ITEM NO. 2

PUBLIC UTILITY COMMISSION OF OREGON
STAFF REPORT
PUBLIC MEETING DATE: January 28, 2015

REGULAR X **CONSENT** ____ **EFFECTIVE DATE** February 1, 2015

DATE: January 16, 2015

TO: Public Utility Commission

FROM: Erik Colville

THROUGH: Jason Eisdorfer and Aster Adams

SUBJECT: AVISTA UTILITIES: (Advice No. 14-11-G) Establish Optional Compressed Natural Gas Service.

STAFF RECOMMENDATION:

Staff recommends the Commission approve Avista Utilities' (Avista) application for Waiver of Less Than Statutory Notice (LSN), and it's request to make Advice No. 14-11-G (aka Schedule 441) effective on and after February 1, 2015, subject to the following condition:

> Schedule 441 is effective for a period of two years. Prior to the end of the two-year period, the Commission will determine whether the service should be continued as is, modified, or discontinued.

DISCUSSION:

Avista filed Advice No. 14-11-G (Schedule 441) on December 11, 2014, proposing to establish an optional compressed natural gas (CNG) schedule. Avista filed a revised tariff and an LSN on January 15, 2015. Staff's investigation focused on analysis of the risk that non-Schedule 441 customers would absorb some costs of this optional service, whether Avista's offering of CNG Service as a regulated service would affect competition of this service in Oregon, and whether provision of this service would result in a net benefit to Avista ratepayers. As discussed more fully below, Staff is satisfied that sufficient safeguards are in place to prevent subsidization of CNG Service by non-Schedule 441 customers. Further, Staff concludes that Avista's offering of this service as a regulated service will not harm competition in Oregon, and that Avista ratepayers will receive a net benefit from the service.

<u>The Filing</u>

If approved, Schedule 441 will allow Avista to provide company-owned and maintained compression and dispensing equipment on customer-owned property for the purpose of allowing those customers to fuel their Natural Gas Vehicles (NGV) fleet at specified pressures of up to 3600 pounds per square inch (psi). Customers under this optional, behind-the-meter service will continue to obtain natural gas service at approved tariffed rates. To receive CNG Service, customers will be required to enter into a Compressed Natural Gas Service Agreement (CNG Service Agreement).[1]

According to Avista, it is pursuing the CNG Service schedule in response to inquiries from public and private fleet operators interested in capturing the economic and operating advantages of using natural gas for transportation. Avista states that service under Schedule 441 will provide Customers with a turn-key NGV refueling facility (Facility) solution not otherwise available for providing the gas pressure required for vehicle fueling, without a significant upfront capital investment into compression facilities. Avista asserts that the increased availability of CNG in Oregon responsibly supports the State's interest[2] to improve air quality, lower greenhouse gas emissions and reduce its dependency on higher-cost, carbon-based fuels. In addition, Avista states the proposed CNG Service removes a potential barrier to CNG adoption for fleet operators by removing the significant upfront capital investment that otherwise would be required of the Customer, and also assigns operating responsibility for the maintenance and repair of high-pressure facilities to Avista.

Avista proposes that all of the costs associated with this optional service be borne by those customers taking service under the schedule, and to the extent any costs are unrecovered, Avista would not pass those costs to non-participating ratepayers. During engagement with Staff and the Citizens' Utility Board of Oregon (CUB) following the initial filing, Avista committed to account for and redirect to non-utility operations any initial development and unrecovered[3] ongoing incremental and shared core utility costs so that those costs are not passed on to ratepayers who do not take the CNG Service.

The terms of service and pricing for CNG Service will vary for each installation and will be laid out in the Customer's CNG Service Agreement. The Customer will be billed a monthly facility charge designed to recover all equipment, permitting and siting costs. Avista proposes that the monthly facility charge be derived by multiplying the actual project costs by an annual cost recovery factor, divided by 12. The cost recovery factor

---

[1] A copy of the CNG Service Agreement is attached to Avista's application as Attachment A.

[2] Avista's proposal to offer CNG Services to qualified NGV Fleet Operators advances Governor Kitzhaber's energy plan, and is consistent with Oregon State Senate Bill 844.

[3] The word "unrecovered" here is intended to represent that portion of ongoing incremental and shared core utility costs not included in the CNG Service Agreement monthly Scheduled Maintenance Charge.

is designed to recover in each year the depreciation on the CNG equipment plus Avista's financing costs at its authorized return, for the investment made on behalf of the customer.

