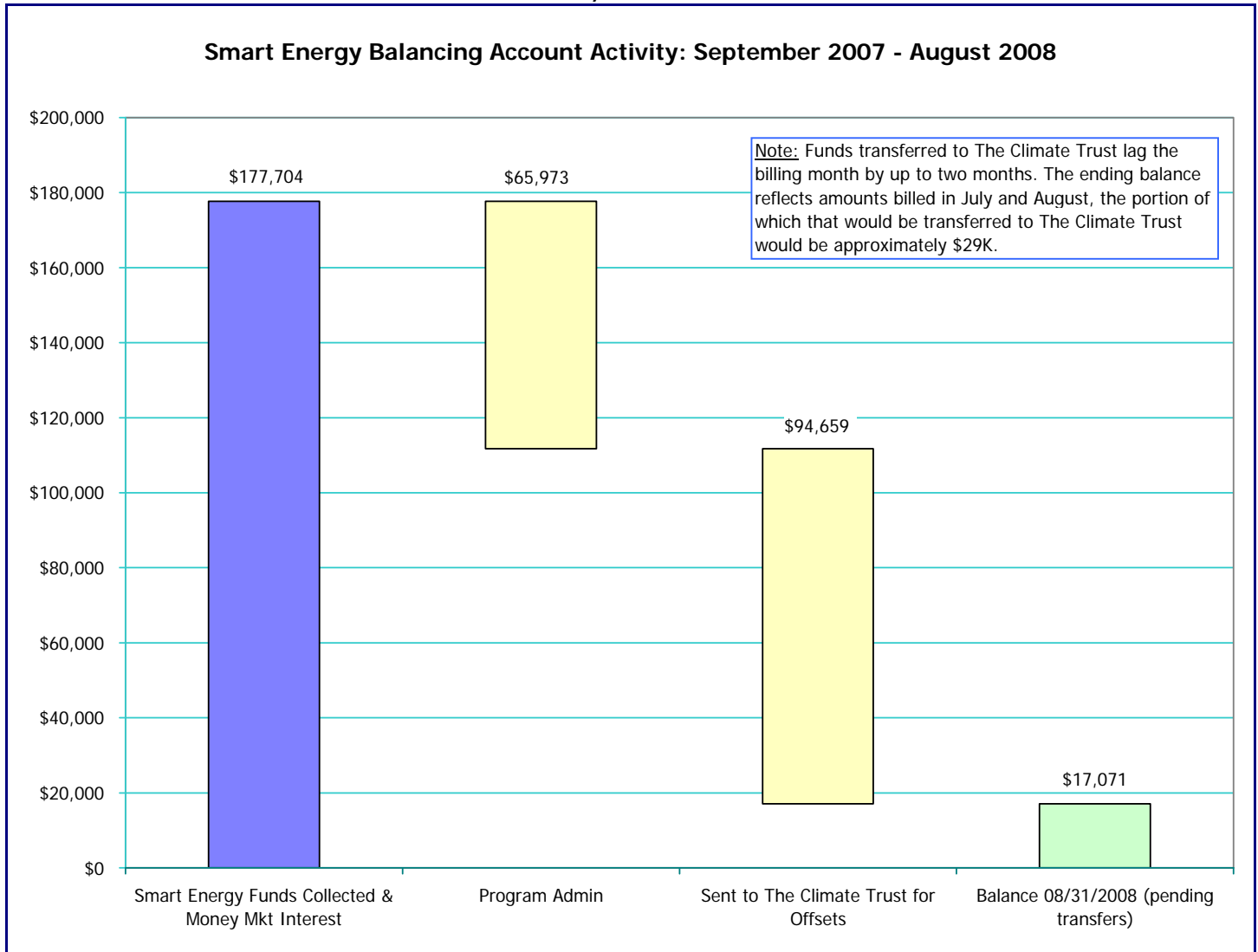
ANALYSIS OF PARTICIPANT FUNDS COLLECTED

The Company uses a balancing account to record the activity of the Smart Energy™ program. Increases (credits) to the account include monthly receipts from customer billings and money market interest on the bank account the Company has set up solely for Smart Energy™ funds. Decreases (debits) to the account include the cost of the program administration and the transfer of funds to The Climate Trust for the purchase of offsets. Program administration costs consist primarily of the payroll and payroll overheads associated with the program manager. Prior to the hiring of the program manager, we incurred costs for a temporary employee who acted as program manager. Schedule 400 provides for the payment of program administration costs from funds collected.

