

**BEFORE THE PUBLIC UTILITY COMMISSION
OF OREGON**

UG 286 & UM 1722

In the Matter of)	
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PUBLIC UTILITY COMMISSION OF)	
OREGON,)	REPLY TESTIMONY OF THE
Investigation into Recovery of Safety Costs)	CITIZENS' UTILITY BOARD
by Natural Gas Utilities (UM 1722))	OF OREGON
)	
and)	
)	
NORTHWEST NATURAL GAS)	
COMPANY, dba NW NATURAL,)	
Request to Continue Schedule 177, the)	
System Integrity Program Recovery)	
Mechanism (UG 286))	
)	

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

March 9, 2016



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1 My name is Dr. Jaime McGovern, and my qualifications are listed in CUB
2 Exhibit 101.

3 **I. Introduction**

4 This docket, UM 1722, the generic Commission Investigation into the Recovery
5 of Safety Costs by Natural Gas Utilities, grew out of NW Natural's SIP docket, UG 286.
6 NW Natural withdrew Advice 14-23 on March 4, 2016, simultaneously requesting that
7 the Commission close UG 286. Therefore, CUB will be focusing its Reply Testimony on
8 UM 1722. Moreover, during the settlement conference on Tuesday, February 16th, 2016

1 parties agreed that new issues could be raised¹ in Reply Testimony. In particular, CUB,
2 Staff and NWIGU expressed interest in laying out, to the Commission, the rationale for a
3 safety planning approach that would inform the eligibility of any Safety Cost Recovery
4 Mechanism (SCRM). In Opening Testimony, CUB presented its concerns about the Joint
5 Utilities proposal for a cost recovery mechanism. CUB, in Opening Testimony, also
6 presented key principles for a SCRM. CUB believes that a SCRM should necessarily be
7 preceded by a Safety Planning Process (SPP). In this testimony, CUB will detail its
8 conception of a SPP and briefly address its response to Staff's and NWIGU's opening
9 testimony.

10 We provide our testimony in detail, but summarize the organization here:

11 I. Introduction

12 II. A Safety Planning Process and Cost Recovery Mechanism

13 III. CUB's response to Staff

14 IV. CUB's response to NWIGU

15 V. Conclusion and Recommendations

16 **II. A Safety Planning Process and Cost Recovery Mechanism**

17 In its Opening Testimony², CUB explained that the companies, under the
18 jurisdiction of the OPUC, have always had the opportunity to file for recovery of safety
19 investments. It is true that, in the absence of prudence demonstration, a utility does not
20 enjoy an unconditional guarantee of recovery. CUB continues to assert that no

¹ *In re NW Natural*, OPUC Docket No. UM 1722, Motion to Revise Procedural Schedule at 1 (Feb 29, 2016), <http://edocs.puc.state.or.us/efdocs/HAO/um1722hao142758.pdf>.

² UM 1722/CUB/100/McGovern/16-17.

1 reasonable mechanism should allow unconditional recovery. That is not at issue here.
2 Therefore, CUB addresses what it believes to be the issue. In UM 1722, the Joint
3 Utilities argue for overarching recovery allowance principles while, at the same time,
4 requesting an extreme amount of latitude for each utility and that each project be
5 considered individually. However, as a departure from traditional ratemaking this is
6 unilaterally an upside for the Joint Utilities. In fact, CUB believes that in the interest of
7 transparency and continuous improvement, changes should be made, but they should not
8 be in the scope of what the Joint Utilities are recommending.

9 Oregon engages in a two part process concerning utility investments to serve rate
10 payers. Phase 1 is the planning process and Phase 2 is the ratemaking process.
11 Fundamentally, the planning process and the ratemaking process address different issues.
12 The planning process aims to determine need and identify options to meet that
13 demonstrated need. Costs and risks are considered. However, in the ratemaking process,
14 and specifically, in a utility's general rate case, the prudence of the utility's investments is
15 considered, as well as compensation and risk for actual resources that are being used to
16 serve customers by the rate effective date.

