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May 2, 2014

VIA ELECTRONIC FILING & U.S. MAIL

Oregon Public Utility Commission
Attn: Filing Center
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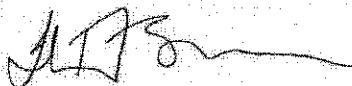
Re: In the Matter of Northwest Natural Gas Company dba NW Natural
Mechanism for Recovery of Environmental Remediation Costs
Docket No. UM 1635

Dear Filing Center:

Enclosed please find the original and five (5) copies of Response Testimony of Michael C. Gorman on behalf of Northwest Industrial Gas Users' in the above-referenced docket.

Thank you for your assistance with this filing. Should you have any questions, please feel free to contact me.

Very truly yours,



Tommy A. Brooks

TAB:sk
Enclosures

cc: UM 1635 Service List

BEFORE THE
PUBLIC UTILITY COMMISSION OF OREGON

In the Matter of)
)
)

NORTHWEST NATURAL GAS)
COMPANY, dba NW NATURAL,)

UM 1635 Phase II

Mechanism for Recovery of)
Environmental Remediation Costs.)
_____)

Response Testimony and Exhibit of

Michael P. Gorman

On behalf of

Northwest Industrial Gas Users

May 2, 2014



BRUBAKER & ASSOCIATES, INC.

BEFORE THE
PUBLIC UTILITY COMMISSION OF OREGON

_____)	
In the Matter of)	
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NORTHWEST NATURAL GAS)	
COMPANY, dba NW NATURAL,)	UM 1635 Phase II
)	
Mechanism for Recovery of)	
Environmental Remediation Costs.)	
_____)	

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BEFORE THE
PUBLIC UTILITY COMMISSION OF OREGON

_____)	
In the Matter of)	
)	
NORTHWEST NATURAL GAS)	
COMPANY, dba NW NATURAL,)	UM 1635 Phase II
)	
Mechanism for Recovery of)	
Environmental Remediation Costs.)	
_____)	

Response Testimony of Michael P. Gorman

1 Q PLEASE STATE YOUR NAME AND BUSINESS ADDRESS.

2 A Michael P. Gorman. My business address is 16690 Swingley Ridge Road, Suite 140,
3 Chesterfield, MO 63017.

4 Q WHAT IS YOUR OCCUPATION?

5 A I am a consultant in the field of public utility regulation and a Managing Principal of
6 Brubaker & Associates, Inc., energy, economic and regulatory consultants.

7 Q PLEASE DESCRIBE YOUR EDUCATIONAL BACKGROUND AND EXPERIENCE.

8 A This information is included in Exhibit NWIGU/101.

9 Q ON WHOSE BEHALF ARE YOU APPEARING IN THIS PROCEEDING?

10 A I am appearing on behalf of the Northwest Industrial Gas Users ("NWIGU"). NWIGU
11 member companies purchase sales and transportation service from Oregon local

1 distribution companies, including Northwest Natural Gas Company (“NW Natural” or
2 “Company”).

3 **Q WHAT IS THE PURPOSE OF YOUR RESPONSE TESTIMONY?**

4 A I will respond to the Company’s proposed allocation of environmental remediation
5 costs (“ERC”), and comment on an earnings test to correspond with this ERC
6 recovery. I will respond to NW Natural’s proposed earnings test. Finally, I will
7 respond to the issues and questions posed by the Public Utility Commission of
8 Oregon (“Commission”) in its UM 1635 Phase II memorandum dated December 5,
9 2013.

10 **Q PLEASE SUMMARIZE YOUR RECOMMENDATIONS AND FINDINGS.**

11 A I will recommend an allocation, recovery mechanism, and proposed earnings test for
12 ERC. My recommendations are as follows:

- 13 1. I recommend ERC costs be allocated between regulated and non-regulated
14 companies of NW Natural.
- 15 2. The regulated jurisdictional and inter-class allocation of ERC should be based on
16 non-gas margin revenue between regulated jurisdictions, and also between retail
17 rate classes.
- 18 3. The specific amount to be recovered from Oregon retail customers will include an
19 estimated annual expenditure to be included in either base rates, or a fixed
20 amount included in the Company’s proposed Site Remediation Recovery
21 Mechanism (“SRRM”). The ERC charge to customers should be fixed between
22 rate cases, and only adjusted during rate cases.
- 23 4. Because of the unique circumstances of ERC cost recovery, a balancing
24 accounting tracking mechanism should be used to track the difference between
25 the amount of ERC cost recovered in customers’ rates, and the allocated portion
26 of ERC cost to be recovered from customers. The amount of customer costs
27 should be offset by all insurance settlement proceeds, and the revenue
28 requirement of excess earnings should be credited against ERC costs included in
29 the tracking account.
- 30 5. In each rate case, an annual amortization expense to be included in customers’
31 rates should be established based on an amortization of the balance in the ERC

