

**PUBLIC UTILITY COMMISSION OF OREGON  
STAFF REPORT  
PUBLIC MEETING DATE: July 2, 2013**

REGULAR \_\_\_\_\_ CONSENT X EFFECTIVE DATE \_\_\_\_\_ N/A

DATE: June 10, 2013

TO: Public Utility Commission

FROM: Judy Johnson *JJ*

THROUGH: Jason Eisdorfer, Maury Galbraith, and Marc Hellman *MG* *MG* *MH*

SUBJECT: NORTHWEST NATURAL: (Docket No. UM 903) 2013 Spring Earnings Review.

**STAFF RECOMMENDATION:**

I recommend the Commission accept Staff's finding that Northwest Natural's earnings for the 12 months ended December 31, 2012, are below the earnings threshold established in UM 903 and there should be no earnings shared in this filing.

**DISCUSSION:**

In Order Nos. 98-543<sup>1</sup> and 99-284 (Dockets UM 903 and AR 357), the Commission adopted Purchased Gas Adjustment (PGA) Procedures and Standards for Oregon's three regulated natural gas distribution companies – Northwest Natural (NW Natural or Company), Cascade Natural Gas, and Avista Utilities. One of the primary issues dealt with in these orders is the role and structure of earnings reviews. The earnings reviews were originally scheduled to sunset in 2002 but were extended twice, first until 2006 by Order No. 03-198 (AR 449) and then through 2008 by Order No. 07-019 (AR 512). Commission Order No. 08-504 (UM 1286) that adopted revisions to the current PGA mechanism also eliminated the sunset provision.<sup>2</sup>

<sup>1</sup> Amended by Order Nos. 99-272 and 04-203.

<sup>2</sup> The sunset provision was eliminated from OAR 860-022-0070 by Order No. 09-096 (AR 532).

The Commission's findings, as they apply to earnings reviews, are summarized below:

#### Annual Election

Not later than August 1st of each year, each Local Distribution Company (LDC) shall make an annual election for the applicable gas year beginning November 1st whether to choose 90/10<sup>3</sup> Weighted Average Cost of Gas (WACOG) sharing or 80/20 (WACOG) sharing with a corresponding earnings review threshold. In its letter, NW Natural elected a 90/10 sharing beginning November 1, 2011.

#### Spring Earnings Review

An earnings review will be performed each spring (pursuant to OAR 860-022-0070) based on the most recent fiscal year's results of operations. The earnings review will apply to the sharing election made by the LDC the previous August (e.g., the 2011 election will apply to the 2012 Fiscal Year results of operations which are the subject of the 2013 Spring Earnings Review); if earnings are found to be above a specified return on equity (ROE) level, a portion of those revenues will be booked to a deferred account.

#### The ROE Earnings Threshold

An LDC that elects 90/10 sharing will be subject to an earnings threshold 100 basis points above its ROE, adjusted to reflect changes in conditions in capital markets. An LDC that elects 80/20 sharing is subject to an earnings threshold 150 basis points above its ROE, adjusted in the same manner.

#### Structure of Earnings Reviews

By May 1st of each year, the LDC will file results of operations for the twelve months ended the prior December 31<sup>st</sup>. Staff will complete its review and distribute summary conclusions by June 10<sup>th</sup> to all parties. At the first regular public meeting in July, Staff will present the results of the earnings review. If there are unresolved issues, a settlement conference will be held. If there are still outstanding issues, parties will file position statements by August 1<sup>st</sup> and the Commission would issue its decision on unresolved issues by August 15<sup>th</sup>. These rate changes will include amortization of credit amounts in the deferred account, if any, resulting from the spring earnings review.

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<sup>3</sup> Sharing of the variance between the LDC's weighted average cost of gas (WACOG) included in its rates and its actual WACOG. For example, 90/10 designates 90 percent of the variance will be deferred for subsequent charge or credit to customers, and 10 percent is absorbed or retained by the LDC. See Order 08-504 at 17. The earnings threshold is adjusted each year by 20 percent of any change in the risk free rate for the twelve-month calendar year preceding the annual earnings review (See Order No. 04-203 at 3-4 and OAR 860-022-0070(5)(c)).

Earnings Adjustments

Recorded results of operations will be adjusted for Type 1 adjustments as set forth in Order No. 99-272, Appendix B. NW Natural made a one-time election to include a weather normalization adjustment in its spring 1999 earnings review filing and each subsequent annual filing.

Earnings Performance

If adjusted earnings are below the earnings threshold, there will be no rate adjustment. If adjusted earnings are above the earnings threshold, the amount of revenue in the test year representing 33 percent of the earnings (including WACOG earnings) exceeding the threshold level will be shared with customers.

Effective Date of Rate Adjustment and Applicable Interest

Upon completion of the earnings review, any amount of earnings over the sharing dead band determined to be returned to customers will be booked to a deferred account. Interest shall apply beginning the previous January 1<sup>st</sup>. The rate adjustment and amortization will be effective with the date of the subsequent base gas cost change.

Staff's Review of NW Natural's Earnings

The calculated earnings threshold for the Company for this 2013 Spring Earnings review (review of the 2012 results of operations) is 10.92 percent. The 10.92 percent is calculated by using NW Natural's weighted average Return on Equity (ROE). Which in this case are 10 months at 10.20 percent and 2 months at 9.5 percent, which equals 10.08 percent. This ROE is then added to 100 basis points and then subtracted from 20 percent of the change in United States Treasury Risk Free Rate. These calculations produce an Earnings Threshold of 10.92 percent for NW Natural. Pursuant to the rules, NW Natural submitted its 2012 Results of Operations report for the 12 months ending December 31, 2012. The Company states that its report is meant to satisfy the reporting requirements associated with the UM 903 investigation (Order No. 99-272) and AR 357 (Order No. 99-284) as well as the "standard Oregon annual reporting requirements". NW Natural calculates its ROE as 9.87 percent after the application of its Type I adjustments, including weather normalization.

Staff reviewed the Company's revised earnings report and concludes that NW Natural's reported ROE has been calculated correctly. Because the Company's adjusted ROE is below the authorized threshold of 10.92 percent, earnings sharing are not required.

As required by OAR 860-022-0070(6), Staff submitted these findings to the parties in Docket No. UM 903 on June 10, 2013, and received no comments in response.

**PROPOSED COMMISSION MOTION:**

Accept Staff's finding that NW Natural's 2012 earnings are below the earnings threshold designated in UM 903, and that there is no earnings sharing for the 2012 Fiscal Year.