BEFORE THE PUBLIC UTILITY COMMISSION

OF OREGON

UM 1654

In the Matter of NORTHWEST NATURAL GAS COMPANY, dba NW Natural Investigation of Interstate Storage and Optimization Sharing	)	CITIZENS' UTILITY BOARD OF OREGON'S FIRST POST-HEARING BRIEF

I. INTRODUCTION

The Citizens' Utility Board of Oregon ("CUB"), pursuant to ALJ Pines' Pre-hearing Conference Memorandum of June 26, 2014, herewith submits its First Post-hearing Brief in this matter. CUB's Pre-hearing Brief, filed January 27, 2014, set forth in detail the total of its then existing arguments. However, since that time, new evidence has been elicited in the form of the February 3, 2014 and July 10, 2014 hearings, post hearing data responses from NW Natural ("the Company" or "NWN") in April of 2014[1] and also on the March 5, 2014, March 28, 2014, June 10, 2014 and July 1, 2014 Bench Request and Supplemental Bench Request Responses.[2] CUB also relies on its May 2, 2014 Phase II Response Testimony in docket UM 1635 commencing at page 11 wherein CUB conducts a comparison of the negative assets at issue in that docket (old manufactured gas plant caused pollution from plants closed long ago) with the positive assets at

[1] UM 1654 CUB/ 300 – 324/Jenks-McGovern (April 2014 Data Responses from NWN which were admitted into evidence at the July 10, 2014, Hearing – July 10, 2014 Hearing Transcript/6 lines 7-22).
[2] NW Natural's Bench Responses and Supplemental Bench Responses were also admitted into evidence at the July 10, 2014, Hearing – Hearing Transcript/6 lines 23-25 and 7 lines 1-25 and 8 lines 1-9.

issue in this docket (storage assets developed for use by core customers being used now for shareholder storage and optimization profits) and then discusses the disparate treatment that NWN is requesting for each type of asset. Administrative/Official Notice has already been taken of the UM 1635 testimony.[3] As a result of all of the above, CUB has developed several additional arguments which will be set forth in this First Post-hearing Brief.

To avoid redundancy, CUB will focus only on new arguments and innovations in this First Post-hearing Brief. To review all of CUB's arguments, the reader will need to first read CUB's January 2014 Pre-hearing Brief

At the end of this First Post-hearing Brief CUB will, based upon its review of the evidence now present in the record, re-affirm the recommendations made in its Pre-hearing Brief with one modification. CUB's recommendations today are as follows:

- that the Commission order implementation of a cost based study with appropriate in-depth analysis to be included in the next marginal cost study;
- that pending those results, CUB will not recommend any change to the Inter/Intrastate sharing percentages (20 customer/80 shareholder) (Note: Because of the inability to get good, factual information, CUB believes the Commission might want to expand this cost based study from CUB's marginal cost approach to a cost study along the lines proposed by Staff in UG 221);[4]
- that the Commission find that NWN has been misallocating net revenues from Mist Optimization to Interstate/intrastate storage and order that 47% of Mist Optimization Revenues be removed from Interstate/Intrastate storage and the sharing percentage for all

[3] Official Notice was taken at the July 10, 2014 Hearing, Hearing Transcript/6 lines 7-22.
[4] UG 221 Staff/1000/Zimmerman/12 lines 8-19; UG 221 Staff/1900/Zimmerman/13 lines 15-20.

optimization activities including pipeline optimization should be set at 90% customer/10% utility, though CUB would be supportive of phasing this in with a step which moves the sharing from 67% customer/33% shareholder to 80% customer/20% shareholder (the inverse of the sharing percentage for interstate storage);

- that the Commission find that all AMA Optimization revenues must be included in the Company's ROO as utility income (Note: CUB is not proposing that interstate storage be included in the ROO as utility income).

CUB persists with these recommendations because of NWN's inability to demonstrate what it is doing after three rounds of testimony, numerous data requests, a Prehearing Brief, two hearings and answers and supplemental answers to two sets of Bench Requests, all when the Company is the party who must carry the burden of proof. It is, therefore, CUB's position that the current interstate/intrastate and optimization sharing percentages are not supported by the evidence in this record. As a result, CUB respectfully recommends that the Commission modify the sharing percentages as requested by CUB.

II. THE UNSETTLED ISSUES

All of the original unsettled issues remain unsettled and are repeated here in abbreviated form only:

1. Whether NWN has an obligation to maximize the value of regulated assets, including the use of those assets in a manner which generates revenue from non-retail markets and uses that revenue to reduce its revenue requirement from the customer who financed the assets. *CUB's Prehearing Brief argued that NWN does have such an obligation but that "when ratepayer-financed assets are used for activities which benefit shareholders, great*

care must be exercised to ensure that ratepayers are not improperly subsidizing those activities and also to ensure that ratepayers are being fairly compensated for the use of their assets."[5]

2. Whether parties should be concerned about the makeup of the gas that NWN is using in its Optimization program. *CUB argues that they should because NWN, by law, can only use retail customer gas. "Whether NWN is leveraging assets or trading asset is a distinction without a difference. NWN has stated that, 'NW natural buys no gas for speculative purposes – it all must tie to its utility business needs . . . .' Thus, by declaration NWN has stated that it does not purchase gas for options trading or market optimization. Also, FERC jurisdiction does not give the Company rights to third party gas that the company holds on behalf of its intrastate/interstate customers. This means that all gas that NWN 'owns', or has rights to, is actually owned by its regulated utility ratepayers."*[6]

3. Whether NWN should have to include optimization costs and revenues in its Results of Operations (ROO). *CUB, in its Pre-hearing Brief, argued that "The revenues from NWN's AMA Optimization are not exempt or special. They are . . . normal in the course of modern utility operations, and belong in the NWN ROO."*[7]

4. Whether a cost study is needed in order to understand the value of the ratepayer assets being used for interstate storage. *CUB argues in its Pre-hearing Brief that a cost study is*

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[5] UM 1654 CUB's Prehearing Brief/2 citing to UM 1654 CUB/100/Jenks-McGovern/1 lines 8-11 and 2 lines 1-2; UM 1654 CUB/104/Jenks-McGovern/1; UM 1654 CUB/105/Jenks-McGovern/1; UM 1654 CUB/107/Jenks-McGovern/1; UM 1654 CUB/108/Jenks-McGovern/1; and UM 1654 CUB/109/Jenks-McGovern/1.

[6] UM 1654 CUB Pre-hearing Brief at 13 citing to UM 1654 – CUB Exhibit 103 at slide 12; UM 1654 CUB/100/Jenks-McGovern/18 lines 27-33 and at 19 lines 1-13; UM 1654 CUB/200/Jenks-McGovern/11 lines 14 to 13 line 8.

[7] CUB Pre-hearing Brief at 15 citing to UM 1654 CUB/200/Jenks-McGovern/18 lines 2-23 and at 19 line 1.

needed because without one there is "no way to ascertain if customers are being fully compensated for the use of their resources . . . ."[8]

5. Whether Customers have been overpaid for Inter/Intrastate storage, as alleged by NWN. *As argued by CUB in its Pre-hearing Brief, customers have not been overpaid. "It is only after shareholder costs are fully recovered that the company shares the program's net revenues according to the 20/80 split. So we know that shareholders are fully compensated and then received net profits on top of that . . . ."* What we don't know is whether ratepayers are fully compensated.[9]

6. Whether CUB erred in not separately identifying the cushion gas that is shareholder gas is besides the point--if revenues are going to be allocated to Mist gas, cushion gas should be included. CUB's error did not in any way affect the rest of CUB's Analysis. *While CUB erred in not identifying the cushion gas that is shareholder gas, the point remains that if optimization revenues are going to be allocated to Mist gas, cushion gas should be included. Cushion gas is necessary for other gas to be optimized. CUB now understands that of the cushion gas at Mist, ratepayers own* [redacted] *and shareholders own* [redacted].[10]

In this First Post-hearing Brief CUB will take a deeper dive into the optimization of Mist Storage. The first, and the most important, question that will be addressed in detail below is:

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[8] CUB Pre-hearing Brief at 19 citing to UG 221 Staff/1000/Zimmerman/18; UM 1654 CUB/200/Jenks-McGovern/5 lines 11-13; UG 221 Staff/1000/Zimmerman/20 lines 12-16; UM 1654 CUB/200/Jenks-McGovern/5 lines 20-21 and at 6 lines 1-4.

