

**Mark R. Thompson**  
Manager, Rates and Regulation  
Tel: 503.721-2476  
Fax: 503.721.2516  
email: mark.thompson@nwnatural.com



October 21, 2014

NWN OPUC Advice No. 14-23

***VIA ELECTRONIC FILING***

Public Utility Commission of Oregon  
3930 Fairview Industrial Drive SE  
Post Office Box 1088  
Salem, OR 97308-1088

Attn: Filing Center

Re: Schedule 177, System Integrity Program (SIP) Recovery Mechanism

Northwest Natural Gas Company, dba NW Natural (NW Natural or Company), files the following revisions to its Tariff P.U.C. Or. 25, stated to become effective with service on and after March 1, 2015:

Second Revision of Sheet 177-1  
Schedule 177  
"System Integrity Program (SIP) Recovery Mechanism,"

and

Second Revision of Sheet 177-2  
Schedule 177  
"System Integrity Program (SIP) Recovery Mechanism (continued)."

The purpose of this filing is to maintain, with modifications, the regulatory component of the Company's System Integrity Program. Currently, the Company's program is scheduled to sunset on October 31, 2014.<sup>1</sup> In addition to extending Schedule 177, this filing proposes to refine the parameters for cost recovery.

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<sup>1</sup> See Commission Order No. 12-408.

This filing does not seek to gain Commission approval before the time the Company's current SIP program will sunset. Although this would be ideal from the Company's perspective, NW Natural has not been able to meet and work with Staff and other stakeholders on this topic to the extent we believe would be appropriate to have supported that request. Instead, we make this filing with a requested approval date of March 1, 2015. We hope that by this date, we will have had an opportunity to work with Staff and stakeholders to address any concerns they may have with the requests contained in this filing. We make the filing at this time, before the sunset date of NW Natural's SIP program, because we believe it is important to demonstrate that NW Natural is committed to its System Integrity Program and is interested in avoiding any lapse of it that could be perceived as a lack of commitment to the program construct. NW Natural believes that the program has worked well, and that it should be extended, with certain modifications described further below.

NW Natural notes that the regulatory component of the SIP program consists of the ability to update NW Natural's rate base on an annual basis, to reflect a certain subset of system safety investments. This means that so long as the extension requested in this filing is approved well before the annual update period (the next being November 1, 2015), there will not have been any lapse in the effect of the program.

SIP is comprised of three distinct programs: the Bare Steel Program, Transmission Integrity Management Program (TIMP), and Distribution Integrity Management Program (DIMP). In 2001, the Company initiated its current Bare Steel Program to accelerate the replacement of the Company's bare steel distribution and transmission facilities. In 2002, Congress passed the Pipeline Safety Improvement Act, which required operators to identify transmission lines in "high consequence areas" (HCAs) and to implement written integrity management programs for the HCAs. The Company developed its TIMP to comply with these rules. DIMP was developed in response to the 2006 Pipeline Inspection, Protection, Enforcement and Safety Act.

In 2009, the Company asked the Commission to allow the Company to combine the cost recovery of these three programs under one umbrella program entitled System Integrity Program (SIP). This request was approved in Commission Order No. 09-067. The Commission granted an extension to SIP in Order No. 12-408.

The SIP Recovery Mechanism has allowed the Company to maintain a very safe system. Under SIP, the Company's known bare steel pipeline will be completely replaced by the end of 2015—accelerating a 40-year process to 15 years. Under TIMP, approximately 634 miles of transmission pipeline have been assessed for leaks or other damage. And with the implementation of DIMP, a process is in place for modeling, assessing, and remediating risks to the system—including damage caused by third parties.

Other State Commissions have acknowledged that the SIP Recovery Mechanism has been tremendously helpful in allowing the Company to have a safe system. In 2012, SNL Energy recognized NW Natural as being the gas utility with the lowest ratio of distribution main and service leaks. NW Natural credits the Commission and parties to the 2009 SIP Stipulation (in Docket No. UM 1406) for recognizing the benefits gained through the SIP Recovery Mechanism.

Cost recovery for DIMP and TIMP is set to expire October 31, 2014, and December 31, 2015, for bare steel. The Company is filing to extend SIP at this time because we believe maintaining the continuity is important.