In addition to the CNG Facility Charge, the customer will be responsible for charges associated with the Facility's scheduled maintenance and base charges for administrative services, the Scheduled Maintenance Charge. Base charges for administrative services costs can include, but are not limited to, costs for managing the program, performing customer credit evaluations, billing, warehousing and managing inventory of spare parts, monitoring, and dispatching, and any charges for other services such as unscheduled maintenance or back-up natural gas service (offered if the flow of natural gas to the Facility is disrupted) that may be provided by Avista. All charges for natural gas delivered to the metering point upstream of the Facility will be billed to the customer in accordance with the applicable rate schedule under tariff.

To receive CNG Service, customers must enter into a CNG Service Agreement. This CNG Service Agreement is comprised of three sections (Articles 1, 2, and 3). Article 1 is the Feasibility Evaluation section. This section requires the customer to operate in good faith when providing Avista information about the characteristics of its property and CNG consumption projections. Article I also provides for Avista's preliminary estimate of cost for CNG Service. If Avista determines that a CNG Facility could be sited on the customer's premise, and the customer approves of the preliminary cost estimate, the second section of the CNG Service Agreement (Article 2 - Site Design and Permit Evaluation) will become effective.

Article 2 provides the terms and conditions for permitting, site preparation, and facility design and will refine the overall cost of providing the Facility. The third and final section of the CNG Service Agreement (Article 3 – Construction and CNG Services) sets forth all of the terms of service to be performed by the customer and Avista for a ten-year contract period.

The standard components of the Facility provided under Avista's CNG Service will include a high-efficiency compressor unit, a CNG storage vessel(s), and a fast-fill refueling dispenser. The customer may elect to add compression capability, storage capacity, additional fast-fill dispensers or time-fill dispensers which are designed for overnight refueling. Regardless of the equipment configuration, the customer will be solely responsible for all of the costs associated with the selected equipment. Customers may choose equipment that will provide CNG Service not only to its fleet, but also make CNG available to other customers.

Staff's Review Criteria

Criteria Staff considered in reviewing and recommending whether to allow Avista to provide CNG Service as a regulated utility service include:

a. Is there is a need for CNG market development?
b. Does participation by a regulated utility impede CNG market competition?
c. Does the proposal aid in CNG market development?
d. Do the rates proposed cover the costs for offering the service or is it a subsidized rate?
e. Does the proposal allow an exit strategy once the CNG market is developed?
f. Is there a net benefit to ratepayers?

These review criteria are consistent with those used in Staff's review of Northwest Natural's High Pressure Gas Service filing (NWN HPGS) approved by the Commission in January 2014 in Order No. 14-014.[4] Based on Staff's analysis and discussion below, Staff recommends allowing Avista to provide CNG Service as a regulated utility service.

Staff's Analysis

Staff's review of the CNG Service tariff filing included the filing itself, the cost of service work papers, and the revised pages filed in response to Staff and other party input.

a. Is there is a need for CNG market development?

In Order No. 14-014 authorizing NWN to provide HPGS as a regulated service, the Commission found there is no competitive market, robust or otherwise, in Oregon for CNG fueling services.[5]

b. Does participation by a regulated utility impede CNG market competition?

The Commission found in Order No. 14-014 that it is not persuaded that regulated utility participation in the market will act as a disincentive to competitive market entry. In fact, the Commission found evidence tending to prove the contrary to be persuasive.[6]

---

[4] Northwest Natural Advice No, 13-10, Docket No. UG 266.

[5] Order No, 14-014 at 8: "The record in this case clearly shows that there is no competitive market, robust or otherwise, in Oregon for CNG fueling services. At present, despite requests for CNG fueling from fleet owners, there are no third-party providers of HPGS in Oregon. All the existing 28 CNG fueling stations are privately owned and operated by individual fleet owners solely for their own use, leaving most businesses and public bodies that operate fleets without access to CNG fueling."

[6] Order No. 14-014 at 9: "We are not persuaded by Clean Energy's assertion that NW Natural's participation in the market will act as a disincentive to competitive market entry. In fact, we find evidence tending to prove the contrary to be persuasive. We agree with ODOE that, given the lack of a competitive market and the experiences in other states, NW Natural's HPGS proposal may well establish demand for

In addition, the Commission found in Order No. 14-014 that it is not persuaded that regulated utility participation in the market will act as a disincentive to competitive market entry. In fact, the Commission found evidence tending to prove the contrary to be persuasive.[7]

c. *Does the proposal aid in HPGS market development?*

The Commission found in Order 14-014 that a preponderance of the evidence shows the CNG fueling market in Oregon may not develop in the absence of utility company participation and that utility company participation in the market may well stimulate market development for CNG fueling station by facilitating fleet conversions.[8]

d. *Do the rates proposed cover the costs for offering the service or is it a subsidized rate?*

A key consideration in answering this question is to analyze the rates proposed by Avista given that the rate offering is an "above-the-line" service, i.e. recovered from ratepayers. The answer to this question involves a comparison of the Avista incremental and shared core utility costs associated with this offering as compared to the revenues received. A rate is subsidized if the rate does not fully recover the incremental and shared costs associated with the offering. As the CNG Service tariff is structured the CNG Customer will be billed a monthly facility charge designed to fully recover all capital (equipment, permitting and siting) costs. Avista proposes that the monthly facility charge be derived by multiplying the actual project costs by an annual cost recovery factor, divided by 12. The cost recovery factor is designed to recover in each year the depreciation on the CNG equipment plus Avista's financing costs, at its authorized return, for the investment made on behalf of the customer.