- 1 tracking account, and the average annual cost expected to be incurred over the
2 next five years. This methodology ensures that the Company will fully recover its
3 ERC allocated to customers while also ensuring customers' rates will be stable
4 and manageable during the period ERC costs are included in retail rates.
- 5 6. The equal percent of margin spread approved in the parties' earlier settlement for
6 allocating the ERC customer classes is acceptable, if no party objects to the
7 proposed allocation in that settlement. However, NWIGU will assert its original
8 position if the settlement allocation is reopened in this case.
- 9 7. Although NWIGU is not aware of any party seeking to re-open this issue, in the
10 event the spread of ERC costs across customer classes is opened again in this
11 case, then NWIGU advocates its principles in support of a most reasonable
12 allocation of ERC costs. NWIGU is concerned with the limited access made to
13 move rates closer to cost of service, and believes that every opportunity available
14 should be used to move rates closer to cost. Cost-based rates provide more
15 accurate price signals to customers, and encourages them to modify consumption
16 decisions to efficiently utilize delivery system assets. Toward this objective, and if
17 the rate spread issue is reopened, I recommend that ERC revenue requirement
18 will be allocated across customer classes based on a consideration of the
19 following:
- 20 a. Customer classes that are currently priced above NW Natural's cost of
21 providing service should not receive an allocated portion of ERC costs.
- 22 b. For those classes that are currently priced below cost of service, the ERC will
23 be allocated between the below-cost classes using an equal percent of
24 non-gas margin allocator.
- 25 8. Insurance settlement proceeds will be allocated entirely to the benefit of retail
26 customers.
- 27 9. I recommend historical ERC costs be allocated to non-regulated jurisdiction,
28 regulated jurisdictions, and shareholders assume a share of those costs allocated
29 to regulated operations. In the event the Commission does not accept this cost
30 responsibility allocation, then I recommend the structured use of insurance
31 company proceeds to offset historical deferred ERC costs, and insurance
32 proceeds to offset the amount of costs going forward. This methodology will
33 mitigate the cost on generations of customers, and better assure a burden on all
34 generations of customers caused by ERC costs allocated to customers. From
35 this standpoint, I recommend approximately one-third of insurance company
36 proceeds be used to credit historical ERC balances, and two-thirds be retained in
37 a tracking account to offset future ERC costs.

1 Q DO YOU BELIEVE ERC COST JUSTIFIES THE EXTRAORDINARY RATE
2 TREATMENT OF A BALANCING ACCOUNT?

3 A Yes. I believe a balancing account can be used to stabilize the rates to customers to
4 provide full recovery of their allocated share of ERC, while assuring the ratepayer
5 allocated amount is completely offset by insurance company settlement proceeds,
6 and contributions of excess earnings (revenue equivalent) to the full amount of ERCs
7 that are allocated to retail customers. This mechanism is appropriate in this case
8 because it will mitigate rate volatility to retail customers, while providing NW Natural
9 with ERC recovery. I am recommending this mechanism only because of the
10 extraordinary uncertainty of future annual ERC costs, and the need to stabilize rate
11 impacts on retail customers caused by uncertain and material ERC over the next
12 decade or longer.

13 ERC Recovery Mechanism and Earnings Test

14 Q ARE YOU PROPOSING AN ERC RECOVERY METHODOLOGY AND EARNINGS
15 TEST BE USED IN CONJUNCTION WITH NW NATURAL'S RECOVERY OF ERC
16 THROUGH THE PROPOSED SRRM?

17 A Yes. I propose the following recovery methodology and earnings test be used to
18 provide recovery of future ERC through base rates and/or an SRRM.

19 I recommend the Company allocate ERC costs across non-regulated and
20 regulated business functions on the basis of regulated versus non-regulated
21 Company assets. In the Company's 2013 Annual Report, it lists total Company
22 assets of \$2.97 billion. Of this amount, \$2.64 billion are related to regulated utility
23 operations. As such, 11% of ERC costs should be allocated to non-regulated
24 companies, and 89% should be allocated to regulated operations. Further, these

1 regulated operations should use a base rate revenue, or margin basis, to allocate
2 ERC between customer classes. Finally, the amount allocated to retail regulated
3 operations, should be shared between the Company and its shareholders based on a
4 direct allocation of 90% to customers, and 10% to the Company. However, the
5 application of an earnings test, as described below, will provide the Company an
6 opportunity to produce savings to offset its allocated portion of ERC costs.

7 I propose an ERC retail recovery mechanism that recognizes the uncertain
8 annual ERC expenditures, the need for a prudency review, and the need to fully
9 offset the ratepayer's allocated amount of ERC by insurance settlement proceeds,
10 and excess earnings.