[9] CUB's Pre-hearing Brief at 20 citing to UM 1654 CUB/100/Jenks-McGovern/9 lines 13-15; UM 1654 CUB/100/Jenks-McGovern/11 Table "Net Income for Shareholders from Gas Storage";UM 1654 CUB/100 Jenks-McGovern/10 lines 9-14: "Suppose, the value of the items that ratepayers contribute is worth $3 million per year and the net revenues are worth $10 million. Then ratepayers are being asked to subsidize Company storage and Optimization activities to the tune of $1 million even though shareholders are earning $8 million from it (20% of $10 million equals $2 million and represents the rate payer share that would partially offset $3 million of ratepayer costs)."

[10] UM 1654 CUB/313/Jenks-McGovern (NWN Response to CUB DR 81).

Whether, as CUB asserts, there should be only one sharing percentage 90/10 because: there is only one set of gas being optimized; that one set of gas is made up 100% of customer working gas, and during optimization the 100% customer working gas is only *supported* by customer and *other* (non-core/interstate) cushion gas, customer and interstate storage working gas and the deliverability provided by the combined customer and interstate storage gas. The reason this question is so important, and that it will be discussed in great detail below, is that NWN has chosen to assess the income associated with Mist optimization based on *deliverability* and to then use its interstate storage sharing percentage for sharing optimization revenues that it arbitrarily assigned to interstate storage. Because NWN receives 80% of the revenues from interstate storage, and customers receive 67% of the revenues from the portion of optimization allocated to core customers, NW Natural's split of Mist Optimization levels, leaves the Company retaining more than half of the Mist optimization revenues, even though all of the optimized gas is core customer working gas. The sharing percentages devised by NWN look like this:

Shareholders

(47% X 80%) + (53% X 33%) = 55%

Customers

(47% X 20%) + (53% X 67%) = 45%

This question of whether there should only be one sharing percentage of 90/10 with regard to optimization is also being addressed in great detail because NW Natural has failed to provide clear and precise evidence in this docket, and has instead, in CUB's opinion, engaged in an effort to sow confusion. That the Company still cannot explain its own argument that deliverability is the key to Mist optimization only serves to emphasize that deliverability is not, in fact, the key. Ownership of the optimized working gas is the key. CUB thinks NW Natural only assigns Mist optimization revenues based on deliverability because use of that methodology allows the Company to retain a greater share of the revenue for shareholders. This is not how a Commission whose mission is to protect both ratepayers and utilities and to ensure that rates are fair, just and reasonable should allow optimization activities to work.

As CUB will explain below, it strongly disagrees with NW Natural's approach. Assigning some of the Mist optimization to interstate storage makes no sense because the gas in interstate storage cannot itself be used for optimization. Instead, it should be recognized that all the gas that is being optimized belongs 100% to core customers. This, then, is the basis for CUB's recommendation that the sharing percentages be changed to one 90/10 sharing percentage. CUB understands that this is a big leap for the Commission. To the degree that the Commission feels that the Company should be compensated because while the gas being optimized belongs to customers it is made accessible due partly to the use of cushion gas, working gas and deliverability associated with interstate storage gas, then the Commission could adjust the sharing percentage from CUB's proposed 90/10 to 80/20. But the bottom line is that there is only one optimization program and that optimization program optimizes only core customer gas. The real questions that this docket should focus on are whether shareholders should receive oversized compensation simply because a program that optimizes core customer gas makes use of available interstate storage based deliverability in facilitating the optimization of 100% core customer owned gas—and not whether some of the optimization should be considered optimization of interstate storage gas deliverability.

III. CUB'S ADDITIONAL ARGUMENTS IN REGARD TO THE UNSETTLED ISSUES (see CUB's Pre-hearing Brief for the rest of its arguments)

For ease of reference, CUB's First Post-hearing Brief will number the additional CUB arguments sequentially from where the January Pre-hearing Brief arguments left off.

7. Whether, as CUB asserts, there should be only one sharing percentage 90/10.

a. There is only one set of gas being optimized

It has taken some time for CUB to sift through the muddled hearing transcripts, data and bench responses supplied by the Company. But we think we have as good a handle on it now as is possible based on the available information. The bottom line is that there is only one set of gas at Mist that is being optimized and that gas is 100% core customer gas. We know this because in the response to UM 1654 CUB DR 4(b)[11] NW Natural stated that it "does not use the gas belonging to Interstate/Intrastate Storage customers for optimization purposes." While the record is unclear on the role of deliverability in relationship to Mist optimization, the record has established that only core cost gas is used for optimization.

b. The one set of gas used for optimization is made up 100% of core customer gas

So while the total gas stored at Mist when its storage is full is 62% core customer gas - 38% *other* (read interstate/intrastate storage),[12] this *other* gas cannot be used for optimization. NWN has stated that it does not purchase gas for options trading or market optimization. Also, FERC jurisdiction does not give the Company rights to third party gas that the Company holds on behalf of its intrastate/interstate customers. This means that all gas that NWN 'owns,' or has

[11] UM 1654 CUB/109/Jenks-McGovern (NWN Data Response to CUB DR 4).
[12] UM 1654 July 10, 2014 Hearing Transcript/10 lines 20-24.

rights to, is actually owned by its regulated utility ratepayers.[13] This also means that all the gas used for optimization is 100% core customer gas.

c. During optimization, the 100% core customer working gas is only supported by customer and interstate cushion gas, customer and interstate working gas and the deliverability provided by the combined customer and interstate storage gas.

To explain this statement a reader first has to understand how gas storage works. CUB understands that underground gas storage is complicated. CUB also understands that the amount and speed that gas can be removed from storage is affected by the total volume of storage. Cushion gas is needed as a base in the storage reservoir before any additional gas can be withdrawn from storage. And the speed at which one can withdraw gas from storage is affected by what other users of storage are doing with their gas. So how does NWN get 100% core customer owned working gas out of storage for use in optimization (recognizing that when used as collateral it never has to get out of the ground)?

NWN uses *other* (non-core) working gas[14] and customer and *other* (non-core) cushion gas, to provide the deliverability necessary for it to optimize the core customer owned gas.[15] We know this is correct because in CUB Exhibit 109 - UM 1654 CUB DR 4(b) NWN confirmed that it "does not use the gas belonging to Interstate/Intrastate Storage customers for optimization purposes [but that it] does use all the deliverability developed at Mist for optimization purposes, i.e. compression and related facilities." This is why NWN thinks that it is okay to allocate

[13] CUB unsettled issue (2) citing to UM 1654 CUB Pre-hearing Brief at 13 citing to UM 1654 – CUB Exhibit 103 at slide 12; UM 1654 CUB/100/Jenks-McGovern/18 lines 27-33 and at 19 lines 1-13; UM 1654 CUB/200/Jenks-McGovern/11 lines 14 to 13 line 8.
[14] UM 1654 CUB/ 312/Jenks-McGovern (NWN Response to CUB DR 80) Confidential.
[15] UM 1654 CUB/311/Jenks-McGovern (NWN Response to CUB DR 79) Confidential.

between Core Utility and Interstate/intrastate Storage based on deliverability. CUB strongly disagrees.

d. NWN picked the deliverability percentages number to discuss because it is the number most favorable to NWN – the rest of the numbers reviewed favor core customers.

So, as noted above, all the gas used for optimization is 100% core customer gas and yet the allocation of revenue is based upon "deliverability."[16] Why did NWN pick, and why does NWN continue to advocate for, *deliverability*[17] as the basis for application of sharing percentages?

NWN picked deliverability because it is the only percentage that comes close to being even with customer contributions and therefore percentages. NWN backs its claim to the current allocation level by saying it can only use 100% of the core customer gas if it *supports* it with something else to make it deliverable,[18] but the deliverability is in turn supported by the volume of working gas and cushion gas. Here are the sharing percentages upon which NWN's and CUB's arguments are based:

Mist Gas used for optimization: 100% core customer/0% *other* (non core)[19]

Cushion gas at Mist: [redacted] core customer [redacted] *other* [20]

Working gas at Mist: 62 % core customer/38% *other* [21]

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[16] UM 1654 NWN/100/White/10 lines 1-10 with specific emphasis on lines 4-7.
[17] Um 1654 February 3, 2014 Hearing Transcript/111 lines 3-8.
[18] UM 1654 February 3, 2014 Hearing Transcript/134 lines 4-9.
[19] UM 1654 CUB/109/Jenks-McGovern (NWN Response to CUB DR 4(b)).
[20] UM 1654 CUB/313/Jenks-McGovern (NWN Response to CUB DR 81) Confidential.
[21] UM 1654 July 10, 2014 Hearing Transcript/10 lines 20-24.

