

ITEM NO. 8

PUBLIC UTILITY COMMISSION OF OREGON
STAFF REPORT
PUBLIC MEETING DATE: January 30, 2017

REGULAR CONSENT EFFECTIVE DATE February 1, 2018

DATE: January 19, 2018

TO: Public Utility Commission

FROM: Scott Gibbens *SG*

THROUGH: *I* Jason Eisdorfer and John Crider *I for JC*

SUBJECT: NORTHWEST NATURAL: (Docket No. ADV 694/Advice No. 17-21)
Requests an extension for the Company's Schedule H "Large Volume
Non-Residential High Pressure Gas Service (HPGS) Rider."

STAFF RECOMMENDATION:

Approve Northwest Natural's request in Advice No. 17-21 to extend the Company's Schedule H Rider, effective for service on and after February 1, 2018, for a period of five years, subject to the following condition:

- Staff will perform a review of market conditions prior to February 1, 2020 to determine if alternative Commission action is necessary or if the program should be allowed to continue until January 31, 2023.

DISCUSSION:

Issue

Whether the Commission should allow Northwest Natural Gas Company (NWN) to continue to offer its non-residential High Pressure Gas Service (HPGS), for which there is a potential competitive market, for an additional five-year period.

Applicable Rule or Law

The Commission may approve tariff changes if they are deemed to be fair, just and reasonable pursuant to ORS 757.210. Tariff revisions or corrections may be made by filing revised sheets with the information required under the Commission's administrative rules.

In this particular filing, NWN proposes to extend its provision of a regulated service in a potential competitive marketplace. The Commission addressed this issue in Order No. 14-014, concluding that “[a]lthough natural gas vehicle fueling is potentially a competitive business, CNG fueling is properly considered a utility service and may appropriately be offered under regulated tariffs.”¹ Additionally, the Commission adopted policy criteria for approval of NWN’s provision of CNG fueling as a regulated service. The criteria includes: (1) a demonstration that NWN customers are not only protected from the service offering, but will also receive a net benefit from the company’s entry into the market; (2) no competitive market for CNG vehicle fueling currently exists; and (3) the competitive market for the provision of CNG vehicle fueling may not develop absent utility participation, in other words, utility participation will likely be a catalyst to the growth of a competitive market.²

Analysis

Background

NWN filed Advice No. 17-21 on December 21, 2017, requesting a five-year extension of its Schedule H, Large Volume Non-Residential HPGS Rider. NWN originally asked for authority to provide this service in Advice No. 13-10, submitted on June 27, 2013. NWN proposed to add Schedule H, Large Volume Non-Residential HPGS Rider, to its Rate Schedules 3, 31, and 32 non-residential natural gas service schedules. Due to a significant number of parties expressing interest or concerns in the matter, the Public Utility Commission of Oregon (Commission) opened Docket No. UG 266 to investigate NWN’s proposal.

In Order No. 14-014, the Commission approved NWN’s proposal in Advice No. 13-10 as follows:³

We approve NW Natural's request. Although natural gas vehicle fueling is potentially a competitive business, CNG fueling is properly considered a utility service and may appropriately be offered under regulated tariffs. Moreover, NW Natural has structured its HPGS tariff rider in a manner that meets our requirements for a utility proposing to provide a regulated service in a potential competitive marketplace.

¹ Order No. 14-104 at 6-7 (concluding that CNG fueling falls within the definition of utility service because the term “service” in ORS 756.010(8) is used in its broadest and most inclusive sense and includes equipment and facilities related to providing the service or the product served. The Commission further concluded the statutory definition of “public utility” in ORS 757.005 indicates that the legislature contemplated that alternative fuels for use in motor vehicles would be provided both as a regulated and non-regulated service.).

² Order No. 14-014 at 7-8.

³ Order No. 14-014 at 6, 9, and 10.

In reaching these decisions, we acknowledge the concerns raised by Clean Energy and other [sic] that utilities may have certain advantages as marketplace participants. Due to these potential advantages, we conclude that reviews are necessary to assure the viability and integrity of competitive markets.

Accordingly, we condition our approval of NW Natural's HPGS to a period of two years from the effective date of the tariffs. Following that period, we will revisit the offering to determine whether the regulated service should continue, or whether it should be modified or discontinued on a going-forward basis. To assist that effort, we instruct our Staff to undertake an investigation of the CNG fueling market and NW Natural's participation in it, and to make such recommendations to the Commission as will further the growth of a robust competitive market. We specifically direct Staff to examine whether circumstances on which we based our decision have changed, and to report on the market development in parts of Oregon not served by NW Natural.

