

**BEFORE THE PUBLIC UTILITY COMMISSION
OF OREGON**

UG 221

In the Matter of)	
)	CITIZENS' UTILITY BOARD
)	OF OREGON'S PRE-HEARING BRIEF
NORTHWEST NATURAL GAS COMPANY,)	
dba NW NATURAL)	
)	
<u>2011 General Rate Case</u>)	

I. CUB'S PREHEARING BRIEF.

In compliance with the "Notice of Pre-hearing Conference and Memorandum" issued by ALJ Hardie on August 1, 2012, the Citizens' Utility Board of Oregon ("CUB") hereby submits its Pre-hearing Brief. CUB will use this brief to both identify the settled issues, and to frame the unsettled issues that may be raised in cross-examination, in oral argument, or in post hearing briefs.

II. INTRODUCTION.

NW Natural filed its last General Rate Case in 2002 (UG 152).¹ The ROE set in UG 152 was 10.2 percent.² NW Natural has been consistently over-earning since that time. On December 30, 2011, NW Natural Gas Company ("NWN" or the "Company") filed an "Application for a General Rate Revision" with the Oregon Public Utility Commission ("OPUC"). This Application requests a residential rate increase equivalent to 10.5 percent for Schedule 1 Residential Customers and a residential rate increase of 8 percent for Schedule 2

1 UG 221/Staff/200 Johnson/2 line 6.

2 UG 221/Staff/900 Cimmiyotti/5 line 18.

Residential customers.³ The Company, in the worst economic downturn since the Great Depression, is requesting an increase of its ROE to 10.3 percent.⁴ The actual dollar increase requested is \$43.7 million.⁵ An increase of 6.2 percent over already high revenues from current customer rates.⁶ And this is not the only rate increase being requested in this docket by the Company. The Company is also proposing an environmental cost recovery mechanism that will, if approved, result in an additional increase to rates.⁷ The Company requested that this tariff increase become effective on or after February 1, 2012. On January 19, 2012, the Commission, in Commission Order 12-011, suspended the tariff sheets effective February 1, 2012 for a period not to exceed nine months.

According to the Company, the key factors driving its request for a rate adjustment are increases in O&M resulting from safety requirements, improvements to enhance its customer service, contributions to pension funds and cost control efforts.⁸ In addition, of course, to its proposals related to environmental remediation and rate design.⁹ As CUB sees it, the real driver behind this case is the Company's desire to protect its over-earnings by designing a regulatory structure that continues to support over-earning.

While good management practices undoubtedly contributed to the good earnings,¹⁰ much of the good earnings are the direct outcome of regulatory practices in Oregon. For example, by establishing a reasonable rate of return on rate base and then allowing the Company to retain a generous level of revenues associated with storage optimization generated by these rate based

3 UG 221/NWN/1701/King/Original Sheet 1-1 and 2-1.

4 UG 221/NWN/200/Anderson/21 line 16.

5 UG 221/NWN/300/McVay-Siores/3 lines 16-18.

6 UG 221/NWN/300/McVay-Siores/3 line 18.

7 UG 221/NWN/1500/Miller/3-18.

8 UG 221/NWN/Kantor/3 lines 11-17.

9 UG 221/NWN/Kantor/5 lines 5-7.

10 UG 221/NWN/1800/ Anderson/5 lines 9-10.

assets, Oregon guarantees that, under normalized conditions, NW Natural will earn above its rate of return. Another example is the use of automatic adjustment clauses rather than deferrals to recover costs that occur between rate cases – thus avoiding the earnings test associated with deferrals. But the earnings test exists for a reason: if the Company is over-earning at a level that allows it to recover the deferred cost, then ratepayers are paying rates that allow the Company to recover its costs and earn a reasonable rate of return. NW Natural’s use of automatic adjustment clauses allows for costs to be assigned to customers even when customers are already fully covering the Company’s costs and paying it a reasonable return. This is why NWN is so interested in adding additional automatic adjustment clauses for its environmental remediation costs. Another example is the Company’s position on its over-earning related to Pensions. As Staff points out in Staff/900, from 2004 to 2010, while the Company was accumulating \$12,923,909 in cash contributions to its pension in excess of its NPPC, the Company was at the same time earning \$20,048,000 in excess of their authorized 10.2 percent ROE.¹¹

In this case, the Company is trying to ensure that a regulatory structure that currently preserves structural over-earning remains intact. The Company has been unwilling to consider changes to the optimization sharing associated with current rate based assets and at the same time is unwilling to consider sharing of costs associated with environmental remediation that it is seeking to include as an additional rate based asset. Simply put, it is CUB’s position that the Company wants an additional automatic adjustment clause for environmental remediation, to ensure that customers also pay for those costs regardless of the Company’s over-earnings. And to top this off, the Company is also proposing that currently deferred environmental remediation costs, that are subject to an earnings test downward adjustment when amortized, be converted to

¹¹ UG 221/Staff/900/Cimmiyotti/6 lines 1-6.
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an automatic adjustment clause so no earnings test is applied. After years of over-earning NWN is still trying to act the part of a shrunken, under fed little Oliver Twist., “Please Sir, I want some more?”¹²

III. THE SETTLED ISSUES.

On July 9, 2012, after extensive discovery, testimony and negotiations, NW Natural Gas Company (“NWN” or the “Company”), Commission Staff (“Staff”), the Citizens’ Utility Board of Oregon (“CUB”) and the Northwest Industrial Gas Users (“NWIGU”) entered into a Partial Stipulation (the July Partial Stipulation). Northwest Energy Coalition (“NWECC”) participated in the settlement discussions and did not oppose the July Partial Stipulation but it was not a party to the July Partial Stipulation. A copy of the Stipulation is attached as Attachment A. Thereafter, on August 10, 2012, again after extensive discovery, testimony and negotiations, the parties reached a “Settlement In Principle” (the August Settlement In Principle) of the following additional issues.¹³ It is not known if it will be possible to complete the Stipulation prior to the date of Hearing but a copy of the letter is attached as Attachment B.

IV. THE UNSETTLED ISSUES.

Thanks to the July Partial Stipulation, and the August Settlement In Principle, the issues that remain to be addressed at hearing have been greatly reduced. Naturally, it is the most difficult to resolve issues that are now teed up for the Hearing and Briefing. The issues that remain unresolved are:

- Cost of Capital, excluding cost of debt.
- Hedging.
- Pensions.

¹² *Oliver Twist* by Charles Dickens, published by Richard Bentley in 1838.

