

**BEFORE THE PUBLIC UTILITY COMMISSION
OF OREGON**

UG 305

In the Matter of)
)
CASCADE NATURAL GAS)
CORPORATION,)
)
Request for a General Rate Revision.)
_____)

**OPENING TESTIMONY
OF THE
CITIZENS' UTILITY BOARD OF OREGON**

August 11, 2016



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OF OREGON**

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1 My name is Bob Jenks. My qualifications are listed in CUB Exhibit 101.

2 **I. Introduction**

3 Pursuant to Chief Administrative Law Judge Grant's prehearing conference
4 memorandum of May 23, 2016, the Citizens' Utility Board of Oregon ("CUB") submits
5 its Opening Testimony in UG 305. CUB has reviewed Cascade Natural Gas
6 Corporation's ("Cascade" or "the Company") filing in this request for a general rate
7 revision. In our Opening Testimony, CUB addresses the following issues:

- 8 1. The 2016 Test Year for 2017 Rates;
- 9 2. Wages and Salaries;
- 10 3. Cost of Capital and Capital Structure;
- 11 4. Long-Run Increment Cost Study ("LRIC");
- 12 5. Rate Spread; and
- 13 6. Rate Design

14 **II. 2016 Test Year for 2017 Rates**

15 This general rate case ("GRC") filing is unusual because, while the rate revision
16 requested will not be effective until 2017, this filing uses a 2016 test year:

1 Cascade is proposing calendar year 2016 as the test period. As a practical
2 matter, rates are anticipated to go into effect March 1, 2017; consequently,
3 2017 will be the first year rates will be in effect. However, we are unable
4 to project 2017 revenues and costs with any accuracy.¹

5 Ordinarily, CUB would not object to using a 2016 test year for 2017 costs,
6 because doing so would avoid a year of escalating costs. However, in this case, we find
7 the 2016 test year to be problematic.

8 Cascade claims that if it included 2017, the increased revenues would be offset by
9 a greater amount of increased costs:

10 If margin revenue increased by 1%, which is a reasonable expectation, the
11 increase in margin revenue would be approximately \$300,000. A typical
12 wage increase of 3% would offset half that amount while a simple
13 inflation calculation would offset the remaining half. For this reason the
14 selection of a 2016 test year yields conservative results.²

15 But this is based on an example, not on real analysis and this example assumes “a
16 typical wage increase of 3%,” which is three times the current inflation rate of 1.0%.³

17 CUB believes that actual financial projections for 2017 are more useful than this
18 example. The Oregon Public Utility Commission (“OPUC”) Staff asked the Company for
19 its financial statements on an ongoing basis. CUB Exhibit 102 demonstrates that the
20 Company projects ROEs that are above its authorized ROE in 2017 and 2018:

21	<u>Year</u>	<u>ROE</u>
22	2016	7.99%
23	2017	11.85%
24	2018	12.14%

¹ UG 305/CNGC/200/Parvinen/3.

² UG 305/CNGC/200/Parvinen/4.

³ Calculation for 12 months ending June 2016, *available at*:
<http://www.usinflationcalculator.com/inflation/current-inflation-rates/>

1 Because rates in this case will be effective in 2017, not 2016, and the Company
2 seems to be projecting earnings well above its authorized ROE, this suggests that a rate
3 increase is not justified.

4 **III. Wages and Salaries**

5 CUB is concerned that the Company's salary increases are not justified under
6 present economic circumstances. According to the Company:

7 Column (h), entitled "2016 Wage Adjustment" reflects the actual wage
8 adjustment applied to non-union and union employees. Non-union wage
9 increases were effective January 1, 2016, and union increases were
10 effective April 1, 2016. The non-union increase granted was 4% and the
11 union increase on April 1, 2016, increase was 3.1%.⁴

12 This wage adjustment reflects the change in base wages. Therefore, increases due
13 to promotion and performance bonuses are not included. As CUB said above, the
14 inflation rate over the last year is 1%. The union increase was negotiated as part of a
15 multi-year contract. However, providing a base wage increase four times the rate of
16 inflation to non-union employees is problematic.

