

BEFORE THE PUBLIC UTILITY COMMISSION

OF OREGON

LC 64

In the Matter of)
)
)
 NORTHWEST NATURAL GAS) COMMENTS OF
 COMPANY dba NW NATURAL) THE CITIZENS' UTILITY BOARD
) OF OREGON
)
 2016 Integrated Resource Plan)
)
 _____)

I. INTRODUCTION

CUB is generally supportive of NW Natural’s IRP Action Plan. However, there are two elements of the action plan that raise questions and concerns and it is those elements that CUB discusses in these comments.

NW Natural divides its action plan into two parts: demand-side resources and environmental actions; and resource investments. Within the demand-side resources and environmental actions, CUB is concerned with NW Natural’s “upstream carbon emissions reduction” plan described by the Company as follows:

Investigate the viability of developing a pilot project to reduce upstream emissions of methane and, if viable, NW Natural will bring this pilot forward for Commission review and approval. The pilot design would test whether reductions can be achieved at a level consistent with the Base Case carbon values incorporated into the IRP and the range of costs for a larger scale effort. If it is determined that the cost to move the market

exceeds the carbon values in the IRP, the Company may alternatively consider advancing the work as a project proposal under SB 844.¹

Within the resource investments, CUB is concerned with the following Mist underground storage facility investment:

Replace or repair, depending on relative cost-effectiveness, the large dehydrator at Mist's Miller Station. Replacement is currently estimated to cost between \$6 million and \$7 million based on estimates obtained from a third-party engineering consulting firm engaged by NW Natural. NW Natural will evaluate alternatives associated with the AI's Pool and Miller Station small dehydrator systems at Mist to determine if and when additional actions are warranted.²

II. UPSTREAM CARBON EMISSIONS REDUCTION

CUB notes that this action calls for the company to “investigate the viability” of upstream emission reduction to see if a pilot is feasible. According to the Company, the “action item, as proposed, states that the Company will further refine this work before approaching the Commission with a possible pilot proposal”.³ This level of investigation does not require an acknowledgement. An acknowledgement allows a utility to pursue an activity with reduced risk of disallowance. In this case, the Company is not asking to acknowledge an investment or a pilot program, but to acknowledge an “investigation to determine the viability” of a concept. But the Company says little about the cost of this investigation or how this investigation will be conducted. Because it is the investigation that is the activity which the Company seeks acknowledgement, CUB believes that there is not enough information about the investigation to provide acknowledgement.

Ultimately, the Company is considering paying more for natural gas that is certified to meet a “methane standard”:

¹ LC 64: NW Natural 2016 Integrated Resource Plan, page 1.18.

² LC 64: NW Natural 2016 Integrated Resource Plan, page 1.18.

³ LC 64, NW Natural 2016 Integrated Resource Plan, page 4.20.

It may be possible to use the Base Case carbon pricing proposed in the IRP to allow for the purchase of gas certified to the “methane standard” at a modest premium. If we find this more straightforward “IRP approach” is not adequate to provide an incentive for gas producers, the Company may need additional flexibility, such as that afforded under SB 844, to implement this upstream methane reduction effort.⁴

This description raises significant concerns to CUB. CUB believes that NW Natural needs to provide a more significant discussion regarding carbon reduction, SB 844, and the effect of including a price on carbon in an IRP.

A. *SB 844 Construct*

SB 844 was designed to allow, encourage and incentivize voluntary carbon reduction by natural gas utilities.

1. *NW Natural is Proposing a Third Tier for Carbon Reduction Projects*

Under SB 844, the Commission was required to set Tiers for the program.

According to the Commission Order establishing the rules for SB 844 programs:

A project with proposed costs equal to or less than \$1 million and \$85 per metric ton of reduced emissions is a Tier-1 project, and a project with estimated costs greater than either of these thresholds is a Tier-2 project. We also incorporate NW Natural's edits, and note that the introductory sentence in particular is helpful to supply context and explain that the designation of a Tier-1 or Tier-2 project determines the procedural process for the application. We are not persuaded by NWIGU's concerns over the \$85 per ton value because there are two triggers for the Tier-2 process-if a project's proposed costs exceed either the \$1 million benchmark or the \$85 per ton measure, it will receive the additional scrutiny allowed by our contested case procedures. The statute gives us discretion to set the threshold for cost per ton, and considering the lack of any similar programs to use as benchmarks, we find the \$85 per ton figure reasonable.⁵

NW Natural is essentially proposing a third tier based on the carbon costs used in the IRP, which is based on the California cap-and-trade program. If a program costs on a

⁴ LC 64, NW Natural IRP, page 4.21.

⁵ OPUC Order No. 14-417, page 3.