¹³ Attachment B: Staff’s Letter Advising of Settlement in Principal of Several Issues.
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- Environmental Cost Recovery.
- Prudence of the Monmouth Reinforcement and Perrydale to Monmouth (two of the four sections of the Mid Willamette Valley Feeder).
- Rate spread related to environmental remediation surcharge, if any.
- State Taxes.

V. STANDARD OF REVIEW.

With the issues remaining to be addressed now identified, it is appropriate to consider the Standard of Review applicable to a General Rate Case filing. That Standard is discussed below.

A. NWN Bears the Burden to Show that Its Rates Are Fair, Just and Reasonable.

A review of ORS 756.040(1), ORS 757.210(1)(a) and UE 115, Order No. 01-777,¹⁴ demonstrates that NWN has the burden to show that its proposed rates are fair, just and reasonable.¹⁵ That means that the utility must show that the components that make up the costs in the proposed test year are reasonably certain to occur and are prudent.¹⁶

B. NWN Bears the Burden of Persuasion Throughout the Proceeding.

NWN bears the burden of persuasion throughout this rate case to show that its requested rate increase is reasonable. The Commission has directly addressed this issue, by saying:

We . . . affirm that, under ORS 757.210, the burden of showing that the proposed rate is just and reasonable is borne by the utility throughout the proceeding. Thus, if PGE makes a proposed change that is disputed by another party, PGE still has the burden to show, by a preponderance of the evidence, that the change is just and reasonable. If it fails to meet that burden, either because the opposing party presented compelling evidence in opposition to the proposal, or because PGE failed to present compelling information in the first place, then PGE does not

¹⁴ UE 115, Order No. 01-777 at 4- 6.

¹⁵ ORS 757.210(1); *Pacific Northwest Bell Tel. Co. v. Sabin*, 21 Or. App. 200,213-214 (1975). “Any increase in rates must be preceded by the submission of ‘revised schedules,’ and is dependent upon a showing by the utility that the proposed rates are ‘just and reasonable.’ *citing to* ORS 757.210.

¹⁶ UT 125/UT 80 Order No. 00-191 at 9 (quoting Order No. 97-171).

prevail.¹⁷

In OPUC Order No. 09-046, the Commission clarified that there are two aspects to the burden of proof – the burden of persuasion and the burden of production.¹⁸ Those aspects are distributed amongst the parties as follows:

The burden of *persuasion* in a deferral amortization case is always with the utility. The ultimate burden of *producing* enough evidence to support its claims is also with the utility. Other parties in the case, however, have the burden of *producing* evidence to support their argument in opposition to the utility's position.¹⁹

This application of the standard was further clarified in UE 228, when the Commission advised:

To reach a determination on whether proposed rates are just and reasonable, we look at the record as a whole and make a determination based on the preponderance of the evidence. Once a utility has met the initial burden of presenting evidence to support its request, “the burden of going forward then shifts to the party or parties who oppose including the costs in the utility’s revenue requirement.” Although the burden of *production* shifts, the burden of *persuasion* is always on the utility.²⁰

Given the above, it is clear that it is not CUB’s role to prove that the proposed cost is unreasonable or imprudent. Rather it is NWN’s role to prove that the proposed cost increase is reasonable and prudent. Bob Jenks’ and Gordon Feighner’s Testimony on behalf of CUB, and Hugh Larkin’s Testimony on behalf of NWIGU-CUB, address the remaining issues in this NWN General Rate Case and demonstrate why NWN’s has not met its burden of proof with regard to the outstanding issues. While the Commission may take CUB’s and CUB-NWIGU’s testimony and weigh it against the testimony presented by NWN, ultimately the Commission must be convinced that NWN has carried the burden of persuasion, of proving that its proposals are

17 UE 115 Order No. 01-777 at 6 (Aug. 31, 2001)

18 UE 196 Order No. 09-046 at 7.

19 UE 196 Order No. 09-046 at 7-8 (*emphasis added*).

20 UE 228 Order No. 11-432 (Nov 2, 2011)(*emphasis added*). See also *In Re Northwest Natural Gas Company*, Docket No. UG 132, Order No. 99-697 at 3 (Nov 12 1999) *In Re PGE, Application to Amortize the Boardman Deferral*, Docket No. UE 196, Order No. 09-046 at 7-8. Although the burden of production shifts, the burden of persuasion is always with the utility;

reasonable and prudent.

C. Reasonableness Is Based on Overall Rates, Not Each Adjustment.

The Commission is responsible for ensuring that NWN's customers are charged just and reasonable rates.²¹ As the PUC has noted previously:

[T]he validity of the determined rates rests on the reasonableness of the overall rates, not the theories or methodologies used or individual decisions made. As the United States Supreme Court explained in *Hope*, if the total effect of the rate order is not unjust and unreasonable, "[t]he fact that the method employed to reach that result may contain infirmities is not then important."²²

In short, as the courts have previously noted, ratemaking is, and should be, a holistic process.²³

In this proceeding many issues have already been settled leaving only a handful of thorny issues remaining. Each of these remaining thorny issues is individually important but so are the overall rates that will be imposed on customers. CUB encourages the Commission to look long and hard at the thorny issues and to then look long and hard at what its decisions will do to overall rates before finally ruling.

VI. APPLICATION OF THE STANDARD OF REVIEW TO THE UNSETTLED ISSUES IN THIS DOCKET.

1. Cost of Capital

NW Natural has had a decade of obvious, and extensive, over-earning.²⁴ It is time for the Commission to reset NW Natural's Cost of Capital. As stated in UE 115, a utility's revenue

21 ORS 756.040(1); *Pacific Northwest Bell Tel. Co.*, 21 Or. App. At 213.

22 DR 10. UE 88 & UM 989 at p. 7-8 citing to *Hope*, 320 US at 602. *See also* Morgan Stanley Capital Group, Inc. v. Public Util. Dst. No. 1 of Snohomish County, 554 US ___, 128 S Ct 2733, 2738, 171 L.Ed 2d 607 (2008)("We have repeatedly emphasized that the Commission is not bound to any one ratemaking formula.").