Deliverability: 53% core customer/47% *other*[22]

CUB believes that the focus on deliverability obscures the fact that it is core customer gas that is being utilized for storage optimization activities. The assignment of some of the optimization revenues to interstate storage obscures the fact that optimization is an activity that occurs solely with gas that is purchased for use by core customers of the utility. CUB believes that optimization revenues should not be split between the interstate and core functions, but should all be considered only an activity of NWN to optimize the gas asset that it purchased on behalf of core customers. The question is what sharing percentage is necessary to compensate shareholders for supporting this optimization activity. CUB has proposed 90/10 sharing, but recognizes that if the Commission gives more weight to the role of cushion gas, interstate working gas or deliverability in supporting the optimization of core customer working gas that the Commission might want to consider an 80/20 split. CUB's analysis of this issue follows.

NWN attempts to muddy the waters. NWN now claims that that the third party optimization of gas at Mist is based on the total deliverability of all gas stored there. According to NWN, if you factor in deliverability then 53% of the gas belongs to ratepayers so 53% of the revenues associated with optimization are in fact shared with customers on a 67-33 basis; 47% of the gas belongs to storage customers and is shared on a 20-80 basis.[23] Counsel for NWN states in her brief that "the Company optimizes *capacity*, not gas inventory."[24] And that "[t]he ability of NW Natural's partner to trade gas on NW Natural's behalf is not based on the amount of gas inventory at Mist, it is based on the storage capacity at Mist."[25] But the bottom line is that

[22] UM 1654 NWN/500/White/6 lines 17-18.
[23] UM 1654 NWN/500/White/6 lines 17-18.
[24] UM 1654 NW Natural's Pre-hearing Brief/11 line 15.
[25] UM 1654 Northwest Natural Gas Company's Pre-Hearing Brief/11 lines 15-17.

ratepayers own 62% of the working gas stored in Mist, that only ratepayer owned working gas can be used for optimization and that optimization would not take place without that working gas, and that any sharing should recognize that it is core customers' gas that is being optimized. To do otherwise is a disservice to ratepayers and allows use of their assets without appropriate compensation. Indeed, as pointed out in CUB's Pre-hearing Brief, the contract with NWN's partner makes clear that the optimization partner [redacted][26] And the fact that the same volume of working core customer gas can be used several times over the year to backstop different optimization opportunities does not mean that it is capacity that is being optimized and not gas.[27]

At the February 3, 2014 Hearing, Mr. Friedman tried to explain why the Company bases its allocation on deliverability, stating that the Company doesn't:

> [T]ry to track optimization transactions and are we using core capacity or are we using interstate capacity. We just optimize the whole – the whole thing. So basically the portion that's in rates, which currently is 53 percent, that we share at 67 percent back to customers. And the portion that is not in rates, the 47%, is shared 20 percent.[28]

Mr. Friedman then stated that the 47/53 would change through time due to additional recall.[29]

Further discussion of the 53-47 percentage took place in regard to compressors and deliverability when NWN tried to clarify Mr. Friedman's testimony given at the February 3, 2014 Hearing.[30] After the hearing, CUB asked two data requests in this regard. In Data Request

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[26] UM 1654 CUB Prehearing Brief/12 citing to CUB Confidential Exhibit 102 "Natural Gas Asset Management Agreement Between Northwest Natural Gas Company and Tenaska Marketing Ventures, Article 3, Asset Management Agreement Description at Sections 3.1 and 3.3."
[27] UM 1654 CUB Pre-hearing Brief/13.
[28] UM 1654 Hearing Transcript/35 lines 22-25 and at 36 lines 1-4.
[29] UM 1654 Hearing Transcript/36 lines 5-11.
[30] UM 1654 February 3, 2014 Hearing Transcript/122 lines 1-8.

103[31] NWN was asked to provide workpapers that demonstrated that a specifically cited compressor station led to its claimed 53-47 ration. But, rather than provide the requested workpapers the Company stated the following:

> a. Referring to Mr. Friedman's Direct Testimony (NWN/200, Friedman/5, lines 16-17), he states that the "portion of Mist now reserved for core customers totals 275,000 Dth/day out of the current total Mist peak day deliverability of 520,000 Dth/day." Dividing 275,000 by 520,000 equals 52.88%, or 53% rounded. The remainder for Interstate is then 47%. Regarding the compressor station, Mr. Friedman elaborates starting at Transcript page 133, line 16, that it is more than just the compressors that create deliverability and the resulting 53/47 ratio. And whether the ratio is expressed as 53/47 or 47/53, the 53 refers to the percentage of Mist deliverability currently reserved for Core, while the 47 refers to the percentage of Mist deliverability currently available for Interstate Storage services.
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> b. The ratio reflects the relative deliverability rates made possible by Core versus Interstate Storage investments.[32]

In CUB DR 104[33] CUB asked NWN if it had identified a particular compressor as the source of the sharing percentage. NWN's answer was once again unresponsive.

CUB is disturbed by the fact that the Company continues to fail to provide modeling evidence to back up sharing percentages – sharing percentages that, in CUB's memory, were never intended to be permanent.[34] Indeed, the sharing percentage discussed in the original optimization docket was to be used as a determinant of when revenue sharing would start – it was not a ceiling it was a floor.[35]

CUB asked NWN a data request as to why NWN does not track optimization transactions. The Company's answer was largely unresponsive. The final sentence states "Mist

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[31] UM 1654 CUB/323/Jenks-McGovern (NWN Response to CUB DR 103).
[32] UM 1654 CUB/323/Jenks-McGovern (NWN's Response to CUB DR 103).
[33] UM 1654 CUB/324/Jenks-McGovern (NWN Response to CUB DR 104).
[34] UM 1654 CUB/110/Jenks-McGovern/6-7 (conditions included lots of reporting for monitoring purposes to see if the mechanism was working or needed to be adjusted).
[35] UM 1654 CUB/106/Jenks-McGovern/1.

is operated as integrated facility such that the particular dispatch of reservoirs, compressors and other equipment is not based on Core versus Interstate ownership, but rather, by what is collectively more efficient and cost-effective."[36]

The lack of tracking and the additional deliverability percentage numbers appear to be NWN's way of playing the numbers to ensure a higher return for shareholders. Regardless of NWN's assertions, it is not deliverability that is essential to the functioning of the optimization program, and it is not capacity that is essential to the functioning of the optimization program. Rather, it is core customer owned working gas used for actual optimization that is essential to the functioning of the optimization program – and ratepayers own 100% of the 62% of all working gas stored at Mist that is used for optimization. Clearly, the fact that the whole well is made up of 62% customer gas and 38% *other* gas[37] should have no impact on the fact that 100% of gas from that well that is used for optimization comes from core customers entitling the core customers to receive the bulk of the revenues.

In February, the Commission asked NW Natural how much optimization would occur, if only core gas was stored at Mist:

> Alternatively, assume that NW Natural made investments in Mist in or after 2001 only to meet core customer needs. What core customer investments would the company have made, and when would they have been made? What optimization activities could the company conduct with Mist storage using the previously existing facility, with only these hypothetical customer investments in and after 2001? For each year since 2001, compare actual yearly Mist optimization results with the results of Mist optimization using the pre-existing facility with only core customer investments.[38]

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[36] UM 1654 CUB/307/Jenks-McGovern (NWN Response to CUB DR 46).
[37] UM 1654 July 10, 2014, Hearing Transcript/10 lines 16-24.
[38] February 21, 2014 Memorandum and Bench Request/2 at section 2. Mist Storage Optimization (a)(2).

The Company responded with an attachment to its Bench Request answer, which shows that if the Company had expanded Mist to meet the needs of its core customers without adding capacity for interstate storage, [redacted][39] Clearly, this shows that using deliverability as the basis of assigning the revenue between core and non-core customers shortchanges core customers.

Schedules 185 and 186 should be revised to acknowledge that only core customer gas can be used for optimization. In recognition of the value that ratepayers have provided to NWN's optimization activities any revenue from those activities should be shared with ratepayers with 90 percent to core customers/10 percent to NWN. If the Commission finds that this proposed sharing percentage fails to fully compensate the Company for the deliverability value that interstate storage brings in allowing optimization of core gas, then the Commission could consider setting sharing at 80/20.

[39] Confidential Attachment to NW Natural's answer to February 21, 2014 Bench Request 2 titled Mist Storage Optimization Scenarios (in the quotation, the numbers [redacted] to [redacted] refers to Dth/d). CUB's numbers here are simply the sum of the core optimization revenues from 2005 to 2013.