17 CUB accepts the union wage increase of 3.1%, but recommends that the non-
18 union increase be scaled back to 1.5% (150% of inflation). CUB Exhibit 103 shows that
19 this adjustment reduces Cascade's Oregon revenue requirement by \$66,000.

20 **IV. Cost of Capital and Capital Structure**

21 In UG 287, the parties agreed to set Cascade's ROE at 9.55% and its capital
22 structure at 51% equity.⁵ In this case Cascade, is proposing to reduce its ROE to 9.4%
23 and to reduce the equity in its capital structure to 49%.⁶

⁴ UG 305/ CNGC/200/Parvinen/6.

⁵ *In re Cascade Natural Gas Corporation Request for a General Rate Revision*, OPUC Docket No. UG 287, Order No. 15-412 (Dec. 28, 2015).

1 CUB supports the ROE of 9.4%. That is the ROE the OPUC recently established
2 for Avista after a fully litigated GRC.⁷ CUB also supports reducing the equity portion of
3 the Capital structure from 51 to 49%. This reflects the actual capital structure that
4 Cascade has been carrying.⁸

5 **V. Long Run Incremental Cost Study**

6 CUB has reviewed the Company's LRIC Study and has several concerns.

7 **A. Assigning Two-Inch Mains as Customer Related.**

8 According to the Company:

9 The first component of Cascade's distribution mains analysis derives the customer
10 related costs associated with the installation of distribution mains to connect new
11 customers. Mains investments that serve this function were extracted from
12 Cascade's plant accounting records. Oregon new business project work orders
13 were summarized for a fourteen-year period (2002 – 2015). The customer cost
14 was computed by taking the average cost per foot of Cascade's minimum-sized
15 distribution main (two-inch), escalated to current dollars (2015) using the Handy
16 Whitman Index of Public Utility Construction Costs, and multiplying that unit
17 cost by the number of feet of main installed per new customer for Residential
18 (Schedule No. 101), Commercial (Schedule No. 104), and Industrial (Schedule
19 No. 105) service classes.⁹

20 While these two-inch distribution mains were installed to meet customer growth,
21 they carry capacity and annual throughput. If this two-inch main is large enough to meet
22 the design day capacity of a new residential customer, but the entire cost is being
23 allocated as a customer-related cost, it is problematic. That is because that customer is
24 then assigned additional capacity charges to meet its design day capacity.

⁶ UG 305/ CNGC/200/Parvinen/9.

⁷ *In re Avista Corporation Request for a General Rate Revision*, OPUC Docket No. UG 288, Order No. 16-109 (Mar. 15, 2016).

⁸ UG 305/ CNGC/200/Parvinen/9.

⁹ UG 305/ CNGC/300/Amen/11.

1 **B. The System is Oversized**

2 According to Cascade:

3 For a gas utility, detailed studies are not required to assess the impact of
4 additional consumption by existing customers since the delivery system is
5 built for design day requirements and energy conservation has reduced
6 those requirements for most customers. Where new customers are added
7 to the system, growth may increase design day requirements above an
8 amount that existing facilities can serve. The principal factors driving new
9 main investment are customer growth and the replacement of bare steel
10 and cast iron mains to provide safe and reliable service for customers.¹⁰

11 The existing system is oversized because energy efficiency has reduced design
12 day requirements. New investment is being driven by customer growth. However, if the
13 two-inch mains that are allocated as customer-related charges are significantly sized to
14 accommodate design day demand—and the existing system is oversized for design day
15 requirement--then the “growth related” design day increases caused by residential
16 customers are being fully recognized through the assignment of customer related mains
17 that are adequate for design day demand.

18 Because LRIC are long run theoretical studies that represent the marginal cost of
19 providing service, CUB believes that the distribution system should be “right-sized” –
20 i.e., that the utility should project the costs of serving forward looking demand with a
21 system that was sized to meet that forward looking demand, not an embedded system that
22 is oversized for current and future customers.

23 **C. Interruptible Customers**

24 According to Cascade, “For process and interruptible customers, LRIC is zero for
25 existing customers unless the customer expands its operations.”¹¹

¹⁰ CNGC/300/Amen/5.