23 DR 10. UE 88 & 989 at p. 64.

24 *See* UG 221/CUB/200/Jenks-Feighner/3 lines 19-20; UG 221/Staff/200 Johnson/4 line 1 table.

requirement is determined on the basis of the utility's costs.²⁵ And in the revenue requirement phase of a rate case:

[T]he Commission must determine: (1) the gross utility revenues; (2) the utility's operating expenses to provide utility service; (3) the rate base on which a return should be earned; and (4) the rate of return to be applied to the rate base to establish the return to which the stockholders of the utility are reasonably entitled. *Pacific Northwest Bell Tel. Co. v. Sabin*, 21 Or App 200, 205 n. 4, rev den (1975) The purpose of answering these questions is to determine the utility's reasonable costs of providing service and expected revenues, so that the Commission can set utility rates at just and reasonable levels.²⁶

Much of the rate base has already been determined in the July Partial Stipulation and in the August Settlement in Principle. There are, however, two outstanding prudence questions related to two pipeline projects, Monmouth Reinforcement and Perrydale to Monmouth, that remain to be resolved before the Commission can determine the true size of the rate base. Also outstanding is the whole issue of environmental remediation cost recovery and pensions. Before we begin, however, CUB wishes to point out factors that have played into the Company's "extensive, and obvious over-earning."²⁷

NW Natural begins its Reply Testimony by trying to explain away its chronic over-earning by arguing that the Commission should not count any over-earning due to the PGA because WACOG "gains and losses are not predictable, not repeatable and are driven by issues beyond the Company's control."²⁸

A. The PGA, Storage and the WACOG.

CUB fundamentally disagrees with NW Natural's argument that the Commission should ignore any over-earning due to the PGA because WACOG "gains and losses are not predictable,

25 UE 115. Order No. 01-777 at 4 (Aug. 31, 2001)

26 UE 115, Order No. 01-0777 at 4 (Aug. 31 2001)

27 UG 221/CUB/200/Jenks-Feighner/3 lines 19-20.

28 UG 221/NWN/1800/Anderson/4, lines 10-11.

not repeatable and are driven by issues beyond the Company's control."²⁹ The PGA mechanism is part of Oregon's regulatory approach to natural gas utilities. NW Natural is able to use its storage—a rate based asset—to beat the WACOG and increase its earning. In other words, this is not “beyond the Company's control.”

In fact, during the last review of the PGA mechanism (UM 1286), NW Natural did not argue that this was “beyond the Company's control.” Instead, the Company argued that:

As mentioned above, NW Natural's strategic use of its storage capacity represents its primary tool in pursuing lowest cost gas and in managing volatility. And the Company's skill in managing that capacity has been judged by an independent evaluator to be “truly impressive.”³⁰

When the market price of gas is below the WACOG used to establish base rates in the PGA, NW Natural can buy from the market knowing that some of the difference between the WACOG and the market price will be retained as excess earnings.³¹ When the market price of gas is greater than the WACOG, NW Natural can lean on its storage gas and avoid the higher price market purchases.³² While NW Natural has limited market power, storage remains a tremendous tool that allows the Company to earn a return on its gas supply by using storage as an arbitrage opportunity and not simply for reliability purposes. These factors should be taken into account when looking holistically at where to set the Company's cost of capital.³³

²⁹ *Id.*

³⁰ UM 1286 – NW Natural Reply Comments, pg 11 (Jan. 28, 2008).

³¹ *See* UM 1286/CUB/100/Jenks/8.

³² *Id.*

³³ DR 10. UE 88 & 989 Order No. 08-487 at p. 64.

B. Oregon’s Regulatory System Allows NWN to Earn a Return on its Investment in Storage, Share the Savings this Causes in the PGA, Retain Over-earnings Caused by this Use of Storage in the PGA, and share in revenues generated by Commercial Use of rate-based storage.

To be clear, CUB is not arguing against a system that provides the Company an incentive to reduce costs. Customers also benefit when NW Natural uses its storage capacity to reduce its costs. But we also have to be honest. Oregon’s regulatory system allows NW Natural four opportunities to earn a return on its storage. First, it earns a rate of return on its invested rate base associated with storage. Second, when the Storage allows it to beat the WACOG in the PGA, the PGA sharing mechanism allows it to retain some of this savings. Third, when the Storage contributes to over-earning, the Company is allowed to retain most of that over-earning through the earnings sharing mechanism. Finally, the Company shares the revenues that are generated through its commercial optimization of rate based storage.

CUB further points out that the contract with Encana is rate based and the Company is also earning a return on the gas that it sells under that contract. Again these factors must also be taken into account when looking in a “holistic” fashion at where to peg the Company’s Cost of Capital.³⁴

Staff’s Opening Testimony was correct—NW Natural has been chronically over-earning, with an ROE above 11% in recent years.³⁵ This is not a rate case driven by a utility that needs higher rates to get its earning to reasonable levels. To the contrary, this is a rate case that NW Natural was forced into because of concerns over the levels of its over-earnings.

³⁴ DR 10. UE 88 & 989 Order No. 08-487 at p. 64.

³⁵ UG 221/Staff/200 Johnson/4 line 1 table.

C. Programs like Decoupling, SIP and WARM all reduce regulatory Lag

The Commission has authorized many mechanisms since the last NWN rate case in order to help the Company avoid regulatory lag.³⁶ Those mechanisms include Decoupling, WARM and SIP, which have each helped improve the Company's earnings even in a depressed economy.³⁷ All of these mechanisms have been stipulated to again in this rate case as set forth in the July Partial Stipulation and August Settlement In Principle. Each of these programs, subject to some tweaks, will continue after this rate case. Each program benefits the Company through reducing risk and regulatory lag. Specifically, SIP allows the Company to collect the return of and return on certain rate base items without having to file for rate recovery through a general rate case, which would entail thoroughly reviewing all the elements of costs and expenses or subjecting these costs to an earnings test associated with a deferral.³⁸ It is CUB's position that all of these mechanisms must be taken into consideration when determining the level of risk remaining to the Company and thus the appropriate ROE/ROR.