11 Based on these objectives, I propose an annual base rate recovery
12 mechanism, with an accounting deferral balancing account tracking mechanism.
13 Insurance company proceeds, and excess earnings credits (revenue equivalent), will
14 be tracked in the balancing mechanism to mitigate ERC charges on customers.

15 The structure of the ERC recovery mechanism is described as follows:

- 16 1. An annual ERC amortization expense to be built into base rates. NW Natural will
17 project its ERC expenditures over the next five years, and approximate an
18 average annual expenditure. Ninety percent of this expenditure will be included in
19 the annual amortization expense allocation to customers. Next, NW Natural will
20 review the amount of deferred ERC in its tracking accounting balance. This
21 accounting balance will be amortized over a period to mitigate rate impacts on
22 customers, but target it to be approximately five years. If this accounting tracker
23 has a negative balance, the negative credit will be used to offset the expenditure
24 recovered in rates over the next five years.
- 25 2. The annual amount of ERC amortization expense will be recovered from
26 customers in either base rates or in the SRRM. The amount will be fixed in
27 between rate cases.
- 28 3. The Company will use deferral accounting to track the amount of ERC revenue
29 collections, and its actual ERC expenditures incurred each year. The difference
30 between ERC annual collections and the customer allocated share of actual ERC
31 for the year will be added to or subtracted from the ERC balancing account.

- 1 4. The ERC balancing account will be a regulatory asset/liability account that tracks
2 the ongoing ERC rate recovery with ERC actual incurrence, insurance proceeds,
3 and earnings test contributions. A carrying charge rate equal to the five-year
4 Treasury bill rate should be applied to the deferral balance each year.
- 5 5. The ERC annual cost will be spread on an equal percent of margin as outlined in
6 the parties' earlier settlement, which is one of the areas of the settlement the
7 Commission indicated it did not have issues with. However, if that settlement
8 method is not agreeable to all parties or the Commission, then the ERC annual
9 cost should be spread over rate classes as follows: For customer classes that are
10 already priced above cost of service, no increase in rates would be permitted for
11 ERC. For such classes, ERC will be spread amongst customer classes, but
12 limited on base rate revenue and with the allocation limited to only those customer
13 classes which are currently priced below cost of service. No customer class will
14 receive an increase in rates if their current rate charges exceed NW Natural's cost
15 of providing service. The allocation factor used for customers that are currently
16 priced below NW Natural's cost of service will be based on a net base rate
17 revenue, or net margin basis, or "equal percent of margin."
- 18 6. The current net balance of insurance settlement proceeds, and earnings test
19 contribution will be credited to ERC annual cost recovery amount, and any future
20 insurance proceeds will be credited to the ERC balancing account.¹

21 **Q PLEASE DESCRIBE THE EARNINGS TEST YOU PROPOSE TO IMPLEMENT AS**
22 **PART OF YOUR ERC RECOVERY MECHANISM.**

23 **A An earnings test will be used to credit the ERC balancing account for excess earnings**
24 **that will be used to reduce the ERC to be recovered from customers. An earnings**
25 **test will be implemented as follows:**

- 26 1. No earnings sharings if the Company's actual earned return on equity is less than
27 or equal to its authorized return on equity. NW Natural's ability to increase its
28 earnings to equal its authorized return on equity will allow it to produce cost
29 savings that offset its allocated share of ERCs that are not included in retail rates,
30 but are allocated to retail operations as investors' obligation.
- 31 2. If the Company's earned return on equity is up to 50 basis points greater than its
32 authorized return on equity, then: 80% of the difference between the authorized

¹If the Commission rejects my proposal to allocate ERC costs between non-regulated companies, regulated operations, and shareholders, then I recommend a more structured use of insurance company proceeds to mitigate ERC costs on various generations of customers. As outlined below, this entails using one-third of insurance proceeds to credit against historical deferred ERC costs, and using two-thirds of insurance proceeds as credit to future ERC costs. Using the insurance proceeds in this manner will mitigate the impact on generations of customers.

1 return on equity, and earned return on equity (revenue equivalent) will be credited
2 to the ERC balancing account.

3 3. If the Company's earned return on equity is greater than 50 basis points above
4 the authorized return on equity, then:

5 a. 80% of the earnings between authorized return on equity and 50 basis points
6 above the authorized return on equity would be credited to the balancing
7 account, and

8 b. 50% of the earnings in excess of 50 basis points above the authorized return
9 on equity up to the actual return on equity will be credited to the ERC
10 balancing account.