On December 14, 2015 NWN filed ADV 173/Advice No. 15-19 which requested a two-year extension of the HPGS program. As directed by Commission Order No. 14-014, Staff investigated the status of the CNG market to determine if circumstances had changed following the Commission's original decision. Staff found that the market had not changed in a significant manner and recommend approval of the proposed extension. The Commission adopted Staff recommendation in Commission Order No. 16-013, which extended the program through February 1, 2018.

HPGS Service⁴

This optional rider provides HPGS through NWN owned and maintained compression equipment sited on a HPGS customer's premises. According to NWN, the HPGS rider responds to customer requests for utility services that would provide the infrastructure needed to support the customer's ability to fuel vehicles using compressed natural gas (CNG).

NWN states that service under Schedule H provides a non-residential customer with a turn-key solution not otherwise available for providing the gas pressure required for vehicle fueling, without a significant upfront capital investment into compression facilities. The terms of service and pricing for HPGS will vary for each installation and will be laid out in the customer's HPGS Service Agreement. The customer will be billed a monthly facility charge designed to recover all equipment, permitting and siting costs. NWN proposes that the monthly facility charge be derived by multiplying the actual

⁴ The summary in this section is excerpted from the October 14, 2013, Staff Report in Advice No. 13-10, pp. 2 and 3.

project costs by an annual cost recovery factor, divided by 12. The cost recovery factor is designed to recover in each year the depreciation on the HPGS equipment plus NWN's financing costs, at its authorized return, for the investment made on behalf of the customer.

In addition, NWN states the HPGS customer's monthly bill will also include a charge for scheduled maintenance, and when applicable, charges for any other services such as unscheduled maintenance or back-up gas service that NWN may provide. The charges under Schedule H will be in addition to the charges for natural gas service billed in accordance with the non-residential rate schedule on which the customer is served. Both the costs and the revenues of this rate rider are treated as "above-the-line" rate regulated services. HPGS customers served under Schedule H will pay all costs associated with the provision of HPGS, and the addition of this service offering will have no negative cost impact on, and in fact benefit, other ratepayers.

This year NW Natural executed the first HPGS Agreement with the City of Portland. This is the first customer to be on Schedule H. Installation of the CNG equipment was completed in December 2017, and operations are expected to begin in the first quarter of 2018. The Company also has two signed feasibility agreements with customers interested in participating in the Schedule H program.

Market Analysis

Unlike Order No. 14-014, Commission Order No. 16-013 did not direct Staff to perform an investigation into the current status and effects of NWN's participation in the CNG fueling market. However, the Staff report stated:

Prior to the end of the two-year period, the Commission should determine whether the service should be continued as is, modified, or discontinued.

In an attempt to determine whether the service should be continued or modified at this point in time, Staff reviewed three questions in this filing that it derived from the direction found in prior Commission orders⁵:

1. Has the CNG fueling market changed in the previous two years? If so, how?
2. Is there or will there be a competitive CNG market in Oregon in the foreseeable future? Does NWN's participation impact the market in a harmful way?
3. Does the program provide a net benefit to NWN customers?

CNG Market Changes

⁵ See Order No. 16-013 at 4.

Based on information provided by the U.S. Department of Energy, Staff found a total of sixteen CNG fueling stations currently open and operating in Oregon. Comparatively, there were fifteen open stations in October of 2016. Two new stations opened in southern Oregon, both of which are outside of NWN's service territory; one station closed outside of NWN's service territory; and two stations located in Vancouver, WA opened within NWN's service territory. Roughly 30 percent of the CNG locations in Oregon are NWN owned sites. Table 1 below displays a list of the CNG stations open over time. Based on the information from the U.S. DOE, Staff concludes that there is little to no change in the CNG fueling market.

