

BEFORE THE PUBLIC UTILITY COMMISSION

OF OREGON

UM 1744

In the Matter of

NORTHWEST NATURAL GAS
COMPANY dba NW NATURAL,

Application for Approval of an Emission
Reduction Program

NORTHWEST INDUSTRIAL GAS
USERS' PREHEARING BRIEF

Pursuant to the Administrative Law Judge's Ruling in this matter dated October 20, 2015, Northwest Industrial Gas Users ("NWIGU") submits this Prehearing Brief in advance of the hearing currently scheduled for November 19, 2015. The purpose of this memorandum is to summarize NWIGU's testimony and positions taken in this matter at this time. NWIGU reserves the right to make additional arguments at hearing and in post hearing briefs.

I. INTRODUCTION

NWIGU participated both before the Legislature during its consideration of Senate Bill 844 ("SB 844") and before the Public Utility Commission ("Commission") when it promulgated the rules implementing SB 844. While NWIGU supports the broad policies contained in the legislation and in the rule allowing for voluntary programs to reduce carbon emissions, NWIGU remains committed to ensuring programs implementing SB 844 promote a least-cost approach that results in actual carbon savings and that incentives awarded to customers and the Company (which are paid for by existing ratepayers) are no more than is necessary to create a successful program.

From a broad perspective, the combined heat and power (“CHP”) program proposed by Northwest Natural (“NW Natural” or the “Company”) in this docket appears consistent with the intent of SB 844. By enacting SB 844, the Legislature appropriately recognized that natural gas can be used to reduce carbon dioxide emissions by transitioning some customers from reliance on traditional electric service to generating their own electricity from natural gas. Northwest Natural’s proposal provides incentives for customers to make that transition.

Northwest Natural’s proposal, however, is not perfect, and the existing record makes it clear that there is room for improvement in the proposal to reduce the program’s costs and to better protect ratepayers from unnecessary risks and incentives. For these reasons, the Commission should approve Northwest Natural’s proposal, but with modifications informed by the testimony of NWIGU and other parties.

II. NWIGU’S TESTIMONY AND POSITIONS

A. Company Incentive

Northwest Natural’s filing includes an incentive to the Company in the amount of \$10 per metric ton of reduced carbon. While that level of incentive may be appropriate in other contexts, NWIGU opposes such a high incentive for the CHP program. NWIGU has proposed instead that the Commission approve a company incentive that is no higher than \$5 per metric ton of reduced carbon.

Northwest Natural has presented the \$10 per metric ton incentive as an appropriate “baseline” or “default” amount for all SB 844 projects. The Company observes that the \$10 per metric ton incentive is approximately 25% of the total program cost and, therefore, close to the maximum incentive allowed by the SB 844 rules. The Company further observes that a CHP program is likely to be the cheapest SB 844 program and, therefore, that \$10 per metric ton will

be a smaller percentage of future (more expensive) programs. This mathematic approach to calculating the Company's incentive is too rigid and seeks to convert the maximum incentive *allowed by* the rule into an entitlement *required by* the rule. To the contrary, neither the statute nor the rule requires that a company receive any incentive as part of a program, and the wide range of incentives the rule allows – anywhere between 0% and 25% of the total program cost – indicates the Commission is to award an appropriate incentive based on the facts of each case and based on the incentive that is warranted by a particular program.

NWIGU urges the Commission to recognize that the incentive to the Company will be pure additional profit, provided to the Company independently of any of the other costs or benefits of the program. That is, to the extent the Company will incur costs for implementing its program, those costs are fully recovered in rates as part of the overall program, and the Company's receipt of an incentive will be *in addition to* the recovery of those costs. Northwest Natural carries the burden in this case to demonstrate that the incentive payment to the Company is not only reasonable, but that it is necessary for its participation. Northwest Natural has not made such a showing. While the Company asserts broadly that the \$10 per metric ton incentive will send a strong price signal to the Company to develop programs that save a significant amount of carbon, that argument addresses only the Company's opinion that the incentive is reasonable. The Company fails to go to the next step and explain why lower incentives are unreasonable, or why such a high incentive is necessary for it to participate in the CHP program. Indeed, the Company's filing implies that it would participate in the program at a lower incentive because it "hopes to find" an "incentive level that the stakeholders and Commission can agree would make sense going forward."