8. Contrary to NWN's arguments, NWN's $65m Dollar Investment Is Largely Irrelevant Here.

NW Natural has repeated regularly in this docket that it has invested $65 million[40] in interstate storage and customers will benefit as that interstate storage gets recalled.[41] This is true. NW Natural has invested $65 million and has depreciated some of that down and has had some of that investment recalled.[42] Currently, there is about $41 million of investment remaining.[43] However, based on the net income in 2012 from storage and optimization of storage of [redacted],[44] NW Natural is earning a return on equity for its investment of [redacted][45]

In addition, while the Company cites recall as a benefit to customers, it is better to view it as a shared benefit. Customers get storage at a reduced investment level (partially depreciated) -- though with a reduced expected life. Shareholders get a significant reduction in risk if the demand for interstate storage decreases in the future. The new PGE North Mist storage, which is not part of this docket, comes with a 30 year contract associated with the expected life of a gas plant.[46] This provides assurance that allows NWN's shareholders to make an investment in storage. But the interstate storage at Mist that is an issue in this docket is not under 30 year contracts tied to a particular generating asset. NWN is taking a risk that the storage market could

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[40] *See for example* February 3, 2014 Hearing Transcript/85 line 18; UM 1654 NWN/100/White/5 lines 16-17; UM 1654 NWN/100/White/15 lines 1-7.

[41] UM 1654 CUB/321/Jenks-McGovern (NWN Data Response to CUB DR 100 Attachment 1 CONFIDENTIAL); UM 1654 CUB/324/Jenks-McGovern (NWN Data Response to CUB DR 104).

[42] UM 1654 CUB/301/Jenks-McGovern (NWN Data Response to CUB DR 27) Confidential; UM 1654 CUB/322/Jenks-McGovern (NWN Data Response to CUB DR 322) Confidential; UM 1654 CUB/304/Jenks-McGovern (NWN Data Response to CUB DR 34).

[43] UM 1654 NWN/303/White/1.

[44] UM 1654 NWN February 3, 2014 Confidential Hearing Exhibit 8.

[45] UM 1654 CONFIDENTIAL NWN Hearing Exhibit 8 [redacted]

[46] OPUC Advice Filing 14-7 page 2 "Rate Schedule 90" last paragraph. (May 5, 2014).

shrink. Recall reduces this risk. It is unclear whether NW Natural would have taken on the risk to invest in interstate storage without the risk reduction associated with recall.

But CUB is not arguing against this set-up. The current arrangement related to investment in interstate storage, sharing of interstate storage revenues and recall of interstate storage is all reasonable – though CUB would like to see a cost of service study. Our only objection to Interstate storage relates to how interstate storage is used to divert Mist Optimization revenues.

According to the Company's testimony, the sharing with core customers does not kick in until the Company has deducted its expenses and one of those expenses is depreciation.[47] The Company also says that until the investment is recalled the Company receives no return on its investment.[48] But this is misleading. It does not receive a guaranteed regulated return, but the net revenue it receives is greater than its allowed return, so it does better before storage is recalled.

Regardless of what NWN invested in Mist, it is still using 100% core customer working gas for the optimization program at Mist and that 100% is the only percentage number that is important when calculating the compensation that should be paid to core customers as a result of any successful optimization activities.

9. What are the currently rate based core customer assets at issue in this docket?

At the February 3, 2014 Hearing, in terms of Storage, Company witness Mr. White stated

[47] UM 1654 February 3, 2014 Hearing Transcript at 79 lines 14-20.
[48] UM 1654 February 3, 2014 Hearing Transcript at 82-83.

the Company did make “some shared use of facilities.”[49] He further stated that the primary shared facilities were “the LDC transmission lines.”[50] And he noted that there were some shared facilities at the site.[51] The primary focus of NWN’s witnesses was, however, to tell us all about ratepayers getting the shared use of an asset (compressor) paid for by shareholders and used for optimization.[52] CUB notes that NWN did not also state that shareholders were getting the use of customer owned gas to run through their compressor. Storage and optimization programs need both equipment (such as compressors) and gas in order to conduct business. As noted above, the majority of the working gas in Mist storage is ratepayer gas - 62% - and all of the gas used for optimization is core customer working gas.

CUB has for sometime suspected that NWN might be understating the number of shared facilities relevant to this docket and therefore asked a series of data requests in that regard. According to NWN’s response to CUB DR 95,[53] “[a]pproximately 56 underground gas reservoirs have been discovered at Mist, of which 7 have been produced and developed into storage, while another 12 are currently in some state of being produced. The rest of the reservoirs have been produced to the ends of their respective useful lives. None of the reservoirs are in rate base aside from the 3 storage reservoirs fully used by the Core (Bruer, Flora and Al’s Pool) and a portion of a fourth storage reservoir that has been partially recalled (Reichhold).”[54,55] So that makes three complete reservoirs and one partial reservoir in rate base. And, according to

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[49] UM 1654 February 3, 2014 Hearing Transcript at 20 line 25.
[50] UM 1654 February 3, 2014 Hearing Transcript at 21 lines 1-2.
[51] UM 1654 February 3, 2014 Hearing Transcript at 21 lines 9-10.
[52] UM 1654 February 3, 2014 Hearing Transcript at 100 lines 21-24.
[53] UM 1654 CUB/316/Jenks-McGovern (NWN Data Response to CUB DR 95).
[54] UM 1654 CUB/316/Jenks-McGovern (NWN’s Response to CUB DR 95).
[55] UM 1654 CUB/ 300/Jenks-McGovern (NWN’s response to CUB DR 26).

NWN's Response to CUB DR 40,[56] "[t]he shared facilities at the Mist central operations site (referred to as "Miller Station") consist of three previously installed compressors (1 turbine and 2 reciprocating totaling approximately 8,000 HP), gas processing equipment (primarily for dehydration), and the pipelines and appurtenances (meters, valves, etc. used to connect them with the gas entering Miller Station from the storage reservoirs, plus the control building (electronic systems used to monitor and control the operations 24/7) and other pre-existing buildings and structures (a shop for maintenance activities, parts storage, security systems, etc.) that are used by Miller Station staff."[57] This is quite an extensive list of shared facilities.

Then in NWN's Response to CUB's DR 94[58] the items in rate base are further identified, with some repetition, as follows:

[56] UM 1654 CUB/305/Jenks-McGovern (NWN Response to CUB DR 40).
[57] UM 1654 CUB/305/Jenks-McGovern (NWN's Response to CUB DR 40).
[58] UM 1654 CUB/315/Jenks-McGovern (NWN's Response to CUB DR 94).

In rate base

Bruer Reservoir	Odorization equipment
Flora Reservoir	Bunk house
Al's Reservoir	Standby generation
Reichhold Reservoir	Filtration
Miller Station (Compression Facility)	Pressure and flow control
KC 300 reciprocating compressor	Buildings
KC 400 reciprocating compressor	Fire suppression system
GC 500 centrifugal (turbine) compressor	Data lines
Dehydration System (in service 1989)	Power lines
Cushion Gas	Security system
North Mist Pipeline - 12" pipeline to	Water tanks
North Coast Feeder	Fuel storage
South Mist Feeder - 16”	Methanol storage
South Mist Pipeline Extension - 24"	Communications
Gathering pipelines	Microwave
Acreage	Water treatment
Mineral rights	Vehicles
Monitoring equipment	Spare parts
Metering equipment	Tools
Processing equipment	Computers

CUB asks the Commission to particularly take note of the appearance of cushion gas in this list – see CUB’s prior testimony.[59] Cushion gas is one of the items necessary for *deliverability*. CUB respectfully reminds the Commission that CUB has previously detailed its concerns with regard to the use of uncompensated ratepayer cushion gas used in the determination of sharing percentages. [redacted] of the cushion gas is owned by core customers.[60]

Other customer assets used: CUB notes that in Confidential CUB DR 96[61] the Company states that it [redacted][62] Combined, these assets comprise a great deal of shared assets whose use for storage and optimization should be reflected

[59] UM 1654 CUB/200/Jenks-McGovern/15-18.
[60] UM 1654 CUB/313/Jenks-McGovern (NWN’s Response to CUB DR 81) Confidential.
[61] UM 1654 CUB/317/Jenks-McGovern (NWN’s Response to CUB DR 96) Confidential.
[62] UM 1654 CUB/317/Jenks-McGovern (NWN’s Response to Confidential DR 96) Confidential.

appropriately in any sharing percentages based upon deliverability. It is unfair for NWN to retain 55%[63] of the net revenues produced by using core customer gas for Mist Optimization. As discussed earlier, NWN has chosen to assess the income associated with Mist optimization based on *deliverability* and to then to use its interstate storage sharing percentage for sharing optimization revenues that it arbitrarily assigned to interstate storage. Because NWN receives 80% of the revenues from interstate storage, and customers receive 67% of the revenues from optimization, NW Natural's retains 55% of the net income from optimizing core customer gas at Mist.