11 The revenue requirement equivalent of excess earnings will be credited to
12 the ERC deferred account balance. The expenditures in the ERC balance will
13 also be stated on a revenue requirement basis. This allows the tracking of excess
14 revenues (based on excess earnings), and the revenue requirement of ERC costs
15 to be tracked on an equivalent pre-tax basis.

16 **Q PLEASE EXPLAIN WHY YOUR PROPOSED RECOVERY MECHANISM AND**
17 **EARNINGS TEST SHOULD BE ADOPTED IN THIS PROCEEDING.**

18 **A** My proposed recovery mechanism and earnings test accomplishes the following
19 objectives:

- 20 1. The amount of ERC will be shared via the implementation of an earnings test.
- 21 2. Annual amortization of environmental remediation expense, coupled with a
22 balancing account, will stabilize rate recovery and provide an opportunity for NW
23 Natural to receive full recovery of ERC.
- 24 3. Requiring an earnings test when earned return above the authorized return on
25 equity is realized, will accelerate the recovery of environmental remediation
26 expense and reduce the Company's exposure or risk of ERC recovery.
- 27 4. I recommend a tiered sharing concept for actual excess earnings, with the
28 Company sharing more when its overearnings are closer to authorized return,
29 because it is more difficult to increase earnings by more than 50 basis points
30 above the authorized return than it is to increase the earned return up to 50 basis
31 points above the authorized return.

1 A lower customer/shareholder sharing amount for earnings above 50 basis points
2 in excess of the authorized return on equity is fair, because management must
3 achieve larger and likely more difficult cost reductions to realize the higher level of
4 earned return. Also, it is less likely that management can achieve higher levels of
5 actual earned return on equity. Therefore, if exceptional management efforts are
6 achieved, then NW Natural should retain a larger share of excess earnings for
7 investors.

8 **Response to the Company's Proposed Earnings Test**

9 **Q DID THE COMPANY PROPOSE AN EARNINGS TEST IN THIS PROCEEDING?**

10 A Yes. Company witness Alex Miller described an earnings test which will allow the
11 Company to retain all earnings up to 100 basis points above its authorized return on
12 equity. (NWN/800/11). He argues this is appropriate, because over time the utility
13 sometimes earns less than or more than its authorized return on equity, therefore
14 excess earnings contribution to ERC should be limited to only a very high level of
15 earnings. He opines that this will give the Company an opportunity to earn its
16 authorized return on equity on average over time.

17 **Q DO YOU BELIEVE THE COMPANY'S PROPOSED EARNINGS TEST IS**
18 **REASONABLE?**

19 A No. The Company's proposed earnings test does not reflect the extraordinary nature,
20 and the material amount of the ERC costs. These ERC costs are not a cost of
21 providing service to retail customers. Hence, customers are being asked to pay rates
22 that are higher than necessary to fully recover NW Natural's cost of providing service.
23 This represents a material burden on customers to provide NW Natural recovery of
24 ERC.

25 This extraordinary burden on customers should be balanced by placing a
26 comparable burden on NW Natural's investors. As such, an earnings test that

1 provides NW Natural an opportunity to earn its authorized return plus 100 basis
2 points fails to produce a balanced burden of ERC on customers and investors.

3 The Company's proposal for 100 basis points over the base return on equity is
4 simply unreasonable for several reasons. First, a 100 basis point premium over the
5 authorized returns on equity would be an indication that NW Natural's rates are
6 excessive and should be reduced. If instead of reducing the rates, NW Natural was
7 allowed to use the excess revenues reflecting those excess earnings to pay ERC
8 costs, then customers would be forgoing a rate decrease in exchange for allowing
9 NW Natural to recover additional ERC costs. Either way, customers are paying the
10 full ERC, and the Company incurs no burden.

11 Second, a 100 basis point range is simply too wide to create a reasonable
12 balance and burden on customers and shareholders. Typically, a return on equity is
13 estimated within a 100 basis point range. Authorized returns on equity are typically
14 set at the midpoint of the estimated range. Often, the recommended return on equity
15 range is less than 100 basis points. Under the Company's proposal, it would be
16 allowed to retain earnings in excess of the highest estimate of their current market
17 cost of equity if 100 basis point premium over the authorized return on equity were
18 approved. Even if the Company is not asked to accept some non-traditional cost
19 exposure for these extraordinary cost items, the Company's 100 basis point spread is
20 simply imbalanced.

21 A more reasonable spread would be 50 basis points, which would assume
22 about 100 basis point spread between the high and low return on equity estimated
23 range.