D. NWN's Request for 10.0% ROE is still too high.

As CUB pointed out in its Rebuttal Testimony, NW Natural's ROE witness, Dr. Hadaway, updated his analysis and concluded that a reasonable range for an ROE is 9.6% to 10.0%.³⁹ NW Natural, however, rejecting its own expert witness's analysis continued to ask for an ROE of 10.2%:

In Dr. Hadaway's updated analysis, the DCF range narrowed to 9.6 percent to 10.0 percent. In sponsoring this update, Dr. Hadaway testified that current market conditions also undermine the traditional assumption that the best cost of equity estimate for the rate effective period can be found in the most recent data. Considering this testimony, the Company decided to recommend a 10.2% ROE, a

36 UG 221/Staff/200 Johnson/3 lines 3-6.

37 UG 221/Staff/200 Johnson/3 lines 19-20.

38 UG 221/Staff/200 Johnson/3 lines 8-15.

39 UG 221/NWN/2100/Hadaway/2 lines 14-20; 20 lines 5-16.

number which acknowledges the results of Dr. Hadaway's updated analysis, but ultimately gives his original analysis more weight. In my opinion, Dr. Hadaway's original analysis more accurately estimates NW Natural's cost of equity in the rate effective period.⁴⁰

CUB pointed out that it could not remember a utility rejecting its own expert witnesses' analysis and asking for a higher ROE and noted that if its own witnesses' analysis could not support the Company's position, then it was not a tenable position.⁴¹ While NWN's Surrebuttal position of 10.0 percent is still too high, at least NWN is aware that its initial request was off the charts. CUB supports Staff's evolving position. Staff opened, in the current economic climate, at an ROE of 9.2.⁴² With further discovery and testimony Staff has now settled on a 9.4 percent ROE.^{43,44} CUB thinks this level of ROE is all that is appropriate. In addition, CUB agrees with Staff and the Company that a Capital Structure of 50 percent debt and 50 percent equity is appropriate.⁴⁵

As noted in UE 115, the United States Supreme Court established the standard for determining cost of capital allowance in utility rate-making proceedings:

[T]he return to the equity owner *should be commensurate with returns on investments in other enterprises having corresponding risks*. That return, moreover, should be sufficient to assure confidence in the financial integrity of the enterprise, so as to maintain its credit and to attract capital[.]⁴⁶

Based upon the above, Staff looked at and addressed the issue of what similarly situated utilities with corresponding risks were earning.⁴⁷ While recognizing that the Commission only,

40UG 221/ NWN/1800/Anderson/15.

41 UG 221/CUB/200/Jenks-Feighner/45 lines 8-23.

42 UG 221/Staff/1300/Storm/3 lines 8-9 and Staff/1300 Storm 53 lines 8-9 and 12-16.

43 UG 221/Staff/1600 Goodwin/2.

44 UG 221/Staff/1601 Goodwin/1; UG 221/Staff/2200/Storm/3 lines 10-11.

45 UG 221/Staff/2200/Storm/7 Table 1 with the exception of the long term cost of debt which was agreed to in the August Settlement in Principle.

46 UG 115, Order Number 01-0777 at 23, citing to *Federal Power Commission v. Hope Natural Gas Company*, 320 U.S. 591, 603 (1944)(*emphasis added*).

47 UG 221/Staff/1300/Storm/55 lines 5-14 and 56 lines 1-4 and 64 lines 11-14 and 65 lines 1-8.

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[W]ill continue to review ROEs authorized in other jurisdictions to help gauge the reasonableness of the cost of equity estimates derived from independent methodologies [and] will not . . . rely on such decision to base an ROE award for a utility . . .⁴⁸

It is CUB's position that once the cost of each NWN capital component is "estimated and weighted according to its percentage of total capitalization" and these "weighted costs of capital are combined to calculate [NWN's] overall cost of capital," the allowed rate of return on rate base should be 7.711 percent,^{49,50} and the ROE should be 9.4 percent⁵¹ which is in line with what is happening to gas utilities in other jurisdictions that have corresponding risks. And, as Staff notes when discussing its numbers, these numbers meet both the *Hope* and *Bluefield* standards as well as the requirement of ORS 756.040.⁵² The recommendations are consistent with establishing fair and reasonable rates that commensurate with the return on investments in other enterprises having corresponding risks and sufficient to assure confidence in the financial integrity of the utility, allowing the utility to main its credit and attract capital.⁵³

On the other hand, the Company's DCF model compared itself to several electric utilities.⁵⁴ The difference in ROE was the electrics averaged 10.3 percent whereas the gas averaged 9.3 percent.⁵⁵ These numbers do not commensurate with what other LDCs are earning.

In attempting to support the Company's new 10.0 percent ROE position, Mr. Hadaway states that his new DCF model currently indicates ROEs in the range of 9.4 percent to 10.1 percent.⁵⁶ He has now also looked at ROEs for LDCs around the country and reports that the

48 UG 115, Order Number 01-0777 at 34.

49 UG 115, Order Number 01-0777 at 23.

50 UG 221 Staff/100 Goodwin/9 11-12.

51 UG 221/Staff/2200/Storm/3 lines 10-11.

52 UG 221/Staff/1300/Storm/53 lines 14-15.

53 UG 221/Staff/1300/Storm/53 lines 14-20 and 54 Table 5.

54 UG 221/Staff/1300/Storm/67 lines 18-21 and 68 lines 1-7.

55 UG 221/Staff/1300/Storm/67 lines 18-21 and 68 lines 15-20.

56 UG 221/NWN/3200/Hadaway/3 lines 6-7.

most recent quarterly average for LDCs is 9.8 percent ROE.⁵⁷ But CUB finds neither of these statistics very persuasive in regard to the Company's requested 10.0 percent ROE since what they squarely evidence to CUB is that the Company's 10.0 percent ROE request is way too high. Mr. Hadaway attempts to discredit Mr. Storm's analysis by stating that it is inappropriate for him to attach his analytical approach to low GDP growth rate forecasts, "which are the product of the most severe economic downturn since the Depression of the 1930s, [and] can only produce abnormally low ROE estimates."⁵⁸ CUB finds this statement rather ironic. CUB thinks that NWN trying to obtain an abnormally high ROE percentage given the current economic turmoil and that it would be more appropriate for the Commission to set a rational ROE and allow the Company to come back in for another rate case should economic conditions finally change. Why should customers, who are suffering under the "most severe economic downturn since the Depression of the 1930s," continue to fund NWN's over-earning when they are struggling to pay their own bills and when the Company can come back in for a rate case anytime should economic conditions warrant a general rate case increase? Why would the Commission set a high ROE when even the Company agrees that the cost of capital has come down in recent years?⁵⁹

2. Hedging

Staff proposes that ratepayers and the Company share equally a financial hedging loss, removing half that amount from the Company's cost of long term debt. As noted by Staff, OPUC Order No. 07-032 deferred consideration of prudence regarding hedging actions taken

57 UG 221/NWN/3200/Hadaway/4 lines 3-6.

58 UG 221/NWN/3200/Hadaway/8 lines 14-18.

59 UG 221/NWN/2100/Hadaway/13 lines 18-19.

until rate recovery was requested.⁶⁰ Staff states that the hedge in question was imprudent because the Company did not conduct independent, unbiased analysis and due diligence prior to the Company making its decision to execute the hedge.⁶¹ CUB did not write on this issue but may participate in questioning related to this issue at hearing.