While NW Natural generally refers to compressors and pipelines as shared assets, it seems likely that a very great deal more shared assets are in fact in play in this docket. And clearly, NWN has failed to sufficiently identify how any of these shared assets are accounted for in sharing with customers in both the storage and optimization sectors of the business. A cost based study is needed. In testimony, CUB called for including Mist Storage in the Company's Cost of Service study as a way to examine whether customers were adequately compensated for shared assets. However, as this docket has progressed, CUB has become increasingly concerned about the lack of transparency by NWN. CUB now believes that it would be appropriate for the Commission to consider the prior Staff proposal for a cost study made in Docket UG 221:

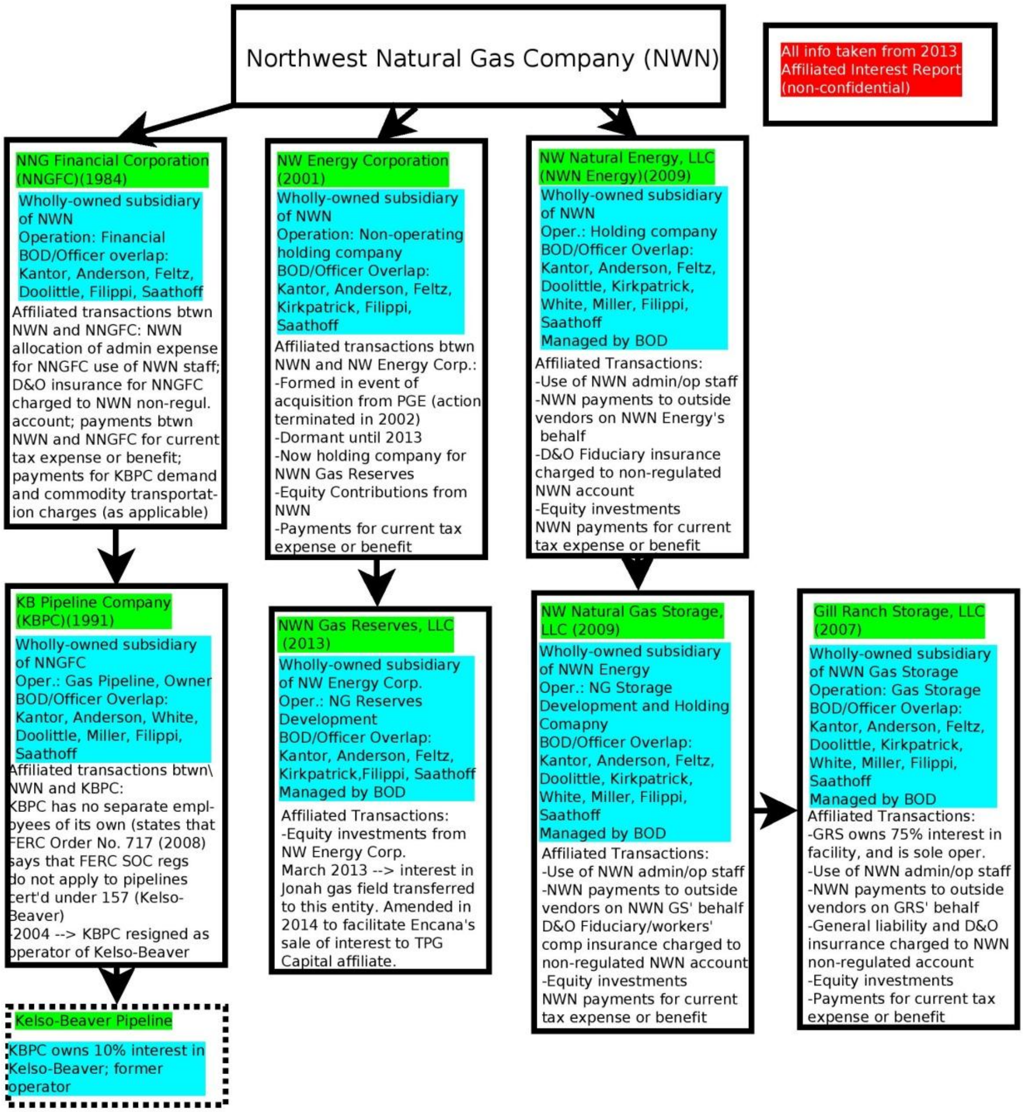
[63] See the breakdown of this calculation near the end of Section II of this brief.

> I recommend the Commission order NWN to conduct an independent review of the operation and financing of the Mist storage facility since its construction through an outside third party chosen by the Commission. This review should be conducted over the six-nine months following the final order in UG 221, with a report detailing the results and recommendations of the reviewers delivered to staff and UG 221 Parties no later than December 31, 2013.[64]

9. Governance – which entity does what and how are incremental costs allocated?

CUB was left scratching its head after the first hearing as to how many NWN subsidiaries are involved in storage and optimization, what those subsidiaries real relationship is to the utility, and how employee time for each entity is tracked. Even after a substantial number of data requests, the Company has still failed to adequately demonstrate how all this works and which FTEs to count towards sharing.[65] To help me with this concept my law clerk Jordan Bailey drafted the following flow chart which I now include as a figure in this brief in the hope that it will be equally enlightening to others.

64 UM 1654 CUB/100 Jenks-McGovern/5 lines 21-27 citing to UG 221 - Staff/1000/Zimmerman/12.
65 *See for example* CUB Exhibit 303 - NWN's Response to CUB DR 29.



Northwest Natural Gas Company (NWN)
All info taken from 2013 Affiliated Interest Report (non-confidential)
NNG Financial Corporation (NNGFC)(1984)
Wholly-owned subsidiary of NWN
Operation: Financial
BOD/Officer overlap: Kantor, Anderson, Feltz, Doolittle, Filippi, Saathoff
Affiliated transactions btwn NWN and NNGFC: NWN allocation of admin expense for NNGFC use of NWN staff; D&O insurance for NNGFC charged to NWN non-regul. account; payments btwn NWN and NNGFC for current tax expense or benefit; payments for KBPC demand and commodity transportat-ion charges (as applicable)
NW Energy Corporation (2001)
Wholly-owned subsidiary of NWN
Operation: Non-operating holding company
BOD/Officer Overlap: Kantor, Anderson, Feltz, Kirkpatrick, Filippi, Saathoff
Affiliated transactions btwn NWN and NW Energy Corp.:
-Formed in event of acquisition from PGE (action terminated in 2002)
-Dormant until 2013
-Now holding company for NWN Gas Reserves
-Equity Contributions from NWN
-Payments for current tax expense or benefit
NW Natural Energy, LLC (NWN Energy)(2009)
Wholly-owned subsidiary of NWN
Oper.: Holding company
BOD/Officer Overlap: Kantor, Anderson, Feltz, Doolittle, Kirkpatrick, White, Miller, Filippi, Saathoff
Managed by BOD
Affiliated Transactions:
-Use of NWN admin/op staff
-NWN payments to outside vendors on NWN Energy's behalf
-D&O Fiduciary insurance charged to non-regulated NWN account
-Equity investments
NWN payments for current tax expense or benefit
KB Pipeline Company (KBPC)(1991)
Wholly-owned subsidiary of NNGFC
Oper.: Gas Pipeline, Owner
BOD/Officer Overlap: Kantor, Anderson, White, Doolittle, Miller, Filippi, Saathoff
Affiliated transactions btwn\ NWN and KBPC:
KBPC has no separate empl-oyees of its own (states that FERC Order No. 717 (2008) says that FERC SOC regs do not apply to pipelines cert'd under 157 (Kelso-Beaver)
-2004 --> KBPC resigned as operator of Kelso-Beaver
Kelso-Beaver Pipeline
KBPC owns 10% interest in Kelso-Beaver; former operator
NWN Gas Reserves, LLC (2013)
Wholly-owned subsidiary of NW Energy Corp.
Oper.: NG Reserves Development
BOD/Officer Overlap: Kantor, Anderson, Feltz, Kirkpatrick,Filippi, Saathoff
Managed by BOD
Affiliated Transactions:
-Equity investments from NW Energy Corp.
March 2013 --> interest in Jonah gas field transferred to this entity. Amended in 2014 to facilitate Encana's sale of interest to TPG Capital affiliate.
NW Natural Gas Storage, LLC (2009)
Wholly-owned subsidiary of NWN Energy
Oper.: NG Storage Development and Holding Comapny
BOD/Officer Overlap: Kantor, Anderson, Feltz, Doolittle, Kirkpatrick, White, Miller, Filippi, Saathoff
Managed by BOD
Affiliated Transactions:
-Use of NWN admin/op staff
-NWN payments to outside vendors on NWN GS' behalf
D&O Fiduciary/workers' comp insurance charged to non-regulated NWN account
-Equity investments
NWN payments for current tax expense or benefit
Gill Ranch Storage, LLC (2007)
Wholly-owned subsidiary of NWN Gas Storage
Operation: Gas Storage
BOD/Officer Overlap: Kantor, Anderson, Feltz, Doolittle, Kirkpatrick, White, Miller, Filippi, Saathoff
Managed by BOD
Affiliated Transactions:
-GRS owns 75% interest in facility, and is sole oper.
-Use of NWN admin/op staff
-NWN payments to outside vendors on GRS' behalf
-General liability and D&O insurrance charged to NWN non-regulated account
-Equity investments
-Payments for current tax expense or benefit

FIGURE 1 – The many subsidiaries and their relationship to NWN (data taken from DR 42[66] - 2013 Affiliated Interest Report – non confidential)

From the Hearing Transcript Testimony, it appears that Northwest Natural Gas Storage, LLC handles marketing and contracting of NWN's interstate and intrastate storage services.[67] Mr. White has to sign off on the marketed deals on behalf of NWN which is actually providing the inter/intrastate storage service.[68] Mr. White's time is not tracked and charged "because his position is not an incremental add due to Mist Storage Services."[69] Therefore, core customers are compensated for "loaning" Mr. White to interstate/intrastate storage through the 80/20 sharing percentage.