1 **Allocation of ERC**

2 **Q SHOULD ERC COSTS BE ALLOCATED TO CUSTOMER CLASSES, AND**
3 **INCREASE THEIR RATES, IF THOSE CUSTOMERS ARE ALREADY PAYING**
4 **RATES THAT EXCEED NW NATURAL'S COST OF PROVIDING SERVICE?**

5 A No. First, let me reiterate that the equal percent of margin spread approved in the
6 parties' earlier settlement for allocating the ERC customer classes is acceptable to
7 NWIGU if no party objects to the proposed allocation in that settlement. However, if
8 other parties or the Commission do not continue to support that portion of the
9 settlement, the spread should be based on the following principle: to the extent
10 customer rates exceed NW Natural's cost of providing service, and customers are
11 paying rates that subsidize the cost of service to other rate classes, then the
12 Commission should restrict ERC allocations to only customer classes whose rates do
13 not fully recover NW Natural's cost of service.

14 As such, if customer classes' rates provide revenue that exceeds the class
15 allocated cost of service, then those customers' rates should not be increased to
16 recover ERCs. Instead, ERCs should be allocated to all other classes whose rates
17 do not fully recover NW Natural's cost of service. This process would reduce the
18 amount of subsidy between rate classes, and create a balanced and fair allocation of
19 ERCs between customer classes.

20 **Q HOW DO YOU PROPOSE TO ALLOCATE ERC COSTS BETWEEN CUSTOMER**
21 **CLASSES IF THE RATES ARE NOT FULLY RECOVERING NW NATURAL'S**
22 **COST OF SERVICE?**

23 A If the earlier settlement or rate spread is re-opened, I recommend the ERC costs be
24 allocated amongst only the rate classes whose rates are not recovering NW Natural's

1 cost of service by using a net margin or non-gas cost base rate allocation to those
2 classes. This will move those classes' rates closer to cost of service, and maintain
3 NW Natural's ability to recover the ERC allocated to retail customers.

4 **Q IS THERE ANY DIRECT COST CAUSATION OF ENVIRONMENTAL**
5 **REMEDATION IN CURRENT CUSTOMERS' COST OF SERVICE?**

6 A No. These ERCs were incurred in the past, and are unrelated to the cost of providing
7 utility service to current customers. Also, current customers have not received any
8 benefit from the actions which caused the ERC to be incurred. Therefore, there is no
9 cost causation basis between ERC and the Company's cost of providing service to
10 current customers.

11 The allocation of the ERC on a net margin basis is balanced and fair because
12 all customers pay an economically comparable share of the ERC based on NW
13 Natural's manageable cost of providing gas delivery service to all customers. Gas
14 cost is a flow-through expense and is not a cost which NW Natural's management
15 can manage to enhance its earnings. Earnings management is based on margin
16 revenue and costs. Because NW Natural's cost of non-gas delivery service
17 represents the costs which it can manage and use to produce excess earnings to
18 offset ERC, it is a reasonable basis to allocate ERC amongst customer classes.

19 **Q WHY DO YOU BELIEVE THAT THE PROPOSED RECOVERY OF THE ERC IS**
20 **REASONABLE?**

21 A The Commission has already stated that it will accept a net margin or base rate
22 allocation of ERC across customer classes. (UM 1635 Phase II Memorandum at 1).
23 Further, the Commission has found that an earnings test should be made in

1 conjunction with cost recovery of environmental remediation expenses. NW Natural
2 recovers rate revenue that supports its actual earnings through margin charges to
3 customer classes. NW Natural's ability to manage cost to produce excess earnings
4 that are available for an earnings test is caused by its ability to manage net margin
5 and related costs.

6 NW Natural's non-gas base rate revenue provides a consistent and fair
7 allocation of the ERC to customer classes.

8 Response to Commission Questions

9 **Q DID THE COMMISSION POSE QUESTIONS RELATED TO RECOVERY OF PAST**
10 **EXPENDITURES?**

11 A Yes. As outlined in the Commission's December 5, 2013 Phase II memorandum,² it
12 posed the following questions:

13 Expenditures before December 31, 2012 (Past Expenditures)

14 In Phase II, parties will be directed to address the following issues and
15 cite to Commission and any other applicable authority:

- 16 • What policy considerations should guide the Commission's
17 adoption of an earnings test mechanism for past expenditures?
- 18 • Should the mechanism consider past earnings and expenditures
19 on an annual or aggregate basis? Why or why not?
- 20 • Should revenue gains or losses from the WACOG incentive
21 sharing mechanism be included in earning for purposes of
22 conducting the earnings test? Why or why not?
- 23 • Should the mechanism include a deadband? Why or why not? If
24 the mechanism should include a deadband, what should be the
25 range of the deadband? Why?
- 26 • How should the Commission determine what constitute reasonable
27 earnings for the utility's historical period? Should the Commission
28 allow recovery of environmental remediation expenses to bring

²UM 1635 Phase II Prehearing conference memorandum issued December 5, 2013.