The Company transfers 70% of the funds collected from participants to The Climate Trust. This reflects the projected split of program administrative costs and funds for offset purchases over the course of the five year pilot program. This 70% was determined when the program price was originally established. Using 70% will mitigate the funding mismatch due to the seasonality of Smart Energy™ funds collected (half of the participants enrolled in the program select the volumetric option) versus the fairly fixed expenses of program administration. It is also anticipated that the use of the 70% transfer practice will mitigate additional funding/cost mismatches in later years of the program, when customer education and communication expenses will be paid by program participants.

The activity and current balance of the Smart Energy™ balancing account is detailed in Chart 6. The ending credit balance reflects the lag that occurs between when customers are billed and when funds are ultimately transferred to The Climate Trust. Collections through June have been transferred. The portion of July and August collections due to be transferred are approximately \$14,500 and \$14,400, respectively, and will be transferred in October and November, respectively.

Chart 6 – Analysis of funds collected

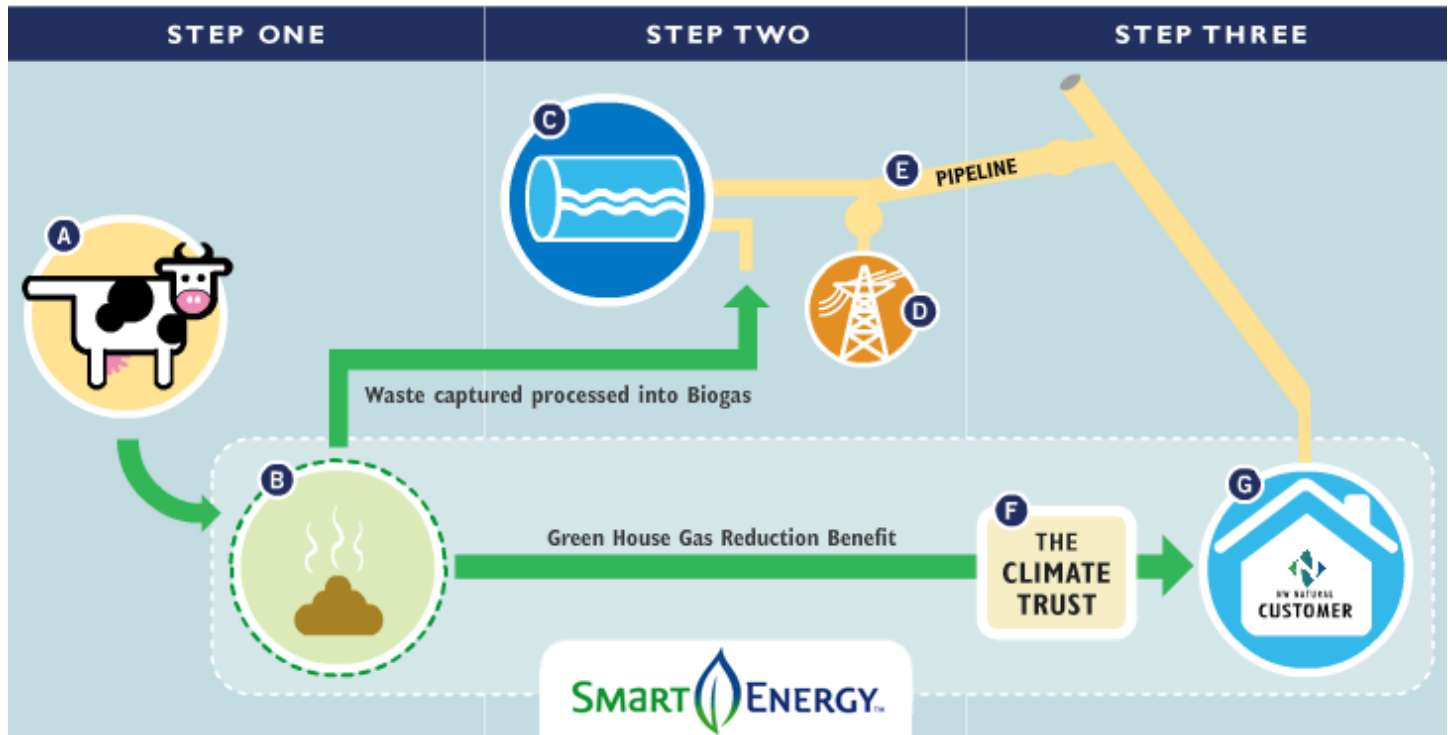


CARBON OFFSET PROJECTS

BIODIGESTERS

The Smart Energy™ Program offers customers the option to purchase carbon offsets acquired through high quality, project-based emissions reductions. NW Natural chose to focus on developing biodigester projects since these projects capture methane which is at least 21 times more potent of a greenhouse gas than carbon dioxide. Biodigestors also produce biogas which can be used as a fuel onsite to replace propane or oil, can be eventually used as a pipeline supply or can be used to generate electricity. Ultimately, Smart Energy™ funding will support the development of regional biodigester projects, helping to protect the viability of large and small Oregon farms that need a cost-effective way to manage livestock waste.

The graphic below illustrates how a biodigester produces biogas and reduces methane emissions.



BIODIGESTERS – PROJECT STATUS

For the reasons stated above, NW Natural is committed to the development of regional biodigesters. We have learned that our efforts are accelerated when we engage partners like the Bonneville Environmental Foundation (BEF). Besides partnering with BEF in Project I, NW Natural continues to explore other partnerships that will help move biodigesters forward. To date, the Company is in detailed discussions on the following two projects:

Project I

- Project I is a commercial demonstration project. The agreement to proceed has been signed by the participants and a public announcement is expected in November. We expect to break ground on the project before the end of the year. On this schedule the biodigester would be operational in early March 2009. This project is being developed through a partnership with NW Natural, BEF, the owner of the dairy operation where the biodigester will be sited and a biodigester technology company. This project will convert waste into biogas that will then be used to offset onsite propane use for the dairy operations. Conservative estimates suggest this first test unit will reduce carbon emissions by 3,300 tons annually. The Climate Trust will purchase and retire the offsets associated with this project on behalf of Smart Energy™ customers.