17 Consider traditional regulatory practice. A RAP/Synapse report, *Best Practices*
18 *in Electric Utility Integrated Resource Planning*³ commends Oregon's IRP process as the
19 most straightforward of those studied. Moreover, the report highlights a key component
20 of the Commission Order that founded IRPs in Oregon: that in Oregon's IRP process, all
21 parties are engaged in determining the appropriate mix of resources to serve customers

³ <https://www.raponline.org/document/download/id/6608>

1 "at its earliest stages"⁴. The state's approach instructs parties to engage in a collaborative
2 process⁵ "to make the best assessment of appropriate risk measures." CUB believes that
3 the Companies should engage parties in a similar process regarding safety investments.
4 This could be done as a part of the IRP. For example, the IRP could have a chapter on
5 safety or it could be done in a separate safety planning docket. The process should
6 include the Company's DIMP. Here, we propose principles and timing that the Safety
7 Planning Process should encompass.

8 The Purpose of the SPP is to: (1) establish a demonstration of need for safety
9 remediation or mitigation, (2) allow the utility to explore which method would be most
10 appropriate, when considering risks, costs and benefits, and (3) establish a basis for the
11 Commission to evaluate investments that will later be recovered through the SCRM. The
12 SPP allows parties and the Commission to be involved in this process, offer valuable
13 feedback, and gain a comprehensive understanding of the safety goals and undertakings
14 of the utility. This ensures that the safety investments are effective and that the utility
15 may recover prudently incurred safety costs.

16 **Stage 1: SPP content requirements:**

- 17 1. The utility should identify the current functional and financial status⁶ of all
18 current and ongoing safety projects.
- 19 2. The utility should identify the safety standards it is trying to meet and identify
20 any safety deficiencies than need to be fixed in order to meet those standards.

⁴ OPUC Docket No. 180, Order No. 89-507 (April 20, 1989).

⁵ *In re Public Utility Commission of Oregon*, OPUC Docket No. UM 1056, Order No. 07-002 at Appendix A, Page 7 (Jan. 8, 2007).

⁶ *See infra*.

1 3. The utility should quantitatively assess the safety deficiency condition or risk
2 (for instance, miles of pipe at risk, chance of failure, financial impact of event, etc.).

3 4. The utility should propose and quantitatively assess multiple remediation and
4 mitigation measures (for example: manual intervention, automation, replacement of
5 infrastructure, etc) and detail the likelihood of success of each option.

6 5. The utility should explicitly detail how each plan moves towards a position of
7 safety sufficiency (i.e. how the replacement of the most at risk percentage of pipe reduces
8 risk by a certain percent, etc).

9 6. The utility should provide detailed accounting of all the safety mitigation
10 options considered, including alteration of capital depreciation.

11 7. The utility should identify the preferred safety remediation measure(s) for each
12 safety deficiency

13 8. The utility should provide a metric in the planning process allows parties to
14 consistently measure (1) status quo, and (2) progress made in Stage 2.

15

16 **Stage 1: SPP process requirements:**

17 1. The SPP should be filed with the Company's IRP or could be done through a
18 separate process.

19 2. At the time that the Company files its DIMP with PHMSA, it should also file a
20 copy with the Commission.

21 **Stage 2: SCRM content requirements**

22 The purpose of the SCRM is to allow recovery of capital costs associated with a
23 significant multi-year safety investment. CUB believes that such an approach is

1 appropriate because multi-year capital investments could otherwise result in annual
2 general rate cases to allow for cost recovery

3 1. In the SPP, the Company will have chosen a preferred safety measure. The
4 SCRM should have a metric which measures progress toward the remediation goal.

5 2. The SCRM should only include capital investments associated with safety
6 investments.

7 3. The projects and measurements included in the SCRM should be discrete well
8 defined projects that take multiple years to complete (not single year capital investments)

9 4. The SCRM should include updates to depreciation tables that reflect the safety
10 remediation measure's impact on capital longevity (i.e. replaced pipes should last longer).

11 5. The SCRM is only available for significant investments. The investment
12 should be expected to be greater than the utility's annual expected depreciation, so as not
13 to double charge customers. One option would be to set a threshold such as 100 basis
14 points from ROE or a percentage of annual revenue requirement.

15 6. In line with NWIGU's testimony⁷, the SCRM must not include costs for: (1)
16 inspection and monitoring, (2) locating pipe eligible for replacement, (3) "pipeline costs
17 associated with normal growth, system expansion, and repair and replacement of pipe
18 damaged by third parties"⁸.

19 7. The revenue requirement associated with the SPP should be subject to an
20 earnings test. Where appropriate, the rate base associated with a SPP will be moved into
21 base rates at the time of the next General Rate Case.