On the optimization side, it appears from the Transcript Testimony that Randy Friedman oversees optimization. While optimization, unlike storage, is not handled by a subsidiary, the bulk of it is handled by a third party – Tenaska.[70] This, as we will discuss later, greatly reduces NWN's risk.[71]

Next, NW Natural describes why storage and optimization are not fully run by subsidiaries by stating that what those programs do "is not big enough" so NWN has created a

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[66] UM 1654 CUB/306/Jenks-McGovern (NWN Response to CUB DR 42).
[67] UM 1654 February 3, 2014 Hearing Transcript at 23 line 6.
[68] UM 1654 February 3, 2014 Hearing Transcript at 22 lines 18-23.
[69] UM 1654 CUB/314/Jenks-McGovern (NWN Response to CUB DR 87).
[70] UM 1654 February 3, 2014 Hearing Transcript at 23 line 13-15.
[71] http://www.tenaska.com/wp-content/uploads/2013/02/Facts-And-Figures1.pdf "Tenaska Marketing Ventures/Tenaska Marketing Canada (TMV) is ranked by leading industry news publication *Platts Gas Daily* among the top 10 natural gas marketers in North America based on wholesale physical volumes sold. TMV sold or managed 2.5 trillion cubic feet of natural gas in 2013, a volume equal to about 9.5 percent of the total U.S. natural gas consumption. *TMV helps its customers manage their natural gas needs efficiently, bringing added value and reduced financial risk. (emphasis added).* As noted in the more detailed discussion of optimization later in this First Post-hearing Brief, CUB continues to explore the issue of risk and encourages the Commission to do likewise.

profit center.[72] Mr. White concludes stating that all incremental costs related to this profit center and storage and optimization are recorded below the line.[73]

Given that the Company did not conduct studies on avoided costs when the initial investments were made,[74] CUB is concerned by how these incremental costs are determined and allocated – the process described by Mr. White is not exactly scientific,[75] and CUB is concerned about how the non-incremental costs are not determined and not allocated. Indeed, the Company characterizes, in its original filing documents, the percentages set then as "somewhat anecdotal."[76] And even then, it was arguing that a cost allocation approach was not desirable – the Company stated that the cost allocation was not needed for setting FERC rates, that it "would be difficult to determine what fixed costs to appropriately assign given their fixed cost nature and the fact that it is more efficient to operate storage facilities as an integrated whole rather than to attempt to allocate individual reservoirs to core and interstate customers."[77] The Company ultimately did go on to prepare a simplistic cost allocation analysis but their intent in doing so was to "illustrate the amount of complexity and work that would need to be involved to perform a more complete study each year."[78]

CUB is not dissuaded from pursuing a cost study. After 13 years, it is time to do a study that is for more than "illustrative" purposes. Right now, CUB cannot even tell how to account for FTE costs in determining sharing.[79] CUB asked a data request related to incremental costs

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[72] UM 1654 February 3, 2014 Hearing Transcript at 25 lines17-21.
[73] UM 1654 February 3, 2014 Hearing Transcript at 26 lines 1-10.
[74] UM 1654 CUB/105/Jenks-McGovern (NWN Response to CUB DR 3).
[75] UM 1654 February 3, 2014 Hearing Transcript at 27 lines 15-20.
[76] UM 1654 CUB/106/Jenks-McGovern/ 1-2.
[77] UM 1654 CUB/106/Jenks/McGovern/3 at Section 2. A..
[78] UM 1654 CUB/106/Jenks-McGovern/3 Section 2. B. 3.
[79] UM 1654 CUB/303/Jenks-McGovern (NWN Response to CUB DR 29).

for Mist storage.[80] The data request was based on statements made by Mr. White and Mr. Friedman at the February 3, 2014 Hearing. At the hearing, those witnesses stated that incremental costs were paid for by storage.[81] Non incremental costs must fall to system. CUB asked the Company to identify costs on a list as incremental or non-incremental – the answers were illuminating. For example, in regard to the time spent by NWN's Treasurer on the financing of interstate storage, the answer was that it was non- incremental because "there have not been any separate financings for interstate storage. The capital requirements for individual expansions have been worked into the overall Company capital budget and associated financing plan."[82]

These answers and this methodology about how NWN categorizes incremental costs seem to be in contrast to the original Staff Report of 2000, detailing the basis for recommendation of support for Interstate Storage.[83] In that Report, Staff Recommendation #1 insisted that the Company produce an annual pro forma financial statement utilizing an incremental cost methodology, but Staff's definition included "any incremental investment or O&M above core customer needs."[84] The time Mr. White spends on interstate storage is incremental above core customer needs. The time the Treasurer spends arranging financing for interstate storage is above customer needs, even if it is combined with capital projects associated with core customers. NW Natural defines incremental costs as costs not currently in rates. Staff defined it as costs not serving core customers.

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[80] UM 1654 CUB/302/Jenks-McGovern (NWN Response to CUB DR 28).
[81] UM 1654 February 3, 2014 Hearing Transcript/112 lines 1-3 and 19-25.
[82] UM 1654 CUB/302/Jenks-McGovern (NWN Response to CUB DR 28 (a) but see also the answers to (b)-(e)).
[83] UM 1654 CUB/110/Jenks-McGovern/6 at Staff Recommendation (1) and at pg. 3.
[84] UM 1654 CUB/110/Jenks-McGovern.

NWN contends that if a cost of service study were to be conducted it would show that customers should not be receiving any sharing at all.[85] However, NWN does not want a cost of service study conducted and went out of its way at the February 3, 2014 hearing to try and state every reason that a cost of service study would be inappropriate.[86]

In CUB's eyes, what is inappropriate is that for twelve years NWN has been able to retain the same sharing percentages without the transparency provided by a cost of service study. It is long past time that a transparent cost study should have been conducted for Mist detailing governance structure, employee time etc.

10. NWN's long experience with third party optimization (Tenaska) results in significant decreases in risk for the Optimization Program – should NWN still receive an incentive of any kind?

CUB does not agree that what NWN is doing requires them to earn a higher incentive.[87] Why does NWN need such a large incentive to participate in the optimization of customer assets when doing so is, after 13 years, no longer new or unique to NWN or anyone else; when NWN is not personally doing the optimizing (whether or not the optimizing that is being done for it is unique) and when the optimization is being carried out in a largely risk free manner to NWN using many customer assets? This is especially perplexing when one considers how the gross proceeds are divided, according to NW Natural, this is how the optimization percentages are divided:

[85] UM 1654 February 3, 2014 Hearing Transcript at 101 at 22.
[86] UM 1654 February 3, 2014 Hearing Transcript at 116 -117.
[87] Mr. Friedman testified to the Company's whole motivation is to make the pie bigger because we know if we do both of our key stakeholders are going to benefit. And that's actually really empowering." UM 1654 February 3, 2014 Hearing Transcript at 70 lines 8-11.

> So Tenaska is going to get [redacted] percent of that. [redacted] percent of it we retain. And then [redacted] percent go through [redacted] to customers, [redacted] to the company shareholders. So when you apply that math, basically what's going on in an average year is customer are getting [redacted] percent of what we're able to create, and Tenaska is getting a [redacted], and the company shareholders are getting a [redacted].[88]

But this is misleading. Tenaska gets [redacted]% and NW Natural retains [redacted]%. NW Natural leaves out the step of assigning some of the revenues from Mist optimization to interstate and retaining 80% of this. Adjusting for this means that Tenaska gets [redacted]%, NW Natural gets more than [redacted]%, and customers get less than [redacted]. CUB does not oppose Tenaska getting [redacted]% as Tenaska is providing the optimization expertise and taking on the bulk of the risk associated with optimization. But if Tenaska is providing the expertise and taking on the risk, why is NW Natural is getting more than [redacted]%? Finally, when this is an activity that is making money off core customer assets, why do core customers get less than [redacted] of the revenue?