Project I is sited on a large farm that could accommodate another 12-15 biodigesters, potentially capturing an additional 40,000 plus tons of carbon each year. Future projects at this site will consider a more diverse use of the biodigester-produced biogas including using the gas to run a gas chiller (for milk cooling), to generate electricity, or to offset a neighbor's energy needs.

Project II

- The second project is with a small dairy operation that has 1,500 cows (750 at 2 separate farms). In the first phase, two farms will be sited with biodigesters. NW Natural is serving in an advisory role to this project. In addition to the 4,500 tons of carbon that will be captured annually, the Company expects to gain the experience and understanding necessary to replicate this solution for other small sustainable farms. As this project moves forward, The Climate Trust will lead the effort to quantify, verify and retire offsets on behalf of Smart Energy™ customers.

PROGRAM ADJUSTMENTS

We refined our financial forecast based on knowledge gained during this first program year. Our initial forecast assumed the total number of participants for each year's enrollment goal would contribute a minimum of \$6 per month for all twelve months. In reality, most enroll between April and August. This errant assumption resulted in fewer revenues than anticipated. This means that meeting our long term revenue goal may require more time than initially projected. However, we are confident that we can generate more revenue in less time by increasing the number of total participants each year through aggressive and focused educational efforts.

SUMMARY

NW Natural believes this first program year was a success. We reached our participation goal, and in so doing, we observed enrollment patterns based on the media channels used and the frequency of the delivered message. We also learned where our initial budget assumptions require refining. The Company made excellent progress towards the development of biodigesters through partnering with other stakeholders and expects to learn more in the following program years as we continue to make strides toward the development of additional regional biogas development.

OPUC DOCKET UM 1327

EXHIBIT B



CERTIFICATE OF SERVICE

I certify that I have this day served the foregoing NOTICE OF APPLICATION FOR REAUTHORIZATION TO DEFER EXPENSES FOR SMART ENERGY PILOT PROGRAM COMMUNICATION COSTS upon all parties of record in this proceeding (UM 1327), by e-mailing an electronic copy to the following parties or attorneys of parties:

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DATED at Portland, Oregon, this 3RD day of December 2008.

/s/ Jennifer Gross

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