



May 15, 2015

Oregon Public Utility Commission

Attn: Chair Susan Ackerman

Commissioner John Savage

Commissioner Steve Bloom

PO Box 1088

Salem, OR 97308-1088

RE: ADV 18, NWN Advice Filing No. 15-03

Dear Commissioners,

CUB urges the Commission to reject NW Natural's Advice Filing No. 15-03 ("Compliance Filing"), which it filed pursuant to Commission Order No. 15-049.

To the best of my knowledge, this is the first time that CUB has urged the Commission to reject a compliance filing. Compliance filings are normally straightforward attempts to implement a Commission order. Generally, they simply require a ministerial review to ensure that the calculations are correct.

NW Natural's compliance filing in this case, however, is different. This Compliance Filing ignores the Commission's decision on interstate allocation, which established a single allocation factor for both environmental remediation costs and insurance proceeds. Additionally, the Compliance Filing assumes that Order 15-049 granted NW Natural authority to retroactively charge current customers a surcharge of \$12.1 million to cover the time period from January 2013 to May 2015, while at the same time failing to follow the Commission's direction in Order 15-049 on the allocation of insurance proceeds to 2013 costs. Finally, the Company is attempting to reduce the required write-off of historic costs by including additional interest after the application of the earnings test, and then offsetting the additional interest with interest on the insurance proceeds.

To the degree that a utility wishes to challenge a Commission order, or is legitimately unsure about how to implement it, the utility can request reconsideration and/or clarification of the Commission's order. The fact that NW Natural asked for reconsideration on one issue in this docket the same day that it filed this Compliance Filing demonstrates an internal decision not to seek clarity on these additional issues, and to plow ahead with an interpretation that is clearly at odds with the actual language of the Order. The fact that the Company asked the Commission for an order approving the Compliance Filing further suggests that the Company was aware that its Compliance Filing was inconsistent with Commission Order No. 15-049 – if it was consistent with the Order, there would be no need for an additional order on the Compliance Filing.

1. Interstate Allocation: The Compliance Filing is Not Consistent With the Commission Order.

Interstate allocation of environmental remediation costs and insurance proceeds between NW Natural's service territory in Oregon and Washington was a contested issue.

CUB's Position.

CUB has consistently advocated allocating the costs and insurance receipts based on current allocation practices, which would allocate 90.7% of the costs to Oregon and 9.3% of the costs to Washington.¹ CUB's recommendation was based on the belief that these costs are not related to actual utility service and that the current customers are only being charged because this is a current cost to the Company.

NW Natural's Position.

NW Natural has argued for two allocations of cost: 96.68% of the costs associated with the GasCo plant to be allocated to Oregon and 100% of the costs of the Portland Gas Manufacturing site to be allocated to Oregon.²

Phase 1 Settlement.

For the purposes of settlement, the parties agreed to use the 96.68% figure in the Prudence and Earnings Test Stipulation:

State Allocation Factor

The parties agree that 96.68% of the deferred costs amortized through the SRRM will be allocated to Oregon customers.³

¹ UM 1635 – CUB/100/Jenks/21; UM 1635 – CUB/200/Jenks/20.

² Advice Filing at fn. 7.

³ UM 1635 – Prudence and Earnings Test Stipulation filed July 11, 2013.

This was a compromise made in the context of a settlement. CUB compromised on interstate allocation because we believed the stipulation would require NW Natural to contribute a fair amount of its future earnings to future remediation activities.

Order 15-049.

Order No. 15-049's resolution of this contested issue was clear, and directed NW Natural to use the allocation that was agreed upon in the Prudence and Earnings Test Stipulation:

We also adopt the parties' initially agreed-upon interstate allocation, which relies on historic operations to determine the allocation of costs between Oregon and Washington.⁴

The Compliance Filing

In its Compliance Filing, the Company ignores the Commission Order for the purposes of costs and proposes to allocate to Oregon customers 96.68% of the costs for the GasCo site and 100% of the costs for the Portland Gas Manufacturing site. However, for the purposes of insurance, the Company allocates 96.6% of the insurance to Oregon:

NW Natural allocated \$147.1 million of the \$152.2 million of Insurance Proceeds to Oregon customers based upon the state allocation of 96.6%.⁵

This is perplexing—for purposes of insurance receipts, the Company believes there is an established “state allocation of 96.6%,” but for costs, the Company believes there is a blend of 96.68% and 100%. Further, the Company believes that this is consistent with Order 15-049.