Table 1

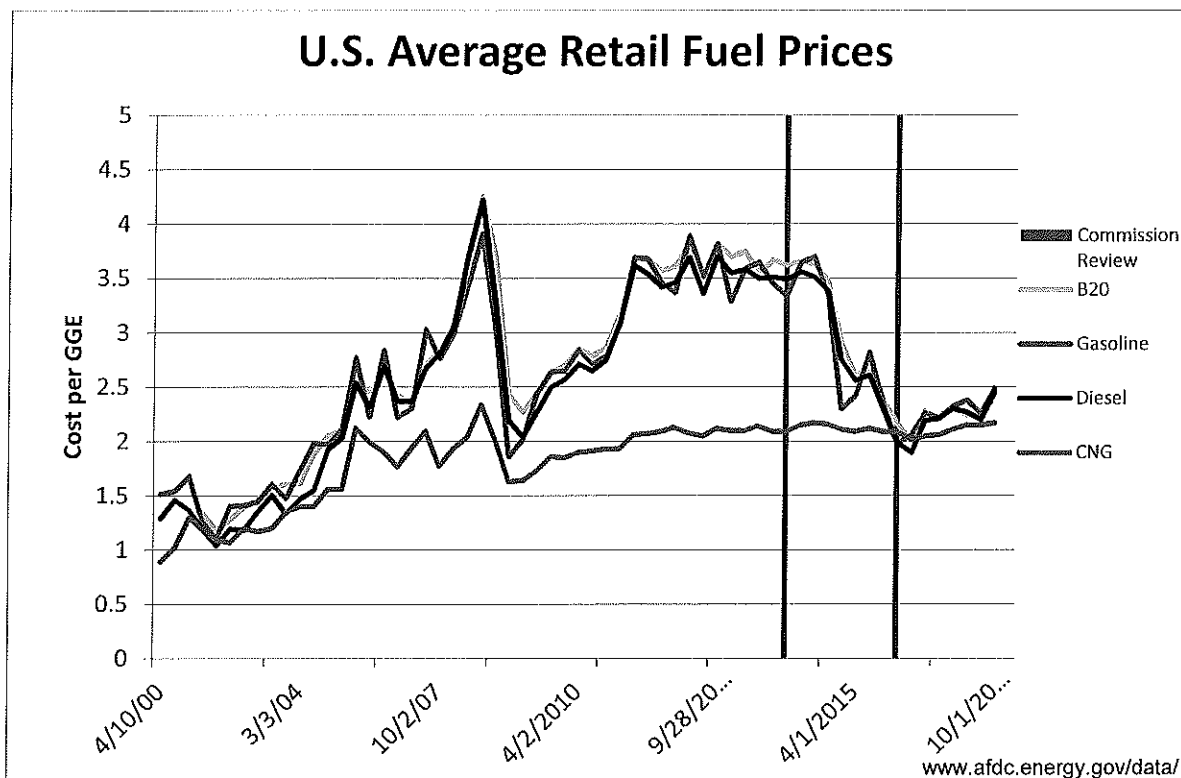
<u>May 2013 Stations</u>	<u>October 2015 Stations</u>	<u>December 2017 Stations</u>
Northwest Natural Gas - Parkrose Service Center	Northwest Natural Gas - Parkrose Service Center	Northwest Natural Gas - Parkrose Service Center
Northwest Natural Gas - Mt Scott Service Center	Northwest Natural Gas - Mt Scott Service Center	Northwest Natural Gas - Mt Scott Service Center
Northwest Natural Gas - Salem Service Center	Northwest Natural Gas - Salem Service Center	Northwest Natural Gas - Salem Service Center
Oregon Department of Administrative Services Motor Pool	Oregon Department of Administrative Services Motor Pool	Oregon Department of Administrative Services Motor Pool
Northwest Natural Gas - Sunset Service Center	Northwest Natural Gas - Sunset Service Center	Northwest Natural Gas - Sunset Service Center
Rogue Valley Transportation District	Rogue Valley Transportation District	Rogue Valley Transportation District
Port of Portland Airport	Port of Portland Airport	Port of Portland Airport
Salem - Keizer Transit	Salem - Keizer Transit	Salem - Keizer Transit
Avista Klamath Falls Service Center	Avista Klamath Falls Service Center	Avista Klamath Falls Service Center
Northwest Natural Gas - Sherwood Service Center	Northwest Natural Gas - Sherwood Service Center	Northwest Natural Gas - Sherwood Service Center
Northwest Natural Gas - Tualatin Service Center	Waste Management - Portland Hauling	Waste Management - Portland Hauling
Northwest Natural Gas - South Service Center	Truck 'N Travel CFN #746	Truck 'N Travel CFN #746
Jackson County Motorpool	Waste Management - Washington County	Waste Management - Washington County
	South Metro Area Regional Transit Agency	South Metro Area Regional Transit Agency

	Jackson County Motorpool	Clean Energy - Central Point Pilot #391
		TruStar Energy - Rogue Green Fuels LLC
		Clean Energy - Waste Connections*
		Trillium CNG*

* Station located in Vancouver, WA

Staff also analyzed how external market forces have affected the growth of the CNG fueling market over the past two years. Table 2 below shows the price of CNG compared to several substitute fuels. The relative price of CNG compared to other fuels which could be utilized to power large vehicles has gotten more expensive. Although the gross price has remained relatively flat, the competing fuels have become cheaper. This occurred dramatically during 2014 and 2015, where the price of CNG went from being roughly 40 percent cheaper than competing fuels to roughly the same price. This makes building new CNG stations less attractive to investors as the long run cost savings or revenues are less likely to offset upfront capital costs in a given amount of time. The dramatic change in relative price was occurring around the same time frame as Staff's previous review of the CNG market. Since that point, prices have remained relatively close, although the most recent data shows a small divergence.