3. Rate Base Issues⁶² - Prudence of Monmouth Reinforcement and Perrydale to Monmouth (two sections of the Mid Willamette Valley Feeder)

As stated by Hugh Larkin, Jr. in his Direct Intervenor Testimony on behalf of NWIGU-CUB, to be included in rate base in the test year, a project must be prudent.⁶³ It must meet certain basic criteria. First, the investment must be in service in the test year; if the investment will be in service during the test year, the investment cost must be known and measurable and the benefit of the investment must be reflected in the test year as well (i.e., reduced O&M costs, increased efficiency).⁶⁴ Also the project must be used and useful pursuant to ORS 757.355(1).⁶⁵

The Mid Willamette Valley Feeder Project is made up of four distinct sections. Only two of those sections remain at issue (Monmouth Reinforcement and Perrydale to Monmouth). The issue in both cases is one of prudence for both sections of the Project. The Company claims that notwithstanding that the projects were included in the 2011 Modified IRP but not selected for the IRP Preferred Portfolio, that the projects were prudently begun and will be prudently completed during the test year and should thus be included in rate base.⁶⁶ As noted by the Company, Staff claims that the Company should not have developed the two projects on their current timeframe

60 OPUC Order No. 07-032.

61 UG/221/Staff/1200/Muldoon/4 lines 11-17 and at 13 - 16.

62 The Testimony of Moshrek Sohby has been adopted by Ken Zimmerman UG 221/Staff/1900/Zimmerman/4 lines 20 – 22.

63 UG 221 NWIGU-CUB/100/Larkin/5 lines 22-24.

64 UG 221 NWIGU-CUB/100/Larkin/5 lines 3-7.

65 UG 221 NWIGU-CUB/100/Larkin/5 lines 10-16.

66 UG 221/NWN/3300/Yoshihara/2 lines 14-16; UG 221/NWN/2200/Yoshihara/1 lines 20-21.

because the 2011 Modified IRP does not select the projects until the 2025-2026 timeframe at the earliest.⁶⁷ In response, the Company argues that the IRP Guidelines do not require the inclusion of distribution planning, that the projects are needed to enhance the reliability of the system, that a modeled service outage would show the need and that because they have to address bare steel anyway it is cost effective to do it all now.⁶⁸

While the July Partial Stipulation requires the Company to provide an attestation as to the in-service date for the Monmouth Reinforcement and Perrydale to Monmouth projects the July Partial Stipulation does not settle the issue of whether or not these two projects were prudently begun at this time. It is CUB's view that construction of these two projects was premature.

As detailed by Moshrek Sobhy in his Opening Testimony, the Company has failed to justify rate basing of portions of this project.⁶⁹ The Perrydale to Monmouth project investment expense was not prudently incurred for several reasons. First, while this project was included in the Company's Integrated Resource Plan ("IRP") analysis, the IRPs analysis did not choose the project for the current action plan.⁷⁰ Second, when you consider the negative growth projected in this proceeding, there is no validation for this project being completed at this time.⁷¹ And, third, because the Company's response to OPUC-DR-216 stated that the Company did not conduct a financial analysis of the investment for this project, the Company was not prudent in moving forward with this project at this time. The decision to invest was based on the system

67 UG 221/NWN/2200/Yoshihara/3 lines 1-4.

68 UG 221/NWN/2200/Yoshihara/4 lines 17-18; UG 221/NWN/3300/Yoshihara/3 lines 2-3; NWN/3300/Yoshihara/4 lines 6-8; and NWN/600/Yoshihara/5 line 23.

69 UG 221/1100 Sobhy/2-3.

70 UG 221/Staff/1100/Sobhy/10 lines 3-6; UG 221/Staff/1900/Zimmerman/5 lines 1-4 and lines 16-17.

71 UG 221/Staff/1100/Sobhy/13 lines 14-16.

reliability, replacement of legacy bare steel and system reinforcement.⁷² As Staff notes, this should ring additional alarm bells.⁷³

The Company memo dated August 24, 2011 identified the “rough estimated cost” for this project as \$13,300,000.⁷⁴ The response to the OPUC-DR-165 stated that all work would be performed by NW Natural crews.⁷⁵ Based on the above, the Company has failed to fully justify that the \$13,500,000 estimated project cost is a known and measureable expense. It is, therefore, CUB’s position that the Company has failed to meet its burden of proof to prove that these two segments of the MWVF project were prudently constructed at this time. CUB is requesting that the estimate for this project be removed from the test year. Staff concurs.⁷⁶ Staff, however, also offers the option that the Company can come back to the Commission at a later time and then attempt to prove that the projects are needed and will be used and useful when put into rates.⁷⁷ CUB also notes that the July Partial Stipulation provides that to the extent the Commission finds that such projects were prudent, parties have agreed that the lower of the forecast or actual costs of such projects, incurred as of the rate effective date, will be added to rate base for purposes of the Company's revenue requirement. Nothing in that paragraph of the July Partial Stipulation precludes the Company from filing a deferral application in the event that the Company believes it will incur additional costs related to a project after the rate effective date, or if the amounts that have been incurred or will be incurred by the rate effective date are greater than the amount included in the Company's original filing for that project and are eligible for deferral.

72 UG 221/Staff/1100/Sobhy/15 lines 16-18 and 16 lines 19-23 and 17 lines 1-8.

73 UG 221/Staff/1100/Sobhy/17 lines 8 – 11.

74 UG 221/NWIGU-CUB/100/Larkin/9 lines 5-6.

75 UG 221 NWIGU-CUB/100/Larkin/10 lines 4 – 9.

76 UG 221/Staff/1000 Zimmerman/4 lines 15-19; see also Staff/1002 pages 1-4; Staff/1002 pages 12-13; Staff/1003 pages 1-11; Staff/1003/Sobhy/1-2; UG 221/Staff/1900/Zimmerman/5 lines 19-23.

77 UG 221/Staff/1900/Zimmerman/6 lines 10-14.

Additionally, nothing precludes other Parties from taking any position (supporting or opposing) on the deferral application and application for amortization.