CUB notes that in its public meeting memo, Staff suggests that if the Commission were to modify the allocation for costs, it should also require the Company to allocate the insurance in a symmetrical manner. But this is not possible without waiting until all of the costs have been incurred. Because the total cost from each of the two sites is not known, it is impossible to identify what the ratio of costs between the two sites will be. NW Natural testified that through 2012, only \$2.5 million of the \$97 million cost has been associated with the Portland Gas Manufacturing site. There is no evidence on the record in this case that provides any guidance as to what this ratio will be over the 20 year life of the remediation. In addition, CUB notes that many of the costs, such as attorneys' fees for insurance litigation, are common to both sites. NW Natural's proposal will require a constant review of costs to ensure that NW Natural is allocating the cost to the correct site.

Finally, CUB notes that we are not asking the Commission to reconsider our proposal to allocate 90.7% of the costs to Oregon. We made our arguments. The Commission reviewed the record

⁴ Order at 6.

⁵ Advice Filing at 5.

and rejected them. But the Commission should also reject the Compliance filing because it is not consistent with Order 15-049.

2. The Compliance Filing assumes that the Commission Order granted authority to charge current customers a surcharge of \$12.1 million, in addition to the \$5 million surcharge that was clearly authorized and does not allocate the insurance proceeds in the manner prescribed by the Commission Order.

Order 15-049 authorized the Company to recover environmental remediation costs from customers through 2 mechanisms: 1) a \$5 million tariff rider charged to customers on a going-forward basis that will be used to offset the first \$5 million of costs; and 2) one-fifth of the costs in the SRRM that will be charged to customers each year. Because of the length of time of the docket, the costs were split into a historic period (before 2013) and future period (2013 and beyond).

The Commission ordered the \$5 million tariff rider on a going forward basis:

we adopt Staff's recommendation to allow NW Natural to use a tariff rider to collect a certain amount of remediation expenses in base rates going forward. We agree with Staff that we should adopt a conservative amount to offset deferred costs, and adopt the higher end of Staff's recommendation-\$5 million. We direct NW Natural to file a compliance tariff to add this rider using sales estimates and allocation factors from docket UG 221, its last general rate case.⁶

In its Compliance Filing, in addition to the authorized tariff rider to collect \$5 million going-forward, the Company proposes an additional surcharge to collect approximately \$12.1 million from current customers. The Company says that this additional surcharge is designed to collect the funds that would have been collected through a tariff rider from customers in 2013, 2014, and the first five months of 2015. The Company offers no rationale as to how Order 15-049 authorized it to charge current customers for almost 3.5 years of worth of annual tariff riders.

CUB admits that there is some confusion in the Commission's Order. If 2013 and 2014 are part of the "future" period, then should they also be part of the "going forward" tariff rider? While CUB believes the Order does not explicitly address the treatment of 2013 and 2014 expenses (historical years that are included in the future period), CUB cannot find authorization in the Order for two surcharges, which combined charge current customers \$17.1 million. Because we are dealing with a deferral, retroactive ratemaking is not strictly prohibited, but retroactively charging current customers a surcharge to recover a tariff rider that was not collected in 2013, 2014 and the beginning of 2015 is not something that should be done based on inferred authority from the Order and CUB sees no direct authorization to do so.

⁶ Order at 11.

In addition, CUB believes it is unfair to charge current customers a surcharge of \$12.1 million to account for the tariff rider from 2013, 2014, and the first part of 2015, in addition to a tariff rider of \$5 million and 1/5 of the SRRM. There is no basis for charging current customers such a significant amount compared to last year's customers or next year's customers. CUB also notes that the 2013 costs have been reviewed and there are \$6.8 million of prudently incurred costs. The \$5 million tariff rider is supposed to combine with \$5 million in insurance proceeds to offset the first \$10 million in costs. Forcing current customers to pay \$5 million for 2013 in order to create a pool of \$10 million makes little sense when the 2013 costs were only \$6.8 million.