1 earnings up to the bottom of the deadband range, to the authorized
2 return on equity, or to the top of the deadband range? Why?

- 3
- How should the mechanism address insurance proceeds?

4 **Past ERC Expenditures**

5 **Q IS IT YOUR UNDERSTANDING THE COMPANY HAS FULLY RECOVERED ALL**
6 **PAST ERC THROUGH INSURANCE COMPANY PROCEEDS?**

7 A Yes. NW Natural witness Miller stated that it recovered \$150.5 million from insurance
8 companies which more than offset the deferred cost balance set for recovery from
9 customers. Previous deferred ERC balances should be allocated to non-regulated
10 operations, to investors, and retail customers. If my allocation proposal is adopted,
11 11% of the ERC costs would be allocated to non-regulated operations, 10% to
12 investors, and approximately 79% to retail customers. Of the approximate
13 \$97.6 million of environmental costs previously incurred (multi-party rate settlement at
14 page 4), this would allocate that cost \$10.7 million to non-regulated companies,
15 \$8.7 million to investors, and \$78.2 million to retail customers. Approximately 52% of
16 the insurance company proceeds will be used to pay off this historical deferred ERC.
17 The remaining 48% of insurance proceeds would be left available to cover the cost of
18 future ERC collections.

19 However, if the Commission rejects my proposed allocation between
20 non-regulated, investor, and retail customer allocation of ERC costs, I recommend
21 approximately one-third or \$50 million of the insurance proceeds be credited against
22 historical deferred ERC costs, and \$100 million be left available to credit future ERC
23 collections. Again, this mitigates the impact on all generation of customers for ERC
24 charges.

1 **Forward-Looking Mechanism**

2 **Q DID THE COMMISSION POSE CERTAIN QUESTIONS RELATED TO A**
3 **FORWARD-LOOKING EXPENDITURE MECHANISM?**

4 **A** Yes. the Commission posed the following questions:³

5 Forward-Looking Mechanism (expenditures after December 31, 2012)

6 In Phase II, parties will be directed to address the following issues and
7 cite to Commission and any other applicable authority:

- 8 • Should the Commission provide an incentive for NW Natural to
9 minimize environmental remediation costs and pursue insurance
10 remedies? Why or why not? If we should provide such an
11 incentive, how should we provide it? Why?
- 12 • What policy considerations should guide the Commission's
13 adoption of an earnings test mechanism for expenditures after
14 December 31, 2012? Why?
- 15 • How should the Commission address such issues as the inclusion
16 or not of WACOG earnings in earnings calculations, average
17 versus aggregate earnings tests, treatment of insurance proceeds,
18 earnings deadbands, and all other factors relevant to the design of
19 the earnings test? Why?

20 **Q DO YOU BELIEVE THE COMMISSION SHOULD PROVIDE AN INCENTIVE FOR**
21 **NW NATURAL TO MINIMIZE ERC AND PURSUE ANY REMAINING INSURANCE**
22 **RECOVERIES?**

23 **A** Yes. NW Natural and all utilities should always have a strong incentive to minimize
24 cost and lower rates to retail customers. NW Natural can minimize ERC collection by
25 efforts to reduce ERC expenditures. The financial obligations under any remaining
26 insurance policies should be pursued in order to minimize the Company's and
27 customers' cost of ERC.

³*Id.*

1 Further, because ERC costs are not related to the provisions of current
2 service, and represent a significant obligation to NW Natural, it is in the best interest
3 of all stakeholders to pursue all opportunities to mitigate the financial effect of ERCs
4 on all stakeholders.

5 Under an earnings test, NW Natural may be asked to forgo an opportunity to
6 earn more than its authorized return on equity, but the excess earnings will be used
7 to contribute to the ERC recovery. This will mitigate NW Natural's financial exposure,
8 and strengthen its financial position. Also, while it may forgo earnings in excess of its
9 authorized return on equity, it will retain the cash flows produced by these excess
10 earnings which will be used to pay down ERCs.

11 Similarly, customers forgo an opportunity to argue for rate decreases in the
12 event of excess earnings, but benefit if the excess earnings are used to mitigate their
13 exposure to ERC charges. Also, customers will be burdened by rates above NW
14 Natural's cost of service while ERCs are charged to customers. Investors should also
15 assume an ERC cost burden.

16 There is a balance between customers and shareholders for using excess
17 earnings to offset ERC costs. The Company forgoes excess earnings but retains the
18 cash flows realized by the excess earning and uses it to strengthen its financial
19 position, and lower its financial risk.