We are recommending that Schedule 177 allow for the recovery of \$8 million of capital costs after the first \$1 million spent for SIP in a Purchased Gas Adjustment (PGA) Year. New Pipeline and Hazardous Materials Safety Administration (PHMSA) regulations are expected to be adopted by 2017, which will put new requirements on the Company. Rather than speculate what those new requirements will be, the Company would like to extend SIP now based on the known costs of DIMP and TIMP, which are ongoing programs. The Company is proposing to extend the revised SIP until the Company and the parties are able to reevaluate the known requirements and costs at that will come with the new PHMSA regulations. The Company expects that at that time, the program will need to be modified to reflect the requirements under those regulations.

Attached is a work paper demonstrating that \$9 million dollars is the expected cost for DIMP and TIMP for the next three PGA Years. This \$9 million is lower than the current program cap of \$12 million, in order to reflect that the Company's bare steel replacement efforts are substantially concluded.

The Company is proposing to forego annually adding \$1 million of SIP spend to rate base to provide a measure of continuity between the new program and the current program, which requires NW Natural to bear regulatory lag on \$4 million of SIP spend. The Company believes that reducing the number from \$4 million to \$1 million is appropriate because the Company's current "run rate" of leakage replacement work is around \$1 million, whereas it was around \$3 million when the SIP program was first adopted. It was this run rate on leakage repair that originally justified the \$3 million of regulatory lag, which was later raised to \$4 million through a negotiation that led to an increase in the amount of bare steel replacement work the Company was allowed to add to rate base.

For you information, we are working to set up stakeholder meetings to discuss NW Natural's proposal with Staff and other parties, and would be happy to keep the Commissioners informed in any way that we can.

Please contact Jennifer Gross at (503) 226-4211, extension 3590, if you have any questions.

Sincerely,

*/s/ Mark R. Thompson*

Mark R. Thompson  
Manager, Rates and Regulation

attachments

# NORTHWEST NATURAL GAS COMPANY

P.U.C. Or. 25

Second Revision to Sheet 177-1  
Cancels First Revision of Sheet 177-1

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## SCHEDULE 177 SYSTEM INTEGRITY PROGRAM (SIP) RECOVERY MECHANISM

### **PURPOSE:**

The purpose of this Schedule is to continue, with modifications, the cost recovery of the Company's System Integrity Program (SIP) as previously approved in OPUC Orders 09-067, 12-408, and 13-179 by identifying adjustments to rates in the applicable Rate Schedules for the annual recovery of costs associated with maintaining a safe and reliable transmission and distribution system.

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### **APPLICABLE:**

The rate adjustments in this Schedule apply to all Sales and Transportation Service Customers served under the following Rate Schedules of this Tariff:

Rate Schedule 2	Rate Schedule 3 Rate Schedule 27	Rate Schedule 31 Rate Schedule 32	Rate Schedule 33
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### **TERM:**

Cost recovery for Part A shall remain in effect for SIP costs incurred through the year 2015. Cost recovery for Parts B and C shall remain in effect for SIP costs until such time as the Commission may order otherwise.

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### **ADJUSTMENT TO RATES:**

All rate adjustments under this Schedule shall be made coincident with the Company's annual Purchased Gas Cost and Technical Rate Adjustment filing.

### **SYSTEM INTEGRITY PROGRAM (SIP):**

The SIP consists of three parts:

**Part A – Bare Steel Replacement Program** – This program was first initiated in 2001 with an estimated completion date of 2021. See OPUC Order No. 01-843 in Docket UM 1030. This date was accelerated to 2015 in OPUC Order No. 13-179.

**Part B – Transmission Integrity Management Program (TIMP)** – This program was initiated in response to the Pipeline Safety Improvement Act of 2002 (“2002 Improvement Act”) and PHMSA Natural Gas Integrity Management Rule. The Initial Accounting Order was approved in Docket UM 1156, OPUC Order No. 04-390.

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**Part C - Distribution Integrity Management Program (DIMP)** – This program was initiated from the Pipeline Inspection, Protection, Enforcement and Safety Act of 2006 (2006 PIPES Act), which expanded requirements for the 2002 Improvement Act to require PHMSA to prescribe minimum standards for DIMP with a focus on damage prevention. The PHMSA rules for DIMP were initiated in 2008.

The three parts described above are integrated to comprise the SIP as adopted by the Commission in Docket UM 1406, OPUC Order No. 09-067.