NWIGU's witness has proposed that the Company incentive be reduced to no more than \$5 per metric ton of reduced carbon. This reduction has multiple benefits. NWIGU's proposal, for example, recognizes that Northwest Natural needs little additional incentive itself to participate in a program like this and that the true "need" is for an appropriate customer incentive that will ensure participation in the program. As Staff rightly noted, the Company has incentive to participate in this program even without the additional incentive payment, because it will benefit from increased load on its system. NWIGU's proposal also retains the Company's ability to obtain a large amount of additional revenue, while reducing the overall program cost by millions of dollars.

B. Customer Incentive

Northwest Natural's filing proposes an incentive payment to customers of \$30 per metric ton of reduced carbon emissions. NWIGU's initial testimony in this matter is that the customer incentive amount appears to be within a zone of reasonableness, but that the Commission should reduce that amount if it finds that customers are likely to participate at adequate levels with a lower incentive.

After reviewing the testimony of other stakeholders, NWIGU believes there are indeed bases for reducing the customer incentive Northwest Natural has proposed. Staff, for example, provided testimony demonstrating several factors likely to increase a customer's willingness to participate in the program, such as the level of returns for participating customers compared to the Commission-approved cost of capital for Northwest Natural, the potential for receiving incentive payments beyond the payback period contemplated by the program, and benefits from improved power reliability associated with CHP which are not identified in the Company's payback computations.

NWIGU recognizes that a market-based approach for establishing a more precise customer incentive is desirable. NWIGU, however, is not yet prepared, based on the current record, to endorse proposals by other parties to create a “reverse auction” mechanism. As described in the testimony of NWIGU’s witness, the concept of a reverse auction is premised on an assumption that Northwest Natural will actually receive bids from potential companies seeking to participate in the program. To submit a bid in the auction, however, a company with a large number of projects competing for capital would have to invest significant time and resources into developing a bid for the auction. The obvious risk with this approach is that no bids come in. The record is also unclear on what protections would be put into place to ensure either adequate participation in an auction, or that the auction does not result in a customer incentive that is actually higher than what the Company has proposed.

The advantage of establishing a set incentive amount is that it provides companies considering a CHP investment with a concrete number to run their assumptions against. If the investment meets internal approval, companies could then apply for the incentives. It is possible that a reverse auction could be set up with enough parameters to address NWIGU’s concerns. However, NWIGU does not believe that the record contains enough information at this point on which the Commission could design an effective reverse auction process.

C. Earnings Test

In its response testimony, the Citizens’ Utility Board of Oregon (“CUB”) asserted that the Commission should apply a deferral earning test to the Company’s incentive and set an earnings test threshold at the level of the Company’s authorized return on equity plus its incentive level. NWIGU supports any approach that captures the intent of CUB’s proposal, which is to prevent the Company from raising rates to cover costs when current rates are already sufficient for that

purpose. The benefit of CUB's approach is that it does not seek to erode Northwest Natural's ability to recover the incentive it is relying on to participate in the program, but it also does not place an additional, unnecessary burden on ratepayers when the Company is in an overearning situation.

D. Fuel Switching

The record in this matter contains testimony asserting that Northwest Natural's proposal is flawed because it improperly provides incentives for customers to fuel switch. It is NWIGU's position that such an argument does not serve as a basis for rejecting Northwest Natural's filing.

NWIGU recognizes that it has been the policy of the Commission to not allow utilities to provide incentives for customers to fuel switch. That policy, however, cannot be strictly adhered to in light of SB 844. That legislation must be fully implemented despite any Commission policies that existed prior to its enactment. As NWIGU's witness observes, SB 844 expressly authorizes Oregon natural gas local distribution companies to incentivize their customers to reduce carbon dioxide emissions through the greater use of natural gas. Since natural gas is a fossil fuel, the only way one can use natural gas as a carbon dioxide emission reduction measure is to use natural gas instead of a more carbon-intensive fuel. Moreover, the Commission can presume that the Legislature was aware of the Commission's existing policies when it enacted SB 844. The intent of SB 844 to use natural gas by switching from a more carbon intensive source of energy to natural gas must therefore be deemed to have superseded that policy, or at least to serve as an exception to that policy. In other words, if the Commission were to rule that the tariff filed by Northwest Natural is inappropriate because it incentivizes fuel switching, the Commission would be undermining the entire intent of SB 844.

III. CONCLUSION

The foregoing represents a summary of NWIGU's testimony in this matter and the current position it has taken on various components of Northwest Natural's filing. NWIGU will continue to participate in this docket throughout the hearing and post-hearing briefing process, and will offer a final position and argument once the record is fully developed.

Dated this 12th day of November 2015.

Respectfully submitted,



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