Un-phased by the Enron debacle, NWN, after casting around for how to earn more from Mist, hit on the idea of the backdraft deal with Tenaska[89] who by contract carries most of the risk.[90] After years of working with Tenaska NWN is now very experienced and further removed from trading risks. Remember what NWN is doing is no longer, even it once was, new or unique. Lots of utilities do this[91] - NWN is only one of them. As stated by NWN at the July 10, 2014 Hearing: [redacted]

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[88] UM 1654 February 3, 2014 Hearing Transcript at 69 lines 9-16.
[89] UM 1654 February 3, 2014 Hearing Transcript at 51 lines 1-4.
[90] UM 1654 February 3, 2014 Hearing Transcript at 54 lines 5-6 – Tenaska is "[d]oing very speculative financial trades that are prohibited by our gas supply risk management policy."; CUB/102/Jenks-McGovern at Article V and Article IX.
[91] UM 1654 CUB – Pre-hearing Brief at 6-12, Section V 1 A-C.

[redacted][92] "We would be moving gas to Tenaska in March and they will return it to us back in April."[93] In other words, "the more transactions [Tenaska] can do to make money on, the more revenues you're creating for Tenaska and us to share, which means more revenues for us and the customers to share."[94] "And then this was the – this was the simple version of this, how [NWN] started. And then over the years its grown to encompass other months also, but this is, at its essence, what started us doing Mist – optimization."[95]

> [W]hen we first started doing the backdraft optimization. [redacted]
>
> [redacted][96]

Also during the July 10, 2014 Hearing, in regard to its *experience* with optimization, the company stated:

> Well, what we've been doing is we've actually been building up. [redacted][97]

In fact on February 3, 2014 Mr. Friedman described the long-range long-term

[92] UM 1654 February 3, 2014 Hearing Transcript at 45 lines 1-5.
[93] UM 1654 February 3, 2014 Hearing Transcript at 53 lines 20-21.
[94] UM 1654 February 3, 2014 Hearing Transcript at 57 lines 12-15.
[95] UM 1654 February 3, 2014 Hearing Transcript at 58 lines 8-13.
[96] UM 1654 July 10, 2014 Hearing Transcript/18 lines 18-25 and 19 lines 1-4 (emphasis added) Confidential.
[97] UM 1654 July 10, 2014 Hearing Transcript/20 lines 9-16 (emphasis added) Confidential.

relationship as follows:

> And one of the really interesting things about this as we got into it is by setting this up months and months and months ahead of time, like in the summer of the year before, they're actually financially trading this March-April spread. Watching for it to move, trading in - - in and out of it. *Doing very speculative financial trades that are prohibited by our gas supply risk management policy* .[98]

In response to CUB DR 63,[99] the Company provides its risk management policies which discuss why derivatives "[redacted][100] CUB is confused. The Company has, on multiple occasions, justified its large cut of revenues based on risk but its actions seem to demonstrate that it has set up its optimization program so as to designate the extreme risk to Tenaska and retain only modest risk for itself. The Company cannot have it both ways. Either its experienced or its not. Either its new or its not. Either its risky or its not. The Company obviously feels that the involvement in optimization and storage outweigh any risks. There is no basis upon which to continue to pay NWN a large incentive.

11. NWN's Inability To Keep Its Stories Straight.

NWN has stated the basis of the 20/80 storage sharing as being shared assets.[101] The basis of the 67/33 pipeline optimization as being primarily the unique nature of liquids extraction.[102] And, the basis of the 45/55 Mist optimization as being deliverability (see prior arguments). CUB notes that the Commission asked for more information on NWN's liquid extraction in its February 21, 2014 Bench Requests. In its response to the February 21, 2014

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[98] UM 1654 February 3, 2014 Hearing Transcript/53 lines 24 – 25 and at 54 lines 1-6 (*emphasis added)*.
[99] UM 1654 CUB/310/Jenks-McGovern (NWN Response to CUB DR 63) Confidential.
[100] UM 1654 CUB/310/Jenks-McGovern (NWN Response to CUB DR 63 confidential attachment 4 page 12).
[101] UM 1654 NWN/100/White/2, lines 19-23.
[102] UM 1654 February 3, 2014 Hearing Transcript/31, lines 1-6.

Commission Bench Request, NWN continued to insist that what it does is unique and therefore carries risks beyond those undertaken by other utilities.[103] As discussed below, CUB does not accept this assertion. NWN is greatly removed from any risk because of its contract with Tenaska, regardless of what other companies do or do not do. Tenaska makes the trades and carries the risk.[104] Even the Company realizes this "by using a third party, though, they are taking that trading risk."[105]

After liquids extraction, the Company justified its retention of 55% of Mist optimization revenues with a discussion of compressors. For that reason, CUB asked NWN a data request related to compressors. NW Natural responded that with the rest of the Mist facility, this compressor is operated in an integrated fashion – "it would be impossible to track this unit's operation to a specific percentage of core gas being placed into or pulled out of Mist Storage."[106] And so NWN moved once again to its argument that the sharing of revenues was based on deliverability not upon specific compressors.[107]

Recently, just prior to the July 10, 2014 Hearing, NWN submitted Supplement Bench Request Responses to the Commission,[108] trying to explain again the process it utilizes and upon which the methodology for calculating percentages is based. But at the hearing, it became clear

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[103]UM 1654 March 5, 2014 NWN Responses to Bench Requests 1(a) pages 1-6 Confidential.

[104] http://www.tenaska.com/wp-content/uploads/2013/02/Facts-And-Figures1.pdf "Tenaska Marketing Ventures/Tenaska Marketing Canada (TMV) is ranked by leading industry news publication *Platts Gas Daily* among the top 10 natural gas marketers in North America based on wholesale physical volumes sold. TMV sold or managed 2.5 trillion cubic feet of natural gas in 2013, a volume equal to about 9.5 percent of the total U.S. natural gas consumption. *TMV helps its customers manage their natural gas needs efficiently, bringing added value and reduced financial risk. (emphasis added).* As noted in the more detailed discussion of optimization later in this First Post-hearing Brief, CUB continues to explore the issue of risk and encourages the Commission to do likewise. UM 1654 March 5, 2014 NWN Responses to Bench Requests 1(b) pages 6-8; UM 1654 March 28, 2014 NWN Supplemental Response to Bench Request No.1(Pursuant to Modified Protective Order).

[105] UM 1654 February 3, 2014 Hearing Transcript at 39 lines 10-11.

[106] UM 1654 CUB/319/Jenks-McGovern (NWN's Response to CUB DR 98).

[107] UM 1654 July 10, 2014 Hearing Transcript/25 at 17.

[108] UM 1654 NWN Hearing Exhibit 13.

that all of the information presented in both the original and Supplemental Bench Responses to the Commission June 3, 2014 bench Requests was based on "illustrative" numbers[109] – more fuzzy math that only further confused the issues on the table.

Currently, NWN retains 55% of Mist optimization revenues even though Mist optimization utilizes core customer gas. NWN has had trouble explaining the basis for this sharing and why deliverability is the key concept utilized in the sharing. After three rounds of testimony, a Pre-hearing Brief and two hearings, and answers and supplemental answers to two sets of Bench Requests, it is time to recognize that NWN has not met its burden of proof to show on a factual basis that optimization revenues should be allocated based on deliverability. As a result, CUB respectfully recommends that the Commission modify the sharing percentages as requested by CUB.

12. NWN's disparate requests for treatment of customer assets – CUB's UM 1635 Fairness Test: A Tale of two assets testimony.[110]

In this gas optimization docket, NWN seems to be of the opinion that an old asset which was once paid for with customer dollars, but is no longer paid for with customer dollars, is no longer a current customer asset whose use is subject to revenue sharing with current customers.[111] This is an interesting position for NWN to take given that in the UM 1635 docket, NWN is of the opinion that an old Company asset, paid for with customer dollars, is a current customer asset today and the cost of its clean-up must be paid for by today's customers who did

[109] UM 1654 July 10, 2014 Hearing Transcript/12 lines 12-16.
[110] UM 1635 CUB/200/Jenks/2 – 4.
[111] UM 1654 CUB/300/Jenks-McGovern (NWN's Response to CUB DR 26(d)) ("Production gas wells prior to 1995 may have been paid for with some mix of ratepayer and third party dollars. . . . Since 1995, all new gas production wells have been drilled by Enrfin Resources . . . . No ratepayer dollars have been used to pay Enerfin's exploration, drilling or development costs. NWN only pays for gas that is produced and delivered by Enerfin to NW Natural's system in that area. That gas purchase agreement with Enerfin is included in each year's PGA filing.").

not benefit from the service provided. CUB is of the opinion that what is sauce for one goose should also be sauce for the other – it's a matter of fairness. If customers are to be required to pay for the clean-up (development) of a Company asset from which they have never benefited then the Company must be required to pay customers for an asset even if the current customers did not personally benefit from its development. In other words, in terms of this docket, if a customer-paid-for asset is being used in the optimization process then the customer must be compensated for that asset's use whether it is, for example, the gas being pumped into a well, the well itself, the pipes the gas is flowing through or the compressor that is pumping the gas in.