20 **Q WHAT POLICY DO YOU RECOMMEND THE COMMISSION CONSIDER IN**
21 **ADOPTING AN EARNINGS TEST?**

22 **A** I recommend the Commission observe the mutual benefits of accelerating the
23 recovery of ERCs. Again, ERCs represent a significant financial obligation of the
24 Company, and eliminating that obligation (through full cost recovery) will mitigate its

1 financial exposure and reduce its financial risk. At the same time, these costs are
2 unrelated to provisions of current utility service, so asking customers to assume full
3 ERC responsibility is not a balanced regulatory treatment.

4 Providing a sharing mechanism allows the Company to offset additional cost
5 recovery through exemplary management performance, which benefits shareholders.
6 An earnings test which targets excess earnings to help mitigate the ERC financial
7 obligation creates benefits to both customers and shareholders.

8 **Q HOW SHOULD THE COMMISSION INCLUDE THE WACOG IN THE EARNINGS**
9 **TEST CALCULATION?**

10 A All excess earnings produced by NW Natural should be used to credit the amount of
11 ERCs allocated to retail customers. These credits should be adjusted for the revenue
12 requirement value of the excess earnings, and used to completely offset ERC cost
13 included in the ERC tracking balance.

14 **Inclusion in Rates**

15 **Q DID THE COMMISSION ALSO POSE QUESTIONS CONCERNING INCLUSION IN**
16 **RATES?**

17 A Yes. The Commission also offered the following questions:⁴

18 **Inclusion in Rates**

19 In Phase II, parties will be directed to address the following issues and
20 cite to Commission and any other applicable authority:

- 21 • Should the Commission continue to defer all environmental
22 remediation expenses, or place a certain amount in rates each
23 year on a forward-looking basis without subjecting that amount to
24 deferral? Why?

⁴*Id.*

- 1 • If the Commission should place a certain amount of expenses in
2 rates each year without subjecting that amount to deferral, what
3 should the amount be or what process should the Commission use
4 to determine that amount?

5 **Q PLEASE RESPOND TO THE COMMISSION'S QUESTIONS LISTED ABOVE.**

6 A As outlined above, I recommend a methodology that provides expedited and efficient
7 opportunities for recovery of ERCs. This includes a level annual recovery amount
8 with a tracker balancing account.

9 A level annual recovery amount will provide rate stability to customers, and
10 the tracker balancing account provides NW Natural assurance of recovering ERC
11 allocated to customers.

12 This annual recovery in conjunction with an earnings test provides NW Natural
13 opportunities for accelerated ERC recovery. Insurance settlements should be
14 credited against the ERC cost in the balancing account, whether past recoveries or
15 future recoveries. To the greatest extent possible, insurance recoveries should be
16 used to eliminate the ERC liability of the Company and ERC rate exposure to
17 customers.

18 **Q SHOULD THE COMMISSION DETERMINE WHAT CONSTITUTES REASONABLE**
19 **EARNINGS FOR THE UTILITY'S HISTORICAL PERIOD?**

20 A Yes. I believe the authorized return on equity on jurisdictional operations can be
21 used as a reasonable earnings threshold for constructing an earnings test.

22 Because customers are asked to pay rates higher than NW Natural's cost of
23 providing service, it is appropriate to ask NW Natural's shareholders to forgo
24 opportunities for excess earnings. This process creates burdens on both customers
25 and shareholders for full recovery of ERC cost. The Company's last authorized return

1 on equity is reasonable in establishing this level of earnings threshold to establish
2 when earnings can be considered as "excess" earnings.

3 **Q DOES THIS CONCLUDE YOUR RESPONSE TESTIMONY?**

4 **A** Yes, it does.

BEFORE THE

PUBLIC UTILITY COMMISSION OF OREGON

_____)	
In the Matter of)	
)	
NORTHWEST NATURAL GAS)	
COMPANY, dba NW NATURAL,)	UM 1635 Phase II
)	
Mechanism for Recovery of)	
Environmental Remediation Costs.)	
_____)	

Exhibit NWIGU/101

Qualifications of Michael P. Gorman

May 2, 2014

1

Qualifications of Michael P. Gorman

2 **Q PLEASE STATE YOUR NAME AND BUSINESS ADDRESS.**

3 A Michael P. Gorman. My business address is 16690 Swingley Ridge Road, Suite 140,
4 Chesterfield, MO 63017.

5 **Q PLEASE STATE YOUR OCCUPATION.**

6 A I am a consultant in the field of public utility regulation and a Managing Principal with
7 Brubaker & Associates, Inc. ("BAI"), energy, economic and regulatory consultants.

8 **Q PLEASE SUMMARIZE YOUR EDUCATIONAL BACKGROUND AND WORK
9 EXPERIENCE.**

10 A In 1983 I received a Bachelors of Science Degree in Electrical Engineering from
11 Southern Illinois University, and in 1986, I received a Masters Degree in Business
12 Administration with a concentration in Finance from the University of Illinois at
13 Springfield. I have also completed several graduate level economics courses.