\$/ton level is less than the California cap-and-trade costs, then it does not require SB 844 flexibility. But the SB 844 rules state that a voluntary carbon reduction program does not contemplate a third tier. If a voluntary carbon reduction program costs less than \$1 million and \$85 per metric ton, then it is a Tier-1 program. If it costs more than \$1 million and \$85 per metric ton, then it is a Tier-2 program. In the case of NWN's pilot program, the Company envisions that it will be less than \$85 per metric ton, but it does not say what the total cost is expected to be. If the total cost is more than \$1 million, it is a Tier-2 project.

2. *Commission Biennial Report to the Legislature*

SB 844 requires the Commission regularly study whether voluntary programs are still required:

The commission shall biennially conduct a study on whether federal law or regulation or other state laws or rules provide adequate incentives for public utilities that furnish natural gas to invest in projects that reduce emissions in the ordinary course of business. The commission shall report the results of a study conducted under this subsection, and may make recommendations for legislation, to the Legislative Assembly in the manner described in ORS 192.245 not later than February 1 of each odd-numbered year.⁶

The Commission submitted such a report to the 2015 legislature:

The Commission reviewed federal and state laws and rules to determine whether any incentives exists for Oregon's natural gas utilities to undertake voluntary GHG emission reduction projects as part of their ordinary course of business. The Commission concludes that no law or rule exists that now would spur natural gas utilities to undertake GHG emissions reduction projects.⁷

However, under NW Natural's approach, by including the price of carbon under California's cap-and-trade program, an incentive exists outside of SB 844. An actual

⁶ SB 844, Section 2 (11).

⁷ OPUC 2015 Biennial Report to Legislature on SB 844.

state or federal law or regulation is not required, because for planning purposes the utility is imputing the values of California's law.

3. 4% Cost Cap

The PUC rules for SB 844 contained a 4% cost cap for voluntary carbon reduction programs. By proposing a voluntary carbon reduction program outside of the construct of SB 844, NW Natural allows itself to conduct carbon reduction activities outside of the cap established under Commission rules.

B. Interaction of SB 844 and NW Natural's Upstream Carbon Reduction

By including a price of carbon in the IRP, and then proposing carbon reduction programs that are below the SB 844 cap, NW Natural suggests that a prudent utility would act on the carbon values in the IRP without authorization of SB 844. However, if this is what a prudent utility would do, then it is no longer voluntary because Oregon expects utilities to act prudently.

The implications of NW Natural's proposal on SB 844 are huge. SB 844 is based on the assumption that utilities will not take up carbon reduction programs without a legal or regulatory requirement and therefore need an incentive. But if a prudent utility will conduct carbon reduction activities up to a level supported by California's cap-and-trade, then there is no basis for providing an incentive to a gas utility – at least up to the level of carbon costs reflected in the IRP.

In addition, it raises the fundamental question of whether SB 844 is still needed. The PUC biennial reports to the legislature examine whether there are laws or rules that would "spur" natural gas utilities to reduce carbon emissions. NW Natural's approach

suggests that “laws and rules” are not required. Instead, Oregon can impute California cap-and-trade values.

1. Using a Carbon Price in the IRP

CUB is not suggesting that forecasting future carbon regulatory costs in an IRP is inappropriate. CUB, in fact, supports NW Natural and other utilities including an expected cost of carbon regulation in IRP planning. CUB notes that originally SB 844 was intended to apply to electric utilities which have included carbon costs in their IRP for several years.

CUB agrees with NW Natural that carbon regulation is likely to occur at some point over the planning horizon, and a prudent utility should incorporate expected carbon costs into its IRP planning. This is critical in evaluating long-term investments whose useful lives will likely include a period of carbon regulation. For DSM programs this makes a lot of sense. Weatherizing a home will reduce natural gas usage and at some time in the future that usage reduction is likely to reduce NW Natural cost of carbon regulation. When evaluating long-term investments it is important to consider the impact of carbon regulation.

2. Fitting SB 844 and IRP Planning Together

NWN fails in its IRP to provide its vision as to how these programs fit together. CUB's view is that it is important for utilities to consider future carbon regulatory costs when planning and investing in their system. NW Natural's bare steel replacement program likely reduced future carbon regulatory costs and it would have been appropriate to evaluate that benefit in an IRP. But that is an investment that has a long useful life and

is part of the utility's on-going investment in its system. A prudent utility should include expected carbon regulatory costs in its planning.

SB 844 applies to voluntary activities that go beyond what a prudent utility would do without the authority of SB 844. NW Natural seems to believe that the separation between SB 844 voluntary activities and "prudent" utility operations is defined based on the per ton carbon price. Activity above the price in the IRP are voluntary, prices below it are reasonable and prudent without SB 844.

