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April 5, 2006

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VIA ELECTRONIC FILING

PUC Filing Center
Public Utility Commission of Oregon
PO Box 2148
Salem, OR 97308-2148

**Re: Request for Hearing and Response to Staff Recommendation
Docket UM 1244**

I enclose for filing NW Natural's Request for Hearing and Response to Staff Recommendation in the above-referenced proceeding. Since there is no service list for this proceeding, other than our client, no parties were served and no certificate of service is attached.

Very truly yours,

A handwritten signature in cursive script that reads 'Marcus Wood'.

Marcus A. Wood

MW:knp
Enclosure

cc: Elisa Larson, NW Natural
Alex Miller, NW Natural

1 BEFORE THE PUBLIC UTILITY COMMISSION
2 OF OREGON

3 UM 1244

4 In the Matter of NORTHWEST NATURAL
5 GAS COMPANY (d/b/a NW Natural)
6 Application for an Accounting Order

**REQUEST FOR HEARING AND
RESPONSE TO STAFF
RECOMMENDATION**

7 **I. REQUEST FOR HEARING**

8 Pursuant to ORS 757.259(2), Northwest Natural Gas Company (“NW Natural”) requests a hearing on its Application for Deferred Accounting for Revenues and Expenses in this docket UM 1244. Pursuant to ORS 757.259(2), any party is entitled to such hearing upon request.

12 **II. RESPONSE TO STAFF RECOMMENDATION**

13 This docket initially was scheduled for the regular agenda for the Oregon Public Utility Commission’s (the “Commission”) March 23, 2006 public meeting, but then was deferred until the April 11, 2006 public meeting. The Commission staff’s (“Staff”) report for the earlier public meeting recommended denial of NW Natural’s application. Because NW Natural has requested a hearing, to which it is entitled as a matter of right, NW Natural recognizes that Staff might conclude that its recommendation has become moot. However, as a matter of caution, NW Natural submits this brief response.

20 NW Natural filed its application in this docket in order to address what it believes is an unintended consequence of Senate Bill 408 (“SB 408”)—a consequence NW Natural refers to as the “double whammy” effect. That is, if NW Natural realizes a return from Oregon utility service in excess of its allowed return, customers may as a result of such higher earnings be required to pay the utility a surcharge, while if NW Natural is unable to earn its allowed return, the utility may as a result of such lower earnings be required to pay its customers a refund.

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1 NW Natural and other parties are attempting to address this perverse consequence of
2 SB 408 in the ongoing permanent rulemaking process for SB 408. Staff in its memorandum
3 prepared for the March 23 public meeting acknowledged that the double whammy problem
4 “is a legitimate issue.” Because NW Natural does not know whether other approaches
5 considered in the ongoing SB 408 permanent rulemaking proceeding will prove workable
6 and sufficient, it has proposed that the Commission use its deferred accounting authority to
7 maintain just and reasonable rates and avoid the double whammy effect.

8 NW Natural seeks to preserve this application until the Commission has determined
9 how the double whammy effect of SB 408 will be addressed, if at all, in the permanent rules
10 implementing SB 408. The utility would be prejudiced by a dismissal of its application at
11 this time, because according to ORS 757.259(4), the deferral may be authorized “beginning
12 with the date of application.” If the application were dismissed, and the Commission later
13 determined that it should consider the relief here requested, NW Natural might lose the
14 ability to implement the deferral until the date it refiled its application. On the other hand, no
15 party would be prejudiced if the Commission scheduled a hearing on this application after the
16 permanent rulemaking process was completed, because according to ORS 757.259(5),
17 deferred amounts can be allowed in rates only to “the extent authorized by the [C]ommission
18 in a proceeding under ORS 757.210 to change rates and upon review of the utility’s earnings
19 at the time of application to amortize the deferral.”

20 NW Natural respectfully disagrees with Staff’s two objections to its application, but
21 believes that both objections can be heard and resolved more surely when the content of the
22 SB 408 permanent rule is known and after a hearing on the application in this docket. With
23 respect to the objections, NW Natural provides a short initial (albeit incomplete) response:

- 24 1. The requested deferral ties to a single expense item—income tax expense.
25 The double whammy effect will arise only if the ratio of the net revenues from regulated
26 operations of the utility to gross revenues from regulated operations of the utility, as

1 determined by the commission in establishing rates, proves to be incorrect. Such inaccuracy
2 in the net-to-gross revenue ratio in turn would arise from a difference between revenues and
3 expenses as allowed and as paid. This difference between revenue and expenses as allowed
4 and as paid in turn would cause a difference between income tax expense as allowed and as
5 paid. In the absence of the requested deferral account, NW Natural would be required to
6 adjust for the differences between income tax as allowed and paid, but would be denied any
7 related adjustment for the differences between the revenues and expenses as allowed and as
8 paid that caused the income tax difference.

9 The differences between revenues and expenses as allowed and as paid may be
10 deferred, and in a subsequent rate filing, the specific items of difference may be advanced for
11 rate recovery. Under the application, however, NW Natural could defer such differences for
12 recovery only as and to the extent they impact SB 408's rate treatment of a single type of
13 expense—income tax expense. Thus, the deferral captures those specific revenues and
14 expense items tied to changes in income tax expense, and the deferral is permitted under
15 ORS 757.259.

16 2. The requested deferral is not barred by SB 408. SB 408 was designed to
17 address the issue of the reduction in taxes paid by a utility as the result of consolidated tax
18 filings. Nothing in the requested deferral application will affect the application of SB 408 to
19 savings realized from consolidated tax filings.

20 The application does address what NW Natural believes is an unintended
21 consequence of SB 408—the double whammy effect. Not only can NW Natural find no
22 legislative statement that the double whammy effect was intended, but if such were the
23 purpose, the law and the Commission's application thereof would be arbitrary and capricious.
24 Imagine, for example, the difficulty of defending on appeal the following finding of the
25 Commission in a rate order (for a utility with a 40 percent effective income tax rate):

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“For the rate period in question, the Commission found that a fair and reasonable return was 10.5 percent. However, for the most recent rate year, the utility was unable to earn a 10.5 percent return with the rates as authorized and in fact suffered a \$50 million earnings shortfall. The Commission finds that the utility as the result of such earnings shortfall should pay a \$20 million refund to its customers.”

As Staff recognized in its report and recommendation, the Department of Justice memorandum dated December 27, 2005, clearly indicated that rates must be “fair and reasonable” including any SB 408 adjustment. The above result, if permitted by the Commission without some form of offsetting deferred recovery of related utility losses, would not be fair or reasonable. While Staff’s report stated a preference that any determination of whether the impact of SB 408 was fair and reasonable be determined on a case-specific basis, SB 408 does not mandate how the Commission is to carry out its ratemaking obligations in this regard. Moreover, nothing in SB 408 modifies the Commission’s preexisting authority to allow the type of deferred accounting requested here. At hearing, NW Natural would intend to present testimony as to why its requested deferral under ORS 757.259 is within the Commission’s ratemaking authority and is superior to a case-by-case adjudication as a means of preserving fair and reasonable ratemaking.

DATED: April 5, 2006.

STOEL RIVES LLP



Marcus A. Wood

Of Attorneys for Northwest Natural Gas Company