(continue to Sheet 177-2)

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and after March 1, 2015

**SCHEDULE 177**  
**SYSTEM INTEGRITY PROGRAM (SIP) RECOVERY MECHANISM**  
(continued)

**SIP COST RECOVERY:**

SIP costs that are eligible for cost recovery through this adjustment schedule are:

- 1) Capital costs in excess of the first \$1 million of capital spent on SIP projects in a PGA Year; and
- 2) Not to exceed the soft cap of \$9 million dollars without a specific order of the Commission, and only after consultation with the parties to the 2009 stipulation approved in Commission Order No. 09-067.

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All SIP costs are classified as capital expenditures, and SIP costs will be tracked on a project basis into the respective capital account. The balances in such capital accounts will be used to calculate the SIP cost of service for the relevant year. The SIP cost of service shall be used to calculate permanent adjustments to Base Rates for the respective rate schedules, as follows:

**Part A – Bare Steel Replacement Program** –Seventy percent (70%) of the cumulative investment is allocated to Residential and Commercial Firm Sales and Firm Transportation Customers on an equal cent per therm basis. The remaining thirty percent (30%) is allocated on an equal percent of margin basis to all customer classes. In accordance with Commission Order No. 13-179, the Company will not seek recovery for Bare Steel costs incurred after December 31, 2015.

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**Part B –Transmission Integrity Management Program (TIMP)** –Costs are allocated across all customer classes based on equal percent of margin.

**Part C - Distribution Integrity Management Program (DIMP)** –Costs are allocated across all customer classes based on equal percent of margin.

The cost of service for the SIP investment will include incremental depreciation expense, property tax, return on investment, income taxes, and other costs customarily relating to utility investment. The capital structure and the cost of long-term debt and preferred stock to be used in the calculation of return on rate base will be that adopted by the Commission in the Company’s most recent general rate case.

**ANNUAL REPORTS:**

The Company will file a report with the Commission on or before October 31 of each calendar year detailing SIP costs incurred in the prior PGA Year; and a forecast of SIP costs for the coming twelve (12) month period.

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**GENERAL TERMS:**

This Schedule is governed by the terms of this Schedule, the General Rules and Regulations contained in this Tariff, any other schedules that by their terms or by the terms of this Schedule apply to service under this Schedule, and by all rules and regulations prescribed by regulatory authorities, as amended from time to time.

(continue to Sheet 177-3)

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### 3 Year SIP Extension Forecast

	2015	2016	2017
1 Bare Steel	\$3,040,520	\$0	\$0
2 ASV/RCV	\$708,653	\$708,653	\$708,653
3 Inserted Steel	\$1,250,000	\$1,250,000	\$1,250,000
4 Ineffective Coating	\$1,000,000	\$1,000,000	\$1,000,000
5 Vintage Plastic	\$309,354	\$309,354	\$309,354
6 Natural Forces	\$250,000	\$820,226	\$820,226
7 Build Overs	\$117,317	\$117,317	\$117,317
8 Coastal Risers	\$42,758	\$42,758	\$42,758
9 Risers - Sunshield	\$69,207	\$69,207	\$69,207
<b>10 MAOP Replacements</b>	<b>\$0</b>	<b>\$1,700,000</b>	<b>\$2,400,000</b>
Wynooski MAOP Replacement		\$1,200,000	
Salem By-pass MAOP Replacement			\$250,000
Newberg Trans MAOP Replacement		\$500,000	\$1,300,000
N Coast Trans MAOP Replacement			\$250,000
Beaver Trans MAOP Replacement			\$100,000
<b>11 Future ILI</b>	<b>\$1,926,604</b>	<b>\$2,051,084</b>	<b>\$2,050,000</b>
S. Mist 24" ILI	\$146,764		
Albany/Corvallis ILI			
SP Newsprint ILI			\$250,000
N Coast Wicks Rd. ILI		\$2,051,084	
P20b 6" Dwyer Lumber	\$1,779,840		
P31 McMinnville 6"			\$1,800,000
<b>12 Class 4 Emergency Repsonse</b>	<b>\$100,000</b>	<b>\$250,000</b>	<b>\$500,000</b>
	<b>\$8,814,411</b>	<b>\$8,318,597</b>	<b>\$9,267,513</b>