In terms of the Monmouth Reinforcement Project, CUB thinks that the project investment expense was not prudently incurred because the Company's response to OPUC-DR 216 stated that it did not conduct a financial analysis of the investment for this project.⁷⁸ As stated by Staff,

[T]he information provided by the Company does not support that ratepayers start paying the return of and return on the \$8.1 million investment in the Monmouth Reinforcement phase in November 2012 while the evidence shows that the project will not be needed until the year 2025.⁷⁹

Evidently, the Company's decision to invest, while not being based upon financial analysis, was based upon system reliability, replacement of legacy bare steel and system reinforcement. And a Company memo, dated August 12, 2011, identifies the "rough estimated cost" as \$7,500,000.⁸⁰ The Company's response to OPUC-DR 175 then identifies the project cost as \$8,100,000.⁸¹ And the Company's response to OPUC-DR 165 states that only a portion of the project was sent to bid and other portions of the project will be performed by NW company crews.⁸² That response provided a copy of the RFP issued by the Company on December 16, 2011 for Phase 1 of the Monmouth project.⁸³ An email provided in response to NWIGU-CUB DR 95, Attachment G-2, dated January 31, 2012, notified Brotherton Corporation as the contractor selected.⁸⁴ An Excel schedule titled "200580 Monmouth" listed amounts charged to various accounts totaling \$3,322,509.⁸⁵ The response to NWIGU-CUB DR 95 states the project is 15% complete.⁸⁶

78 See also UG 221/1100 Sobhy/3 lines 9-13.

79 UG 221/Staff/Sobhy/3 lines 17-21.

80 UG 221/NWIGU-CUB/100/Larkin/11 lines 1-2.

81 UG 221/NWIGU-CUB/100/Larkin/11 lines 2-3.

82 UG 221/NWIGU-CUB/100/Larkin/11 lines 3-5.

83 UG 221/NWIGU-CUB/100/Larkin/11 lines 5-7.

84 UG 221/NWIGU-CUB/100/Larkin/11 lines 8-10.

85 UG 221/NWIGU-CUB/100/Larkin/11 lines 14-15.

86 UG 221/NWIGU-CUB/100/Larkin/11 lines 15-16.

Clearly the Company has not fully justified the \$5,600,000 identified in the filing as known and measureable. The Company's estimate should be removed from the test year, less the amount identified in the confidential exhibit that CUB will present.⁸⁷

4. Operating Income – Out of Period Pension Costs

Given the rather complex history of pensions, CUB has decided to set down a primer of where things currently stand and then to explain what the Company is seeking that is different. The Company currently handles its pension expense in accordance with Order 03-057, which allows NW Natural to collect in rates approximately \$3.8 million annually in FAS 87 pension expense. Under that Order, NW Natural was also supposed to implement deferred accounting to provide customer credits in the event that the actual pension expenses were less than those that were agreed to in settlement. If they were greater, NW Natural could then file an application seeking deferral of those expenses.

- (1) The agreement in Order No. 03-057, however, was modified in docket UM 1475. OPUC Order No. 11-051 (UM 1475) allows the Company to establish a balancing account to track differences between its actual pension expense and the amount recovered in rates. The change was made because NW Natural was under-collecting from the rate allowed in Order 03-057, and the stipulating parties thought that pattern was going to continue. The expectation was that NW Natural's pension expense would decline after a few years and the balancing account amounts would ultimately turn negative and net to 0. Specifically, the agreement states, in relevant part, that: NW Natural will establish a balancing account effective January 1, 2011, for its FAS 87 pension expense. Beginning Jan. 1, 2011, and subject to an earnings test described in paragraph 3, the Company will book to the balancing account on a monthly basis all FAS 87 pension expense incurred by the Company, net of the amounts recovered in rates for FAS 87 pension expense, as stipulated in Order No. 03-507. Pursuant to Order No. 03-057, NW Natural is authorized to collect \$3,796,055 annually for FAS 87 pension expense.
- (2) The balancing account described in paragraph 1 will accrue interest at NW Natural's current authorized rate of return.
- (3) The Company will continue to book amounts to the balancing account and accrue interest as described in paragraphs 1 and 2 above until the balance in the account becomes negative. *After that time, amounts booked to the account will be subject to an earnings test as follows: to the extent that balancing account entries for the calendar year would*

⁸⁷ UG 221/NWIGU-CUB/100 Larkin 10 at lines 21-22 and 11 at lines 1-21.
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cause the company to experience earnings for that year in excess of its Commission-authorized return on equity, NW Natural must remove from the balancing account the amounts that would cause NW Natural to exceed its Commission authorized return on equity.

...

- (4) The balancing account will terminate upon the effective date of the tariffs filed in connection with the first general rate case submitted to the Commission after the balance of the FAS 87 pension expense balancing account becomes negative. The Company may not submit a request to amortize the balancing account balance prior to the termination date of the balancing account.
- (5) At the next general rate proceeding, any party may request that the Commission decrease the FAS 87 expense recovered in rates. *No party will request an increase in the FAS 87 pension expense recovered in rates to be effective prior to the termination of the balancing account.*
- (6) NW Natural is free to request its next rate case that the Commission give consideration to the effect of its pension contributions since the last rate case in setting the Company's capital structure.
- (7) NW Natural has included in its testimony filed in this case the estimated amount of capital contributions it expects to make to its pension accounts over the next several years. The Parties understand that these estimates are based on several assumptions—most notably, expected interest rates. Should actual interest rates or other pension results vary from the assumed levels, the contributions actually required may be higher or lower. The parties agree that this settlement assumes and the Company expressly agrees that the Company will make whatever capital contributions are required to maintain compliance with PPA requirements including the avoidance of benefit restrictions.
- (8) If, during the term of the balancing account, the Commission alters its policies regarding the recovery of pension expenses, the Parties agree to consider whether to alter the arrangement agreed to in this stipulation. In the event the parties cannot agree, NW Natural will be free to request that the Commission revisit the pension expense recovery agreed to in the stipulation.
- (9) The provision in Order No. 03-057 requiring the Company to defer for refund the difference between the actual expense and the rate case level of expense when the actual is lower than the rate case level should be eliminated.

In its current rate case, NW Natural is asking the Commission:

- (1) To continue to include the same annual amount for FAS 87 expense that was included in the 2002 Rate Case (\$3,796,000 allocated to Oregon), consistent with the agreement approved by the Commission in UM 1475.
- (2) Continue with the pension balancing account for annual differences between actual FAS 87 O&M expense and the amount included in rates from the 2002 rate case
- (3) Add to rate base the average unrecovered investor contribution during the Test Year, which is equal to approximately \$39.2 million pre-tax, and
- (4) Include in rates an annual recovery requirement for the return of unrecovered investor contributions amortized over 8 years; annualized amount estimated to be \$4.5 million.

The problem with requests three and four being made by the Company is that the Company did not file for a deferral of the monies that shareholders contributed between 2004 and 2011.

Therefore, it is asking the Commission to amortize into rates amounts that were not properly deferred. Such action by the Commission would constitute retroactive ratemaking.