¹¹ UG 305/ CNGC/300/Amen/9

1 CUB understands the theory behind this. If interruptible customers can be shut
2 off when capacity limitations exist, then they should not be assigned costs associated with
3 capacity. CUB's concern, however, is that because the system is oversized, interruptible
4 customers are not interrupted. All customers have the same impact on this oversized
5 system as do interruptible customers.

6 **VI. Rate Spread.**

7 CUB supports some aspects of Cascade's rate spread/rate design, such as its
8 proposal to keep residential customer charges down, but believes that Cascade begins
9 with an overly rigid approach.

10 **A. The Approach is Overly Rigid**

11 First, it should be recognized that marginal cost studies are fraught with
12 assumptions and do not provide definitive truths. Most of the distribution system is a
13 shared system. Most of the costs are common costs. The cost allocation process should
14 be concerned with creating a fair and reasonable allocation of these common costs.
15 Cascade recognizes that much of the costs at issue are common costs.¹² However, by
16 acting rigidly based on the results of the study, Cascade fails the basic fairness test.

17 Cascade's Exhibit 301 summarizes Cascade's LRIC results. Line 38 shows the
18 revenue to cost ratio. Cascade explains what this means:

19 A revenue-to-cost ratio of less than 1.00 means that the current rates and revenues
20 of the particular rate schedule are below its indicated LRIC (*e.g.*, Rate Schedules
21 101, 105, 111, and 163), while a revenue-to-cost ratio of greater than 1.00 means
22 that the rates and revenues of the rate schedule are above its indicated LRIC.

¹² UG 305/CNGC/300/Amen/6.

1 Cascade then assigns the new revenue requirement associated with this case to the
2 customer classes that are under 1.00 and not to the customer classes that are above 1.00.
3 The problem with this approach is that if you look at the second largest class of
4 customers, Schedule 105, Commercial, their revenue to cost is 1.01. This means these
5 customers are paying very close to the actual cost of service. There are undoubtedly
6 several assumptions in the study that could have moved this class of customers under the
7 1.01. The same thing is true for interruptible customers, whose revenue to cost ratio is
8 1.02.

9 Cascade's methodology would place a rate hike on a customer class that has a
10 revenue-to-cost ratio of .99, but not to one that is 1.01. However, recognizing the
11 impreciseness of an LRIC study, CUB would argue that any customer class that has a
12 revenue-to-cost ratio in the range of around 95% to 105% is paying its fair share of costs.

13 Cascade Exhibit 301 also shows that after the increase, residential customers will
14 be at a 1.00 revenue-to-cost ratio, while Schedule 105, Commercial, is still at 1.01 and
15 Interruptible is at 1.02. This creates the very real possibility that with small changes in
16 some of the costs, the next LRIC study would begin with all three of these customer
17 classes slightly above a 1.00 revenue-to-cost ratio and Cascade's methodology would
18 prevent their rates from going up any more. However, these three classes of customer
19 represent 84% of the non-gas revenues.¹³

20 CUB does not believe that customer classes that are ever-so-slightly above 1.00
21 revenue-to-cost ratios should be exempt from rate increase. In this current docket,
22 Cascade's methodology would remove the second largest rate class from any contribution

¹³ See line 32 of Cascade Exhibit 301.

1 to the higher costs associated with this rate case. It also defies the fairness test, because a
 2 revenue-to-cost ratio of 1.01 is within the margin of methodological error.

3 **B. CUB’s Proposed Rate Spread.**

4 CUB Exhibit 104 shows CUB’s proposed rate spread. CUB made two
 5 adjustments to Cascade’s Rate Spread.

6 First, CUB applied the average non-gas increase, 6.43%, to all rate schedules that
 7 are current near balance between revenue and cost (any class between 98% and 102%).
 8 This increased revenues by \$517,154 by giving Commercial and Interruptible customers
 9 the average increase.

10 Second, because these customer classes were now picking up 27.1% of the overall
 11 *increase*, CUB then reduced the increase to other customer classes by 27.1%.