14 In August of 1983, I accepted an analyst position with the Illinois Commerce
15 Commission ("ICC"). In this position, I performed a variety of analyses for both formal
16 and informal investigations before the ICC, including: marginal cost of energy, central
17 dispatch, avoided cost of energy, annual system production costs, and working
18 capital. In October of 1986, I was promoted to the position of Senior Analyst. In this
19 position, I assumed the additional responsibilities of technical leader on projects, and
20 my areas of responsibility were expanded to include utility financial modeling and
21 financial analyses.

22 In 1987, I was promoted to Director of the Financial Analysis Department. In
23 this position, I was responsible for all financial analyses conducted by the Staff.

1 Among other things, I conducted analyses and sponsored testimony before the ICC
2 on rate of return, financial integrity, financial modeling and related issues. I also
3 supervised the development of all Staff analyses and testimony on these same
4 issues. In addition, I supervised the Staff's review and recommendations to the
5 Commission concerning utility plans to issue debt and equity securities.

6 In August of 1989, I accepted a position with Merrill-Lynch as a financial
7 consultant. After receiving all required securities licenses, I worked with individual
8 investors and small businesses in evaluating and selecting investments suitable to
9 their requirements.

10 In September of 1990, I accepted a position with Drazen-Brubaker &
11 Associates, Inc. ("DBA"). In April 1995, the firm of Brubaker & Associates, Inc. was
12 formed. It includes most of the former DBA principals and Staff. Since 1990, I have
13 performed various analyses and sponsored testimony on cost of capital, cost/benefits
14 of utility mergers and acquisitions, utility reorganizations, level of operating expenses
15 and rate base, cost of service studies, and analyses relating to industrial jobs and
16 economic development. I also participated in a study used to revise the financial
17 policy for the municipal utility in Kansas City, Kansas.

18 At BAI, I also have extensive experience working with large energy users to
19 distribute and critically evaluate responses to requests for proposals ("RFPs") for
20 electric, steam, and gas energy supply from competitive energy suppliers. These
21 analyses include the evaluation of gas supply and delivery charges, cogeneration
22 and/or combined cycle unit feasibility studies, and the evaluation of third-party
23 asset/supply management agreements. I have participated in rate cases on rate
24 design and class cost of service for electric, natural gas, water and wastewater
25 utilities. I have also analyzed commodity pricing indices and forward pricing methods

1 for third party supply agreements, and have also conducted regional electric market
2 price forecasts.

3 In addition to our main office in St. Louis, the firm also has branch offices in
4 Phoenix, Arizona and Corpus Christi, Texas.

5 **Q HAVE YOU EVER TESTIFIED BEFORE A REGULATORY BODY?**

6 A Yes. I have sponsored testimony on cost of capital, revenue requirements, cost of
7 service and other issues before the Federal Energy Regulatory Commission and
8 numerous state regulatory commissions including: Arkansas, Arizona, California,
9 Colorado, Delaware, Florida, Georgia, Idaho, Illinois, Indiana, Iowa, Kansas,
10 Louisiana, Michigan, Missouri, Montana, New Jersey, New Mexico, New York, North
11 Carolina, Ohio, Oklahoma, Oregon, South Carolina, Tennessee, Texas, Utah,
12 Vermont, Virginia, Washington, West Virginia, Wisconsin, Wyoming, and before the
13 provincial regulatory boards in Alberta and Nova Scotia, Canada. I have also spon-
14 sored testimony before the Board of Public Utilities in Kansas City, Kansas;
15 presented rate setting position reports to the regulatory board of the municipal utility
16 in Austin, Texas, and Salt River Project, Arizona, on behalf of industrial customers;
17 and negotiated rate disputes for industrial customers of the Municipal Electric
18 Authority of Georgia in the LaGrange, Georgia district.

19 **Q PLEASE DESCRIBE ANY PROFESSIONAL REGISTRATIONS OR**
20 **ORGANIZATIONS TO WHICH YOU BELONG.**

21 A I earned the designation of Chartered Financial Analyst ("CFA") from the CFA
22 Institute. The CFA charter was awarded after successfully completing three
23 examinations which covered the subject areas of financial accounting, economics,

1 fixed income and equity valuation and professional and ethical conduct. I am a
2 member of the CFA Institute's Financial Analyst Society.

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CERTIFICATE OF SERVICE
Docket No. UM 1635

I CERTIFY that I have on this day served the foregoing document upon all parties of record in this proceeding via electronic mail and/or by mailing a copy properly addressed with first class postage prepaid.

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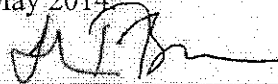
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Dated in Portland, Oregon, this 2nd day of May 2014



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