22

⁷ UM 1722/NWIGU/100/Finklea/8

⁸ UM 1722/NWIGU/100/Finklea/8

1 **Stage 2: SCRM process requirements**

2 1. The SCRM should begin only with a rate case so that the Commission can
3 ascertain what the Company's actual ROE is, what resources will be used in the safety
4 remediation measure, and whether they are already accounted for in base rates. This is in
5 line with FERC standard (1) that the Joint Utilities present in Opening Testimony⁹, and a
6 condition that cannot be accurately proxied by an 'earnings review'.

7 2. The SCRM should not exceed five years or the Company's next rate case,
8 whichever comes sooner. It should not be extended without a rate case.

9 Stage 1 in the safety process, the SPP, is integral to developing a robust and
10 effective safety program. Like other resources in which the utility invests to serve
11 customers, it is important to know why the safety project is needed, how it would
12 improve or eliminate a safety deficit, and how that can be measured. For many safety
13 issues, multiple options exist for resolution. For example, NWN used a method called
14 "inserted steel"¹⁰ to remediate sections of pipe that were susceptible to corrosion.
15 Alternatively, some at-risk pipes were replaced. Different methods or approaches may
16 make sense in different terrain or population densities, etc. However, it is important that
17 the Company demonstrate (1) what the problem is, (2) what the options are, and (3)
18 which option it deems most prudent.

19 The structure of the SCRM is also important. Only multiyear significant capital
20 safety investments should be eligible. If the safety cost was an expense and not an
21 investment, it could be deferred until the next general rate case. If the safety cost was an

⁹ UM 1722/Joint Utilities/100/Thompson-Andrews-Parvinen/11

⁸ UM 1722 NWN/200/KARNEY/3-4

1 investment, became useful in a single year, and it was significant, then the utility could
2 file a general rate case.

3

4 **III. CUB's Response to Staff**

5 CUB generally agrees with Staff that the Joint Utilities do not need special
6 incentive mechanisms to implement safety programs. Safety is, and should be, part of the
7 Joint Utilities' core business.¹¹ CUB also agrees, as acknowledged above, that under
8 very specific conditions, some capital safety investments may be eligible for a SCRM.¹²
9 The principles laid out in the Joint Utilities testimony are overly broad.

10 Staff also distinguishes between significant one time capital safety investments
11 and a plan that includes "numerous smaller projects"¹³. Although the Joint Utilities
12 believe that both of these should be eligible for a SCRM, CUB agrees with Staff that a
13 bundle of smaller projects does not constitute a significant capital investment, and
14 therefore should not be eligible. A utility with multiple small projects may have the
15 option of implementing them sequentially, or to stagger them in order to smooth costs. If
16 a project is small (in dollars) it is not significant in any one given year. Moreover, if it
17 must be performed over multiple years, then it is still small and the financial impact can
18 also be spread. Consistent with CUB's recommendation on a SPP and an SCRM,
19 discussing need and timelines for projects such as these would shed light on whether and
20 how they could be implemented during an IRP type process. This would improve the
21 ability to perform appropriate ratemaking treatment.

¹¹ UM 1722/Staff/100/Koho/2

¹² UM 1722/Staff/100/Koho/6

¹³ UM 1722/Staff/100/Koho/8

1 Finally, CUB echoes Staff's argument that the inclusion of all costs (or even just
2 capital investments) for "safety and/or reliability"¹⁴ is extremely broad. This has the
3 danger of being manipulated to include virtually everything in the Joint Utilities' system,
4 especially since they are experiencing little to no load growth.

5 To get some perspective of what "reliability" might encompass, CUB looked at
6 NW Natural's 2014 IRP. There were 50 instances of the term "reliability." The scope of
7 investments that could fall under that umbrella, and consequently be rolled into a safety
8 tracker, concerns CUB. We quote some of the reliability statements below, and question
9 how closely they are tied to safety.

10 NW Natural

11 1. "To ensure future **reliability**, the Company models a two year phase out of the
12 segmented capacity on NWP from the Company's firm peak resource stack beginning in
13 2017¹⁵". Contract negotiations, termination fees and other costs could be included.