Customer Class	Cascade’s Proposed Increase	CUB’s Proposed Increase
101 Residential	\$1,507,728	\$1,099,077
104 Commercial	0	497,748
105 Industrial	162,555	118,503
111 Large Volume	62,397	45,487
163 General Distribution	173,604	126,557
170 Interruptible	0	19,306
9xx Special Contracts	0	0

1 **C. Rate Design**

2 *i. Residential Customer Charges*

3 CUB supports Cascade’s proposal to maintain the status quo in the residential
4 customer charge and place the increase in revenue onto the commodity charge. While
5 Commission policy allows a customer charge to be set at a level that collects direct
6 customer costs (meter, meter reading, billing), it does not require such pricing. Because
7 the customer charge is non-avoidable, there is no real purpose for trying to get this “price
8 signal” right. Customers cannot react to the price signal. It is more important to focus on
9 the variable cost—the cost that customer can control. This is the cost that customer can
10 avoid through energy efficiency investments. Because the current commodity prices are
11 low, CUB applauds Cascade for keeping the bulk of revenue requirement collection in
12 the variable rate so customers are getting encouragement to consider efficiency. CUB
13 notes that in the long run, climate change will likely push carbon regulatory costs onto
14 the gas system, pushing up the variable cost of gas. Keeping the variable cost as high as
15 possible today encourages customers to purchase efficient equipment and better prepares
16 them for a carbon constrained regulatory environment in the future.

17 *ii. Other Classes Customer Charge*

18 CUB does not take a position on whether the revenue requirement increases
19 allocated to other customer classes should come from fixed or variable charges.

20 **VII. Conclusion**

21 CUB has reviewed Cascade’s rate filing and recommends the following:

- 22 • Based on the Company’s 2017 financial projections, CUB does not believe
23 that a rate hike is justified.

- 1 • CUB proposes an adjustment of \$66,000 to wages and salaries.

- 2 • CUB supports the Company's proposed return on equity and capital
3 structure

- 4 • CUB is concerned with the LRIC's assignment of two-inch distribution
5 mains as fully customer-related, with using an oversized system in the
6 marginal cost study, and with exempting interruptible customers from
7 distribution costs, when in an overbuilt system, they are little different than
8 other customers.

- 9 • CUB proposes and adjustment to rate spread that assigns average cost
10 responsibility to customers that are with 2% of revenue cost balance (98% to
11 102%) which reduces the rate increase to other customer classes.

- 12 • CUB supports the Company's proposal to maintain the current residential
13 customer charge.

WITNESS QUALIFICATION STATEMENT

NAME: Bob Jenks

EMPLOYER: Citizens' Utility Board of Oregon

TITLE: Executive Director

ADDRESS: 610 SW Broadway, Suite 400
Portland, OR 97205

EDUCATION: Bachelor of Science, Economics
Willamette University, Salem, OR

EXPERIENCE: Provided testimony or comments in a variety of OPUC dockets, including UE 88, UE 92, UM 903, UM 918, UE 102, UP 168, UT 125, UT 141, UE 115, UE 116, UE 137, UE 139, UE 161, UE 165, UE 167, UE 170, UE 172, UE 173, UE 207, UE 208, UE 210, UE 233, UE 246, UE 283, UE 296, UE 308, UG 152, UM 995, UM 1050, UM 1071, UM 1147, UM 1121, UM 1206, UM 1209, UM 1355, UM 1635, UM 1633, and UM 1654. Participated in the development of a variety of Least Cost Plans and PUC Settlement Conferences. Provided testimony to Oregon Legislative Committees on consumer issues relating to energy and telecommunications. Lobbied the Oregon Congressional delegation on behalf of CUB and the National Association of State Utility Consumer Advocates.

Between 1982 and 1991, worked for the Oregon State Public Interest Research Group, the Massachusetts Public Interest Research Group, and the Fund for Public Interest Research on a variety of public policy issues.