Staff and CUB confirmed with Avista that the monthly scheduled maintenance charge a CNG customer will pay under Schedule 441 includes cost recovery for base charges for administrative services, (which includes but is not limited to costs for managing the program, performing customer credit evaluations, billing, warehousing and managing

---

CNG fueling stations by facilitating fleet conversions for those entities lacking their own facilities. We find that a preponderance of the evidence shows that the CNG fueling market in Oregon may not develop in the absence of utility company participation and that participation in the market by NW Natural may well stimulate market development for CNG fueling station by facilitating fleet conversions. This demand may be necessary to attract third parties to Oregon."

[7] See footnote 4 above.

[8] Order No. 14-014 at 9: "We find that a preponderance of the evidence shows that the CNG fueling market in Oregon may not develop in the absence of utility company participation and that participation in the market by NW Natural may well stimulate market development for CNG fueling station by facilitating fleet conversions. This demand may be necessary to attract third parties to Oregon."

inventory of spare parts, monitoring, and dispatching). In response to the concerns raised by Staff and CUB, Avista committed to account for and redirect to non-utility operations any initial development and any other ongoing incremental and shared core utility costs so that those costs are not passed on to the general ratepayer population. As a note of clarity, Staff understands that the accounting for and redirecting of any initial development and any other ongoing incremental and shared core utility costs includes marketing expenses, Avista's activities to promote the service to the Public Utility Commission of Oregon (OPUC), and CNG Service feasibility study preparation.

Staff also explored potential costs and risks for ratepayers as additional aspects of cross-subsidization. In Staff's review of potential cost and liability risks for ratepayers the following were identified: 1) CNG Service equipment rehabilitation costs before redeployment, site work costs (earthwork, underground utilities, equipment foundations, paving, landscaping, etc.); 2) liability from site and equipment sizing, and; 3) liability from vehicle fueling activities.

1) CNG equipment may need to be rehabilitated before redeployment if a CNG customer defaults on the CNG Service Agreement with Avista. In addition, if CNG equipment were to be redeployed, the associated site work would be left behind on the customer's site. As the CNG tariff is structured the cost for the equipment rehabilitation would be paid for by a new CNG customer, if one is found, but site work costs could be passed on to ratepayers. Rate Schedule 441 Special Condition 9 and CNG Service Agreement Article 4 require potential CNG customers to undergo a credit review and provide financial assurance if found to be credit deficient. Given the credit review process Staff finds it unlikely that CNG customers will default on the CNG Service Agreement with Avista. In addition, for resulting costs to be passed on to ratepayers, Avista would be required to justify in a rate case that the costs were prudently incurred and that the associated activity is used and useful to ratepayers. While there is a possibility of the equipment rehabilitation and site work costs being passed on to ratepayers Staff considers it remote. As a result, Staff concludes this risk is minimal and reasonable.

2) According to Avista, site size is dictated by physical limitations of the equipment and National Electric Code, National Fire Protection Association Publications 52 and 30A, Oregon Building Code, and Oregon Mechanical Code requirements. Given the extensive code requirements to be met Staff concludes the possibility for incorrectly sizing the CNG site is remote. While there is a possibility for costs associated with incorrect site sizing to be passed on to ratepayers, Avista would be required to justify in a rate case that the costs were prudently incurred and that the associated activity is used and useful to ratepayers. As a result, Staff concludes this risk to ratepayers is minimal and reasonable.

CNG equipment sizing (capacity and pressure) errors are a possibility. Given that the CNG equipment will be sized based upon CNG customer-provided information, and that the CNG customer must agree to the equipment sizing when executing the CNG Service Agreement with Avista, Staff concludes the potential for ratepayer risk is limited. While Staff agrees there is a possibility for costs associated with incorrect equipment sizing to be passed on to ratepayers, Avista would be required to justify in a rate case that the costs were prudently incurred and that the associated activity is used and useful to ratepayers. As a result, Staff concludes this risk to ratepayers is minimal and reasonable.