Table 2



CNG Market Competition

Staff finds relatively little change in the competitive nature of the CNG market both within NWN's service territory and outside of NWN's service territory. Although Staff lacks the data to perform a more traditional test of competition in a given market (Herfindahl index or concentration ratio), Staff notes that little has changed since the previous Commission finding of an infant industry with little evidence of a robust competitive market. An increase of a single station does not warrant a change in the previous Commission position in Staff's view. Likely, the decrease in diesel and gasoline prices due to the shale oil boom had a dampening affect on the growth of the CNG market.

In examining how NWN may have or may be affecting competition in the industry, Staff also finds little impact. NWN's service territory encompasses over 50% of the entire population of the state, including the majority of the major population centers. Similarly, the majority of the CNG fueling stations are located within NWN's service territory. In

2015, 70 percent of the non-NWN-owned stations were located in NWN's service territory. In 2017, 69 percent were located within NWN's service territory. Likewise, half of the public CNG fuel stations were located within NWN's territory in 2015 and in 2017.

In summary, Staff finds that the CNG market has developed roughly the same between NWN's service territory and outside of its territory, which have both seen limited development. The changes have been small and insufficient to change Staff's position on the CNG fuel market. The outlook depends largely on the relative pricing of CNG compared to comparative fuels. This is the predominant reason for Staff's recommendation to approve the Company's request to extend the service for five more years, but on the condition that a follow up review of the market conditions be performed no later than two years from the new effective date of the tariff to ensure that circumstances have not changed enough to warrant a shift in Commission policy. To accomplish this, Staff recommends that the Company file a report which discusses the current state of the CNG market, including:

1. The number of new and existing entrants within and outside of NWN's service territory;
2. The current number of customers enrolled and beginning the process of enrolling in the HPGS program; and
3. Other outside factors affecting the development of a competitive market.

This report should be provided by to the Commission via electronic filing no later than December 1, 2019. Staff will then have approximately 60 days to review the market status and inform the Commission should alternative actions be necessary via a public meeting before the two-year anniversary of February 1, 2020.

Net Benefit to Customers

As discussed above, because NWN is offering a regulated utility service in a competitive market, customers must receive a net benefit from the company's entry into the market. Similar to market conditions, Staff sees little change in the benefit to customers found by the Commission in UG 266. As stated in Staff's report dated December 29, 2015:

The additional sales made through the HPGS offering will provide net benefits generally to other customers. The sales of natural gas to the new HPGS customers will make the same contribution to fixed costs as gas purchases by other commercial gas customers. By spreading these costs over a larger volume of sales, the amount affixed costs that are recovered per unit of sales is reduced. The Commission found that NWN's provision of CNG fueling as a regulated service will provide a net benefit to other customers.

Staff recognizes that NWN has an executed contract with a customer and is actively working at the feasibility study stage with two additional customers. NWN will not likely be able to conclude that work without an extension of Schedule H. Staff concludes there is no evidence that NWN's participation in the market has disrupted the development of a competitive market for CNG fueling stations, and notes that such a market has been slow to develop. As a result of these considerations, Staff recommends that NWN's Schedule H, High Pressure Gas Service Rider, be allowed to continue for an additional five years, with a review of market conditions in no longer than two years' time.

Staff concludes that no legitimate competitive market for CNG vehicle fueling currently exists; and NWN's participation is likely to help with the CNG fueling market, which continues to struggle to develop absent utility participation.

CONCLUSION:

Staff finds that circumstances have not changed in the CNG fuel market. There is no legitimate competitive market for CNG vehicle fueling in Oregon. NWN is providing a service that would not otherwise be available to customers without the utility's involvement in the market. The HPGS program provides a net benefit to all NWN ratepayers.

PROPOSED COMMISSION MOTION:

Approve Northwest Natural's request in Advice No. 17-21 to extend the Company's Schedule H Rider, effective for service on and after February 1, 2018, subject to the following condition:

- Staff will perform a review of market conditions prior to February 1, 2020 to determine if alternative Commission action is necessary or if the program should be allowed to continue until January 31, 2023.