MEMBERSHIP: National Association of State Utility Consumer Advocates
Board of Directors, OSPIRG Citizen Lobby
Telecommunications Policy Committee, Consumer Federation of America
Electricity Policy Committee, Consumer Federation of America
Board of Directors (Public Interest Representative), NEEA

CASCADE NATURAL GAS CORPORATION
Oregon Public Utility Commission
Standard Data Requests

Request No. 4

Date prepared: 2/23/2016

Preparer: Becky Mellinger

Contact: Pam Archer

Telephone: (509)734-4591

4. Please provide, in electronic spreadsheet format, the Company's complete financial statements (e.g., balance sheet, income statement, cash flow statement, statement of shareholders' equity, and statement of comprehensive income) on an annual (or year-end for the balance sheet) *pro forma* basis for each of the ten calendar years subsequent to the current year, specifically including the information requested below. If information associated with any of the following specific requests is not available, please explain why this is the case.
 - a. Return on equity for all property;
 - b. Return on equity for state-regulated property (all applicable state jurisdictions collectively); and
 - c. Return on equity for OPUC-regulated property.

Response:

See attached for Spreadsheet financial statements.

OPUC-4 A & B.xlsx

OPUC-4 C.xlsx

Information is available for four years subsequent to the current calendar year as CNG only forecasts out four years from current year.

Return on Equity for All Property

CNG Consolidated

	Year	Year	Year	Year	Year
Return on Average Equity	2016	2017	2018	2019	2020
Annual Income	10,655	16,444	20,708	20,817	22,417
Average Equity	192,472	198,038	210,471	222,655	236,646

CASCADE NATURAL GAS CORPORATION
Oregon Public Utility Commission
Standard Data Requests

Return on Average Equity	5.54%	8.30%	9.84%	9.35%	9.47%
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Return on Equity for State-Regulated Property

CNG Consolidated

	Year	Year	Year	Year	Year
Return on Average Equity	2016	2017	2018	2019	2020
Annual Income	10,655	16,444	20,708	20,817	22,417
Average Equity	192,472	198,038	210,471	222,655	236,646
Return on Average Equity	5.54%	8.30%	9.84%	9.35%	9.47%

Return on Equity for OPUC-Regulated Property

Oregon Only

	Year	Year	Year	Year	Year
Return on Average Equity	2016	2017	2018	2019	2020
Annual Income	3,423	5,366	6,011	6,738	6,420
Average Equity	42,828	45,283	49,528	53,477	57,946
Return on Average Equity	7.99%	11.85%	12.14%	12.60%	11.08%

<p>Cascade UG 305 2016 Wage Adjustment Twelve Months Ended December 31, 2015</p>

Salaried employees (Annual Wages)	\$10,651,417	\$11,077,473	4.00%	Increases Effective January 1
Bargaining Unit employees (4/1/14-12/31/14 wages)	\$11,554,979	\$11,913,183	3.10%	Increases effective April 1

Total Wages	\$22,206,396	\$22,990,657	\$784,261
3 Factor formula			0.2472
Oregon 2016 Wage Increase			\$193,869

CUB Adjustment	Salaried Employees	\$10,651,417	10811188.03	1.50%
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total wages	22,206,396	\$22,724,371	\$517,975
			0.2472
Oregon Wage Adjustment			\$128,043.51

Change to Cascade's filing \$65,825.81

Customer Class	Current Revenues (non-gas)	Proposed	Percent increase	CUB's Proposed Revenue	Revenue Increase
101 -- Residential	\$ 16,926,173.00	\$ 18,433,901.00	8.91%	\$ 18,025,249.85	\$ 1,099,076.85
104 -- Commercial	\$ 7,741,020.00	\$ 7,741,020.00	0.00%	\$ 8,238,767.59	\$ 497,747.59
105 -- Industrial	\$ 505,501.00	\$ 668,057.00	32.16%	\$ 624,003.60	\$ 118,502.60
111 -- Large Volume	\$ 242,548.00	\$ 304,946.00	25.73%	\$ 288,035.41	\$ 45,487.41
163 -- General Distribution	\$ 2,159,441.00	\$ 2,333,045.00	8.04%	\$ 2,285,998.32	\$ 126,557.32
170 -- Interruptible	\$ 300,244.00	\$ 300,244.00	0.00%	\$ 319,549.69	\$ 19,305.69
9xx Special Contracts	\$ 1,765,115.00	\$ 1,765,114.00	0.00%	\$ 1,765,115.00	\$ -
TOTAL	\$ 29,640,042.00	\$ 31,546,327.00	6.43%	\$ 31,546,719.45	\$ 1,906,677.45