3) Liability related to CNG customer fueling activities could potentially put ratepayers at risk for associated costs. The basic CNG excludes the devices that connect to a natural gas vehicle for fueling, those devices being the responsibility of the CNG customer. The CNG Service Agreement Article 3 includes an optional provision for Avista to supply, install and maintain (but not own) the vehicle fueling devices. Staff identified this optional provision as a potential source of liability related to CNG customer fueling activities. Staff recognizes CNG Service Agreement Article 8 Liability and Indemnification offers a reasonable reliance for associated liability concerns. Also, for costs related to vehicle fueling liability to be passed on to ratepayers, Avista would be required to justify in a rate case that the costs were prudently incurred and that the associated activity is used and useful to ratepayers. As a result, Staff concludes this risk to ratepayers is minimal and reasonable.

Following exploration of costs, and risks to ratepayers Staff concludes the potential benefit discussed below is sufficient compensation to ratepayers for the small amount of potential risk and costs.

e. Does the proposal allow for an exit strategy once the CNG market is developed?

Avista's participation in the CNG market as a regulated utility will be subject to rate case proceedings. The Commission has wide discretion to observe, modify, and end Avista's participation in the CNG market, as provided for in ORS 756.568. In Order No. 14-014, the Commission authorized NWN to offer HPGS to new customers for a two-year period, after which, the Commission would revisit the offering to determine whether the regulated service should continue, or whether it should be modified or discontinued on a going-forward basis.[9] Staff has recommended such a limitation as a condition for approval of Avista's CNG Service.[10]

---

[9] Order No, 14-014 at 10: "Accordingly, we condition our approval of NW Natural's HPGS to a period of two years from the effective date of the tariffs. Following that period, we will revisit the offering to determine whether the regulated service should continue, or whether it should be modified or

f. Is there a net benefit to ratepayers?

The proposed CNG Service tariff establishes rates that recover the direct incremental costs of the tariff offering. Avista has committed to account for and redirect to non-utility operations any initial development and unrecovered ongoing incremental and shared core utility costs. A net benefit to ratepayers accrues through sales of natural gas to the new CNG Service customers. These sales will make the same contribution to fixed costs as gas purchases by other commercial gas customers. By spreading these costs over a larger volume of sales, the amount of fixed costs that are recovered per unit of sales is reduced. Consequently, the new contribution to fixed costs will incrementally lower the portion of fixed costs currently being borne by the existing customer base. The Commission found this net benefit to be persuasive.[11] Therefore, Staff concludes the tariff provides a net benefit to Avista ratepayers.

Conclusion

No stakeholder has come forward to oppose Avista's request to offer CNG Service as a regulated service. In January 2014, the Commission approved NWN's request to provide HPGS as a regulated service.[12] Staff's analysis and the discussion above show the proposed CNG Service tariff satisfies reasonable regulatory criteria. Staff therefore recommends, consistent with the Commission's order in NWN's HPGS docket,that Avista be allowed to provide CNG Service as a regulated utility service.

Staff identified three potential paths for going forward:

1. Approve the CNG tariff filing;
2. Approve the CNG tariff filing, with conditions; or
3. Suspend the CNG tariff filing and open a contested case docket,

---

discontinued on a going-forward basis. To assist that effort, we instruct our Staff to undertake an investigation of the CNG fueling market and NW Natural's participation in it, and to make such recommendations to the Commission as will further the growth of a robust competitive market. We specifically direct Staff to examine whether circumstances on which we based our decision have changed, and to report on the market development in parts of Oregon not served by NW Natural."

[10] Any CNG Service Customer that enters into a CNG Service Agreement with Avista prior to the expiration of the two-year period would continue to receive CNG Service under Schedule 441 until the expiration of the CNG Service Agreement.

[11] Order No. 14-014 at 7 and 8: "For these reasons, we find that NW Natural's provision of CNG fueling as a regulated service will provide a net benefit to other customers."

[12] Order No. 14-014 at 6: "We approve NW Natural's request. Although natural gas vehicle fueling is potentially a competitive business, CNG fueling is properly considered a utility service and may appropriately be offered under regulated tariffs. Moreover, NW Natural has structured its HPGS tariff rider in a manner that meets our requirements for a utility proposing to provide a regulated service in a potential competitive marketplace."

After considering the CNG Service tariff filing, the cost of service work papers, the revised pages filed in response to Staff's and CUB's comments, and interested party input, Staff concludes no further proceedings are warranted. As a result, Staff recommends the Avista proposed tariff should be allowed to go into effect, with a condition.

PROPOSED COMMISSION MOTION:

Avista's application for an LSN and its request for Advice No. 14-11-G, as revised January 15, 2015, to become effective on and after February 1, 2015, be approved, subject to the following condition:

> Schedule 441 is effective for a period of two years. Prior to the end of the two-year period, the Commission will determine whether the service should be continued as is, modified, or discontinued.