CUB believes the distinction between SB 844 voluntary activities and prudent utility operations is based on whether expected future carbon regulation will likely impact a utility's decision. DSM programs and bare steel pipe replacement have useful lives that extend into a future that is likely to include carbon regulation.

But at the same time, carbon regulatory costs do not currently affect NW Natural's system. If NW Natural's upstream emission reduction program is focused on short-term gas purchases that are cleaner, but there is no basis to forecast carbon regulation during the period of those short term purchases, then it is a voluntary activity that goes beyond what a prudent utility would do. But those programs should be considered SB 844 programs.

CUB recommends that the Commission not acknowledge NWN's upstream carbon reduction program. CUB encourages the Company to investigate the feasibility of the program. If the program is feasible, CUB believes that the Company should bring it forward as a SB 844 voluntary program.

III. THERE SHOULD BE NO INVESTMENT IN MIST UNTIL COMPLETION OF THE LONG AWAITED COST STUDY

NW Natural proposes investing \$6-7 million in replacement and repair costs to the Mist underground storage facility. Yet NW Natural fails to identify whether this investment is related to the portion of Mist storage dedicated to core customers or if it is related to interstate storage. According to CUB Exhibit 105 in UM 1654 (NW Natural's answer to CUB DR 3 in that docket), Miller Station is a shared facility with two compressors and three dehydrators (with one compressor and one dehydrator associated with interstate storage):

A secondary shared facility is the Miller Station (compressor station). The operator building, compression building and in-ground piping infrastructure are utilized. Since interstate storage services began being offered, the Company has added a second turbine compressor and a third dehydration unit. These incremental capital additions are being charged to Interstate Storage (and therefore paid for by shareholders and not customers) except for a small amount of customer capacity recall of the turbine compressor.⁸

It is unclear to CUB whether the IRP discussion is in reference to equipment that serves core customers, interstate customers, or both. Both the IRP and the evidence in UM 1654 discuss dehydration units at Miller Station, but UM 1654 makes clear that some of this investment relates to interstate storage. CUB believes that the Company needs to offer more explanation of core versus non-core activities related to this investment.

Mist storage became an issue in NW Natural's last rate case and in a separate docket following that rate case. In those proceedings CUB was concerned that core customers are subsidizing interstate storage and optimization activities that were being allocated to interstate storage. In docket UM 1654, the Commission ordered NW Natural

⁸ UM 1654/CUB/Exhibit 105.

to work with the parties to the case to conduct a cost of service study of interstate storage and optimization:

We determine that a neutral third party should conduct an evaluation and cost allocation study of NW Natural's optimization activities. The study will more robustly examine the risks, costs, and benefits of NW Natural's optimization activities, the assets being utilized for those activities, the allocation between regulated and unregulated services, and the various components of NW Natural's system that drive the costs and revenues associated with interstate storage services. We agree with NWIGU that the sharing mechanisms should be fact-based and reflect the true value of customers' and shareholders' contributions.

We direct the parties to this docket to form a steering committee that will develop the third-party contract, develop and articulate the elements of the study, interview and hire the third party who will conduct the study, and oversee the contractor's work. NW Natural will receive cost recovery for the cost of the study. While the study is being conducted and reviewed, we will retain the company's current sharing percentage, and do not require that revenues be reported in the company's ROO. We will decide these issues after the cost allocation study is complete.⁹

This order was issued nineteen months ago, in March of 2015. Progress has been slow.

After this order came out in 2015, it took more than six months to convene the first meeting of the parties to discuss the order. As of today, the parties still have not agreed to a neutral third party – though we have interviewed some.

CUB does not oppose NW Natural's investment in Miller Station, but we are opposed to adding any additional investments to captive customer rates until the Cost of Service study ordered by the Commission is finalized and reviewed. The cost study is necessary to determine the extent that customers are subsidizing interstate storage at Miller Station.

CUB recommends that the Commission not acknowledge this action because the Company has failed to demonstrate that these assets are not used to support interstate

⁹ OPUC Order No. 15-066, pages 5-6.

activities. Further, the Commission should be clear that this lack of acknowledgement does not create any presumption of imprudence -- that if NW Natural can demonstrate -- and the cost study already ordered by the Commission is an essential element of that demonstration -- that this investment serves captive customers and does not subsidize interstate storage, then cost recovery will be considered without prejudice.

As an alternative, the Commission could acknowledge this investment, but that acknowledgement must come with a big asterisk (in forty-eight point font), declaring that rate recovery is dependent on completion of a cost study which demonstrates that captive customers are subsidizing neither interstate storage nor interstate storage optimization.

Dated this 3rd day of November, 2016.

Respectfully submitted,

A handwritten signature in black ink, appearing to read "Bob Jenks". The signature is fluid and cursive, with a long horizontal stroke at the end.

Bob Jenks
CUB Executive Director