Mr. Feltz's Reply Testimony claims to find it odd that NWIGU-CUB do not address the actual pension numbers being requested.⁸⁸ Mr. Feltz fails to understand that NWIGU-CUB are taking issue with whether the Company should be permitted to have a mechanism of any kind that adds unrecovered pension contributions to rate base regardless of the size of the actual numbers.⁸⁹

Staff details the Commission's past actions in reviewing pension funds in its Opening Testimony at Staff Exhibit/900. Staff notes that the Commission has relied on an actuarial calculation of the Company's Net Periodic Pension Costs (NPPC) since 1986 in determining the appropriate level of pension expense to be included in rates.⁹⁰ The NPPC is calculated as of December 31 of the previous year using the guidelines established by the Federal Accounting Standards board's (FASB) in their Financial Accounting Statement (FAS 87), "Employer Accounting for Pensions."

While an independent actuary is used to perform the calculation, the calculation must include the fair value of the plan, actual/estimated value of the plan, benefits paid, funding status, service costs, interest costs, expected return on assets, amortization of the transitions asset, amortization of prior service cost and recognition of gains or losses.⁹¹ As Staff notes, a major

88 UG 221/NWN/2000/Feltz/18 lines 12-15.

89 UG 221/NWIGU-CUB/200 Larkin 13 lines 14-21 and 15 lines 1-3.

90 UG 221/Staff/900/Cimmiyotti/3 lines 1-3.

91 UG 221/Staff/900/Cimmiyotti/3 lines 1-12.

benefit of relying on the NPPC is that it smoothes out the losses and gains so as to smooth out some of the market volatility associated with equity markets.⁹² Staff further notes that any deviation from FASB guidance would have to be initiated by the issuance of a new statement of financial accounting standard by FASB – this has not happened.⁹³

As detailed by Mr. Larkin in his Direct Testimony, the Company is proposing to add unrecovered pension plan contributions from investors to rate base.⁹⁴ Company witness Mr. Feltz states, in his Direct Testimony, that the Company has been required to pay cash contributions totaling \$57 million between 2009 and 2011 to its pension plans to meet requirements of the Pension Protection Act (PPA) passed in 2006 and the Company now proposes to recover this money by adding these contributions to rate base:

The Company proposes to add the average unrecovered investor contribution amount during the Test Year, estimated at \$21,929,876 net of deferred taxes, or \$36,549,793 pre-tax, to rate base...The Company proposes to amortize the pre-tax amount over eight years...The revenue requirement impact of this proposal is estimated to be \$4,568,724, or \$36,549,793 divided by eight years.⁹⁵

What Mr. Feltz is asking for is retroactive ratemaking.⁹⁶ If the Company truly believed special treatment should be allowed for the net excess contributions, the Company should have filed an application for deferral back in 2004.⁹⁷ It is CUB's position that this proposal is neither

92 UG 221/Staff/900/Cimmiyotti/3 lines 12 -16; UG 221/Staff/2100/Cimmiyotti/3 lines 6-19.

93 UG 221/Staff/900/Cimmiyotti/3 line 23 and 4 lines 1-2.

94 UG 221/NWN/2000/Feltz/25 lines 17 – 22 and 26 lines 1-2.

95 UG 221/NWN/400/Feltz/ 27-28.

96 UG 221/NWIGU-CUB/200/Larkin/15 lines 3-12.

97 UG 221/NWIGU-CUB/200/Larkin/15 lines 15-17; In Order No. 03-629, the Commission interpreted ORS 757.259(3) to mean that deferred accounts can only collect funds prospectively. Since then, the legislature has moved the language quoted by the Commission to ORS 757.259(4):

Finally, even if we can infer that URP would have invoked the catchall authorization, ORS 757.259(2)(e), the application still would have failed because deferred accounts can only collect funds prospectively. ORS 757.259(3) states, in part, "A deferral may be authorized for a period not to exceed 12 months beginning on or after the date of application.

beneficial nor equitable to ratepayers. These cash contributions were necessitated in large part by the country's current economic recession. Mr. Feltz acknowledges as much:

In 2008 and 2009, the equity and bond markets collapsed, which led to a significant decline in the value of the Plans' assets. The recession that followed also caused a significant reduction in interest rates to historic lows, which dramatically increased Plan liabilities.⁹⁸

As CUB and NWIGU's expert Hugh Larkin explains, the effect of the recession was to lower the value of the pension plan assets to the extent that FAS 87 and PPA regulations required further contributions from the Company.⁹⁹ As the market recovers, the value of the assets will rise and the additional contributions will no longer be necessary.¹⁰⁰ This is a temporary issue that should be corrected over time without adjustments to ratemaking procedures.¹⁰¹ Furthermore, according to Mr. Feltz, the Company made contributions between 2009 and 2011.¹⁰² Mr. Feltz argues that the pre-paid pension asset the Company is seeking to recover "was not an expense but rather an investment made by shareholders on behalf of customers and that the contributions are and will continue to provide benefits to our customers into the future. In that sense, the pension contributions are like plant investment and should be rolled into rates in each rate

Commission referred to the NW Natural's acknowledgement that the Commission could not approve a request to defer costs that could occur prior to the application date:

Since Northwest Natural's original application was filed on January 21, 2010, and the investigation related to the soil and ground water was completed prior to December 31, 2009, the Company acknowledges that the Commission cannot approve a request to defer the \$117,000 of costs that occur prior to the application date.

Clearly, NW Natural knows how and when to file for deferrals. Even if it were appropriate to defer and amortize the pension contributions at issue in this docket, NW Natural failed to make appropriate applications in regard to pensions.

98 UG 221/NWN/400/Feltz/23

99 UG 221/NWIGU-CUB/100/Larkin/48 lines 13-14.

100 UG 221/NWIGU-CUB/100/Larkin/48 lines 17-18.

101 UG 221/NWIGU-CUB/100/Larkin/48 lines 18-19.

102 UG 221/NWN/400/Feltz/24

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case.”¹⁰³ CUB disagrees. Pensions are definitely not like plant investments. There is no tangible asset (even Mr. Feltz acknowledges that fact¹⁰⁴), they cannot be said to be used and useful and there was no deferral, neither will they continue to provide benefits to customers. And to argue, without provision of any support, that the Commission has allowed other utilities to include prepaid assets to rate base - such as insurance premiums¹⁰⁵ – is an argument that deserves to be given no weight at all. The bottom line is that to now include past contributions in future rates would constitute retroactive ratemaking. Retroactive ratemaking is not an appropriate or acceptable practice in utility regulation.