We note that Staff's public meeting memo discusses "offsetting" these 2013, 2014 and early 2015 tariff rider with a \$10 million credit. Current customers are being charged \$12.1 million for these previous tariff riders. There is no such thing as a free lunch and there is no such thing as a free offset. The \$10 million credit is compensation to current customers because NW Natural uses ratepayer assets for Mist Interstate Storage and Optimization and CUB has argued that customers are not fairly being compensated. The credit belongs to current customers, and using it to offset costs from 2013 and 2014 is the same thing as charging those costs to current customers -- except customers may not notice they are being charged. A lack of transparency is rarely considered good policy. Customers annually get a credit for Mist Storage and Optimization, and CUB strongly opposes the idea of turning this into a slush fund that the Company can propose be used for a purpose other than compensating customers for the use of customer-financed assets. If the Commission approves this, CUB believes that it is predictable that NW Natural will be back next year with a new proposal that it sincerely thinks will benefit everyone by using the Storage/Optimization credit for something other than compensating customers.

Rather than charging almost 2.5 years worth of past tariff riders to current customers, CUB believes it makes more sense to spread the costs out over a longer period of time. We note that is exactly what would happen if the make-up surcharge is not approved. The SRRM will amortize the costs over 5 years.

2013

Additionally, CUB notes that the Company is not applying this retroactive tariff rider and the insurance proceeds to the 2013 costs in a manner consistent with the Commission Order. In its Compliance Filing, the Company states:

On page 6 of the Order, the Commission found that NW Natural's environmental remediation costs from January 1, 2013 through March 31, 2014 were prudently incurred. In 2013, NW Natural recorded \$6.8 million of environmental spend. After the 2013 expenditures are offset by the \$5 million in base rates, \$1.8 million is left for which Insurance Proceeds will be applied. The \$3.2 million

remainder of Insurance Proceeds (\$5 million less \$1.8 million) will be carried forward to apply to 2014 spend.⁷

But this is inconsistent with the Compliance Filing's Exhibit B (see attached), which shows the mathematics behind the Company's Compliance Filing. According to Exhibit B, the 2013 remediation costs were \$6.8 million, which grew to \$8.19 million with interest. This is then offset by the \$5 million base rate adjustment, and further offset by \$1.8 million in insurance proceeds. The remaining \$1.4 million is transferred to the post-prudence SRRM and the remaining \$3.2 million in insurance proceeds are rolled forward to help cover next year's costs. CUB does not understand the basis of adding \$1.4 million to the SRRM balance after applying \$5 million of insurance proceeds and the \$5 million base rate adjustment to an amount that was only \$6.8 million. And if the amount needed for 2013 has grown, why is NW Natural only using \$1.8 million of insurance, and carrying \$3.2 million of insurance into 2014? CUB believes the Commission Order is clear—if the costs in a year are less than \$10 million, those costs are fully covered with amounts from the tariff rider and from insurance, with no costs being transferred to the SRRM.

3. Earnings Test Adjustment.

Order No 15-049.

Order 15-049 is prescriptive on its decision on its earnings test:

Exercising our discretion in a manner consistent with our regulatory duties, and in consideration of all of the issues discussed above, we reduce NW Natural's share of past costs to \$15 million. NW Natural will amortize the remaining \$29.2 million through its SRRM.⁸

And:

For existing deferrals, we apply \$50.2 million of the insurance proceeds to reduce the deferral balance to \$44.2 million. For this remaining balance, Commissioners Ackerman and Bloom determine that NW Natural should amortize in rates all but \$15 million of the deferral balance. Commissioner Savage dissents, and argues that the company should bear a higher amount.⁹

The math in the order is straightforward:

	\$94.4 million (starting number)
-	<u>50.2 million</u> (insurance)
=	44.2 million
-	<u>15.0 million</u> (earnings test disallowance)
=	29.2 million to SRRM

⁷ Advice Filing at 9.

⁸ Order at 18.

⁹ Order at 2.

NW Natural Compliance Filing.

NW Natural's Compliance Filing, however, used very different math (from Exhibit B):

$$\begin{aligned} & \$94.3 \text{ million (starting point)} \\ + & \quad \underline{17.9 \text{ million (interest)}} \\ = & \quad 112.3 \text{ million} \\ - & \quad 15.0 \text{ million (earning test disallowance)} \\ - & \quad \underline{48.2 \text{ million (insurance)}} \\ = & \quad 49.0 \text{ million to SRRM Post-Prudence} \end{aligned}$$

NW Natural then combines this \$49 million, with \$20.8 million from interest on insurance. This raises several issues. First, it is clear that the Order directed the Company to deduct the \$17.9 million from the \$94.3 million, not from the \$112.3 million. Second, it seems clear that the Commission ordered the Company to transfer \$29.2 million to the SRRM, not \$49 million. Third, the Commission divided the insurance proceeds into thirds. If there is interest, the interest should be accounted for after the division and should be equally applied to each third. Finally, on the same day it filed this compliance filing, the Company filed a motion for reconsideration that argued that the insurance proceeds had been subject to taxes and were reduced by \$38 million, but without disclosing that the insurance proceeds had also grown by \$20 million due to interest.