14 2. The Company plans to continue "developing more statistically sophisticated
15 approaches for probabilistically measuring **reliability** risk management. Explore other
16 modeling tools for potentially supplementing SENDOUT®. Develop a database that
17 allows the Company to more effectively analyze reliability risk."¹⁶ All software costs
18 could suddenly be fair game. CUB has seen cost over runs and extremely large software
19 costs historically.¹⁷

¹⁴ UM 1722/Staff/100/Koho/8

¹⁵ 2014 Integrated Resource Plan LC-60 and UG-131473, NW Natural,
https://www.nwnatural.com/uploadedFiles/NW_Natural_2014_IRP.pdf at 1.4.

¹⁶ *Id.* at 1.22

¹⁷ UG 288/ Staff/300/Johnson/3

1 3. "The ability to plan for customer requirement variations while maintaining
2 **reliability** of service is best accomplished by having a variety of supply resources
3 available.¹⁸"

4 4. "NW Natural has evaluated the options for making modifications to the
5 Newport LNG facility that will enhance **reliability**, reduce maintenance cost and extend
6 the operational life expectancy an additional 25-30 years."¹⁹ CUB imagines any
7 investment that could be described to meet peak or capacity on design day could be
8 placed into this category.

9 In addition, in Avista's most recent rate case, Avista made extensive use of the
10 term reliability, using it to buoy the prudence of contested investments such as Ladd
11 Canyon²⁰ and East Medford²¹. CUB strongly objects to a SCRM that is broad and
12 generous enough to include dollar for dollar recovery for reliability investments.

13 **IV. CUB's Response to NWIGU**

14 CUB wholeheartedly agrees with NWIGU's following statement:

15 The primary obligation of the local distribution companies is to safely
16 deliver natural gas within their allocated service territories. There is
17 nothing extraordinary about the obligation to maintain a safe and reliable
18 system²²

19 Additionally, CUB agrees with NWIGU that Oregon has "proactively addressed
20 pipeline safety on LDC systems". The examples span the Joint Utilities with Bare Steel,
21 Cast Iron and Aldyl-A pipeline replacement programs. The mechanisms that provided

¹⁸ 2014 Integrated Resource Plan LC-60 and UG-131473, NW Natural,
https://www.nwnatural.com/uploadedFiles/NW_Natural_2014_IRP.pdf at 1.22, 3.1.

¹⁹ *Id.* at 1.22, 3.19.

²⁰ UG 288/Avista/1500/Webb/19

²¹ UG 288/1500/Webb/8

²² UM 1722/NWIGU/100/Finklea/2

1 recovery for these replacement programs demonstrate that Oregon ratemaking has
2 allowed SCRM's analogous to the Joint Utilities' example of the CCRM implemented by
3 FERC²³. Moreover, CUB feels that the principles asserted here and in CUB's opening
4 testimony are reflective of the FERC policy guidance, cited by the Joint Utilities, as it
5 translates to distribution.

6 CUB also appreciates the examples of planning and recovery methodology, though
7 non-binding, that NWIGU brought forward from Washington. CUB believes that this
8 principled approach is a solid and balanced way to handle costs and programs that are in
9 the interest of safety.

10 **V. Conclusion and Recommendations**

11 CUB recommends that the Commission require the Joint Utilities to include all of
12 their planned safety programs in their IRP or in a Safety Planning Process. CUB feels
13 that it would be appropriate for the Joint Utilities to file this SPP every two years, and file
14 the current DIMP with the Commission every year. This would inform the Commission
15 as to the status of the utilities safety standing and what progress needs to be made, along
16 with potential paths toward that goal. CUB recommends the Commission adopt this
17 approach, regardless of whether an SCRM is at issue.

18 CUB is comfortable recommending limitations on an SCRM including those
19 outlined above, and in our opening testimony. However, demonstration of need and
20 prudence, along with a demonstration of capital management approach and timing
21 requirements are all very important, and should not be presumed. CUB does not

²³ UM 1722/Joint Utilities/100/Thompson-Andrews-Parvinen/7

1 recommend that the Commission adopt a blanket SCRM policy that gives the utility
2 guaranteed recovery for any safety cost, even with the restrictions. CUB recommends
3 that the Commission define attributes of a safety project that are necessary to meet
4 eligibility for an SCRM, but are not necessarily sufficient for guaranteeing recovery, and
5 CUB recommends that those eligibility attributes are in line with the principles outlined
6 above in the content and process recommendations.