As CUB set forth in its UM 1635 testimony, the question that must be asked is within the context of utility regulation in Oregon, does the proposal at issue seem fair? As stated by Mr. Jenks, to judge what is fair in one situation requires consideration of how similar situations are handled. In other words, context is important.[112] In this case, that means comparing NWN's UM 1635 environmental remediation docket with this UM 1654 NWN docket on Storage and Optimization. As noted above, at their core these two dockets are similar. They both start with property that was once used to produce gas for service to NWN Natural's customers. The Portland Harbor properties that are subject to the UM 1635 docket were used to manufacture gas from coal and petroleum in the early half of the 20th century in order to provide gas to retail customers. The property that is subject to UM 1654 was the site of production wells used to produce natural gas for retail customers beginning in 1979. Properties that were once used to manufacture gas from coal and oil are left with hazardous waste and are liabilities to their

[112] UM 1635 CUB/200/Jenks/2 at lines 24-25.

owners. Properties that were once production wells, depending on their geology, can become assets by becoming a place to store natural gas.[113]

On the one hand, NW Natural's position, as to its environmental remediation liability, is that the liability should fall primarily on customers. The Company is willing to apply excess earnings that are greater than 100 basis points above its authorized earnings to this liability, but it excludes earnings related to pipeline optimization, Mist storage optimization and liquids extraction. The Company clearly believes that the major responsibility for this liability should belong to customers.[114]

On the other hand, NW Natural's position on its storage/optimization asset is that its benefits should fall primarily on shareholders. While some of the Mist property remains in use for gas service for core customers, a significant portion is used for interstate/intrastate storage and optimization, where customers receive only 20% of the net income (after the Company has first recovered all of its costs). This sharing percentage is not based on the fact that the asset was created by producing natural gas for customers, but is instead based on the fact that the interstate/intrastate storage shares some equipment and personnel that is primarily used for core customers. If the property that was once production wells for core customers was used for interstate storage and optimization, but did not share the equipment and personnel that are currently used by core customers, NW Natural's theory of sharing would not require customers to receive any of the benefit.[115]

As noted by Mr. Jenks in his UM 1635 Phase II Response Testimony filed May 2, 2014, the above described NWN requests do not seem fair to CUB. In the past, NW Natural

[113] UM 1635 CUB/200/Jenks/3 lines 1 – 7.
[114] UM 1635 CUB/200/Jenks/3 lines 11 – 16.
[115] UM 1635 CUB/200/Jenks/3 lines 17 – 23 and at 4 lines 1-5.

manufactured gas from coal and oil for its retail customers. In the past, NW Natural also drilled production wells at Mist to produce gas for its retail customers. One former production site is a liability. One is an asset. NW Natural's current proposals in the two dockets would leave customers holding almost all of the liability and shareholders holding almost the entire asset. This makes little sense. Historic property used to produce gas for customers should be treated in a consistent manner regardless of whether the value is positive or negative.[116]

14. The case law previously reviewed by CUB

CUB stands by its prior case law analysis presented in its Pre-hearing Brief at pages 10-11. NWN Exhibit 103, which lists other optimization sharing agreements, fails to support NWN's current optimization arrangement. First, it fails to include Avista. Second, the majority of utilities listed share optimizations on a more generous basis with customers than NW Natural. Third, for 2 states, Maryland and Virginia, NWN shows a 50/50 sharing of the tailblock, but the Company fails to include the sharing that happens *before* the tailblock. In both cases, the sharing begins with a block that is passed through 100% to customers.[117] In both cases there is a second block where customers get 75% of the net revenues.[118] It is only in the case where net revenues are great enough to fall into the third block does the sharing percentage fall to 50/50.[119] Only one of the examples presented by NWN, AGC resources, has sharing that is clearly less generous to customers (60/40) than NW Natural's current 67/33 sharing of a segment of optimization revenues. CUB notes, however, that were the Commission to take into consideration NW

[116] UM 1635 CUB/200/Jenks/4 lines 6-13.
[117] *In re Petition of Commission's Staff for an Investigation into Washington Gas Light Company's Asset Management Practices and Cost Recovery of Natural Gas Purchases*, MD PSC Case No. 9158, Order No. 85059, 15 (Aug. 16, 2012); Washington Gas Light Company – Virginia Tariff Va S.C.C. No. 9 (issued Aug. 1, 2012), accessed at http://washgas.com/FileUpload?File/Tariffs/VA/va7579.pdf.
[118] *Id.*
[119] *Id.*

Natural's fuzzy math with its convoluted and misplaced percentages, even that exception would change.

IV. CUB'S RECOMMENDATIONS

No evidence has been elicited that would cause CUB to change its previously stated recommendations to the Commission although it does make the following modifications:

- that the Commission order implementation of a cost based study with appropriate in-depth analysis to be included in the next marginal cost study;
- that pending those results, CUB will not recommend any change to the Inter/Intrastate sharing percentages (20 customer/80 shareholder) (Note: Because of the inability to get good, factual information, CUB believes the Commission might want to expand this cost based study from CUB's marginal cost approach to a cost study along the lines proposed by Staff in UG 221);[120]
- that the Commission find that NWN has been misallocating net revenues from Mist Optimization to Interstate/intrastate storage and order that 47% of Mist Optimization Revenues be removed from Interstate/intrastate storage and the sharing percentage for all optimization activities including pipeline optimization should be set at 90% customer/10% utility, though CUB would be supportive of phasing this in with a step which moves the sharing from 67% customer/33% shareholder to 80% customer/20% shareholder (the inverse of the sharing percentage for interstate storage); and in addition that the Commission could go to 80/20 for Mist optimization if it finds that there is merit to the deliverability, cushion gas, or other working gas arguments made by NW Natural.

[120] UG 221 Staff/1000/Zimmerman/12 lines 8-19; UG 221 Staff/1900/Zimmerman/13 lines 15-20.

- that the Commission find that all AMA Optimization revenues must be included in the Company's ROO as utility income (Note: CUB is not proposing that interstate storage be included in the ROO as utility income).

Central to all of CUB's recommendations is the idea that full information disclosure assists all parties in reaching equitable, transparent, and agreeable resolutions. To this end, CUB supports all efforts to ensure that a cost of service analysis is conducted. CUB wishes to see ratepayers and investors both being fairly compensated, which seems only equitable in light of the Commission's statutory duty to impose fair, just and reasonable rates for all.

V. CONCLUSION

In conclusion, CUB recommends that the Commission make the following findings:

1. Optimization by utilities is not new.
2. NWN's form of optimization is not unique.
3. NWN has an obligation to maximize the value of regulated assets, including the use of those assets in a manner which generates revenue from non-retail markets and then use that revenue to reduce its revenue requirement from the customer who financed the assets.
4. Compensation for use of customer working gas should be based upon the percentage of customer gas utilized for the purpose of optimization– 100% - not upon deliverability provided by supporting gas.
5. The appropriate sharing percentage for interstate/intrastate storage is 20/80 pending the results of the cost study and optimization programs is 90/10

customers/shareholders (or alternatively 80/20 because some value is given to the role of deliverability).

6. The revenues from NWN's AMA Optimization are not exempt or special. They are . . . normal in the course of modern utility operations, and belong in NWN's ROO.

7. No cost based study has been conducted of the interstate/intrastate storage and optimization programs in many years and no independent third party evaluation has ever been conducted. A third party must be hired to conduct an in-depth cost based study of both the interstate/intrastate storage and optimization programs.

In summary, CUB respectfully requests that the Commission find that NW Natural has failed to carry the burden in this docket and that the optimization sharing percentages should be changed in favor of customers and that a cost study must be undertaken to confirm sharing percentages for the interstate/intrastate program.

Dated this 25th day of July, 2014.

Respectfully submitted,

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UM 1654 – CERTIFICATE OF SERVICE

I hereby certify that, on this 25th day of July, 2014, I served the foregoing **CITIZENS' UTILITY BOARD OF OREGON'S FIRST POST-HEARING BRIEF** in docket UM 1654 upon each party listed in the UM 1654 PUC Service List by email and, where paper service is not waived, by U.S. mail, postage prepaid, and upon the Commission by email and by sending one original and one copy by U.S. mail, postage prepaid, to the Commission's Salem offices.

(W denotes waiver of paper service)

(C denotes service of Confidential material authorized)

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