It is important to remember that what is happening here is happening as part of an earnings test. The purpose of an earnings test is to see if a cost can be absorbed by a utility at its current rates and still allow the utility a reasonable return. If the answer is yes, then there is no basis to surcharge customers for the cost. In essence, the cost was deemed already recovered under existing rates. The reason that the earnings test uses the same calendar year as the cost is to see if the cost could have been absorbed at the time it was incurred. And if a cost could be absorbed at the same time that it was incurred, then there is no basis for that cost to be recovered separately from customers. But key to this is that the costs are offset by earnings in the year they were incurred.

In this case, after contemplating a year-by-year earnings test, the Commission stated that it would reduce the deferral by \$15 million and the Company could move \$29.2 million to the SRRM. CUB feels the proper way to do this would have been to prorate the \$15 million across the years with overearning and offset \$15 million of costs with \$15 million of earnings which would have reduced the \$94.3 million deferred account by more than \$15 million because there would be no interest on the \$15 million since it was effectively recovered in the year it was incurred. But we recognize that is not what the Commission did. We read the Commission order as saying that before 2013, the Company had enough overearning to offset \$15 million of the \$94.3 million in the deferred account, and the remainder should be transferred to the SRRM. The \$15 million does not continue to earn interest, because it is deemed to have been recovered by 2013 with some of the prior overearning. The remainder of the deferral, which the Order identifies as \$29.2 million, is supposed to be placed into the SRRM where it will earn

interest at the SRRM interest rate. Somehow from this, NW Natural is finding authority to transfer \$49 million to the SRRM, which is \$20 million more than the Order direct states.

Conclusion.

NW Natural's Compliance Filing is not consistent with the Commission's Order in this case and should therefore be rejected.

Sincerely,

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
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Citizens' Utility Board of Oregon
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Exhibit B
 NW Natural
 Order 15-049 Compliance Filing
 Summary of Deferred Environmental Activity

	<u>Summary</u>
1 Interest on Environmental Insurance Receipt	(20,775,156) (line 10)
2 Pre-2013 Environmental Expense net of Adjustments	49,047,538 (line 18)
3 2013 Deferred Environmental Expense net of Adjustments	<u>1,368,313</u> (line 24)
5 Total Amount Transferred to Post-Prudence at 3/31/15	<u><u>29,640,694</u></u>

Interest Accruals on Insurance Receipts	<u>Interest on Insurance</u> (a)
6 2012 Interest Accrual	(3,319,623)
7 2013 Interest Accrual	(3,668,218)
8 2014 Interest Accrual	(10,608,925)
9 2015 Interest Accrual through 3/31/15	<u>(3,178,389)</u>
10 To Post-Prudence	<u><u>(20,775,156)</u></u>

Pre-2013 Vintage	<u>LTD 12/31/12</u>		
	<u>Expenditures</u> (a)	<u>Interest</u> (b)	<u>Total</u> (c)
11 Life-to-date @ 12/31/12	68,544,185	25,826,636	94,370,821
12 Interest on pre-2013 balances accrued 1/1/13 - 3/31/15		<u>17,892,930</u>	<u>17,892,930</u>
13 3/31/15 Balance	68,544,185	43,719,566	112,263,751
14 Disallowance			(15,000,000)
15 1/3 of insurance proceeds (Exhibit C line 7)			<u>(48,216,213)</u>
16 To Post-Prudence			<u><u>49,047,538</u></u>

2013 Vintage	<u>2013</u>		
	<u>Expenditures</u> (a)	<u>Interest</u> (b)	<u>Total</u> (c)
17 Current year cost - 2013	6,816,728	612,129	7,428,857
18 Interest on 2013 balances accrued 1/1/14 - 3/31/15		<u>756,183</u>	<u>756,183</u>
19 3/31/15 Balance	6,816,728	1,368,313	8,185,041
20 Application of Base Rate Adjustment			(5,000,000)
21 Application of Insurance			(1,816,728)
22 Note: \$1.8M is the remaining expenditures after application of the			
23 \$5M base rate adjustment			
24 To Post-Prudence			<u><u>1,368,313</u></u>