Several Commissions have come to the conclusion that it is not appropriate for ratepayers to fund past pension contributions.¹⁰⁶ As one example, the Delaware Public Service Commission rejected Delmarva’s proposal to create a regulatory asset from its 2008 pension loss and amortize the asset over five years with rate base treatment of the unamortized balance due to the dramatic increase in 2009 pension expense resulting from the economic conditions outside of its control.¹⁰⁷ There was no deferral in place and the expense remained recorded as an expense on Delmarva’s books.¹⁰⁸ The Commission ruled that “[it] should not abandon the traditional ratemaking practice of including this expense in Delmarva’s cost of service,”¹⁰⁹ because “[u]nder accounting rules, Delmarva was required to receive approval in order to record the pension

103 UG 221/NWN/3100/Feltz/14 lines 19-21 and 15 lines 1-2.

104 UG 221/NWN/3100/Feltz/15 line 8.

105 UG 221/NWN/3100/Feltz/15 line 12-13.

106 *See Re: Appalachian Power Company*, Cause No. PUE-2011-00037, Final Order entered Nov. 30, 2011 (Nov. 30, 2011 Va. SCC) at 27; *Re: American Electric Power*, Case No. 10-0699-E-42T, Final Order entered Mar. 30, 2011 (WV PSC Mar. 30, 2011) at 38; *Re: Delmarva Power & Light Company*, Case No. 9192, Order No. 83085 (Md. PSC Dec. 30, 2009) at 15-16; *Re: Pepco*, DC No. 1076-E-480, Order No. 15710 (DC PSC Mar. 2, 2010) at 45-61.

107 *Re: Delmarva Power and Light Company*, Docket No. 09-414, Order No. 8011 at 48-60.

108 *Id.* at 49.

109 *Id.*

expense on its books as a regulatory asset.”¹¹⁰ The Commission also noted that “many of Delmarva’s customers suffered similar losses, but they have no place to turn to make them whole.”¹¹¹ The Commission specifically adopted the findings of the Hearing Examiner, which seem particularly applicable to the case at hand, in which she stated:

Further, the Company’s proposal in this instance gives me the unpleasant feeling that Delmarva believes its ratepayers should be its private insurance company. Whenever there is a financial downturn or an unfortunate economic event, the Company appears to believe the ratepayers should bail it out and make it whole. What Delmarva has experienced with the recent economic downturn is nothing more than the vicissitudes of business (as painful as that may be) that all companies in the United States are grappling with – nothing more. Although Delmarva’s ratepayers are captive customers; they are not hostages who should be required to open their wallets every time the Company suffers an economic setback.¹¹²

Even if the Commission authorized the deferral of future contributions, it is not appropriate for ratepayers to fund these past contributions. As Staff notes, to include some prior expense increases while not fully examining all expenses and revenues for their respective increases and decreases could lead to overstatement of expenses as well as an understatement of revenues and each time that occurred could result in a Company over-earning its authorized return on equity.¹¹³ Mr. Larkin recommends removing the unrecovered investor contribution of \$21,929,876 from rate base and removing the entire \$4,568,724 from amortizable expenses on an Oregon basis.^{114, 115} NWN is not Oliver Twist, and contrary to what the Company would have the Commission believe, the Company does not need any more.

From 2004 to 2010, while the Company was accumulating the \$12,923,909 in cash

110 *Id.* at 59.

111 *Id.* at 57.

112 *Id.* at 54.

113 UG 221/Staff/900 Cimmiyotti/5 lines 5-9.

114 UG 221/NWIGU-CUB/100 Larkin 47 lines 12-23, 48 lines 1 – 24, and 49 lines 1-6.

115 UG 221/NWIGU-CUB/200 Larkin 13 line 11 through page 16 line 17.

contributions to its pension, in excess of its NPPC and including the weighted cost of gas, the Company was at the same time earning \$20.048,000 in excess of its authorized 10.2 percent ROE. These excess earnings should have provided NWN the flexibility it needed to fund its pensions.¹¹⁶ Instead, NWN pocketed the over-earnings. .

CUB will argue that should the Commission approve NWN's request as proposed that the Commission will be opening the door to every other utility in town. This is the first time this pension issue has come to the Commission but it will certainly not be the last. It is important that this issue be thoroughly vetted now to ensure that other utilities who might think to make the same request will know what the answer will be.

CUB notes that Staff also requests that the Company's pension request be disallowed.¹¹⁷

5. Environmental Remediation/Cost Recovery

NW Natural is proposing that all costs that the Company determines to be related to the environmental remediation of former manufactured gas plants, which the Company or its predecessors operated, should be deferred and collected from ratepayers through a separate mechanism that would amortize deferred amounts through a temporary adjustment set each year during the PGA.¹¹⁸

In addition to the remediation costs discussed above, NWN also wants recovery of the \$11 million to \$30 million it anticipates it will cost to construct a pumping station at the GASCO site, but the Company does not want the same recovery mechanism applied there. Instead, it states that, "the pumping station involves the construction of utility plant that will be operated over a long period of time. Such plant is normally added to rate base, and amortized over the life

116 UG 221/Staff/900/Cimmiyotti/6 lines 1-6.

117 UG 221/Staff/900/Cimmiyotti/2 lines 1-21; see also Staff/902 Cimmiyotti/1.

118 UG 221/NWIGU-CUB/100 Larkin 49 lines 10-13; NWIGU/100 Schoenbeck 13 lines 4- 21.

of the plant.”¹¹⁹ NWN notes, however, that if the Commission decides not to add these costs to rate base, that they should then be treated like the other SRRM expenses.¹²⁰ The requested pumping station at the GASCO site also constitutes environmental remediation for gas supply that is no longer used and useful. This site is no different than the other environmental costs. However, if the Commission agrees with the Company that this pumping station is an asset appropriately added to rate base over its useful life, then it is irrelevant to this case because the pumping station has yet to be built. As such, the Company is essentially asking the Commission to pre-approve a rate base item before it is used and useful.

Northwest Natural argues for these mechanisms notwithstanding the fact that it has insurance policies which should cover all of its costs¹²¹ that it has filed suit to enforce these policies¹²², and notwithstanding the fact that both the United States Environmental Protection Agency ("EPA"), and the Oregon Department of Environmental Quality ("DEQ"), have previously held the owner of the land responsible for the environmental remediation and not its customers.¹²³ This would be true whether the Company was a regulated company such as NW Natural or an unregulated company subject to competitive pricing.¹²⁴ This all goes to show that any cost, subject to earning a return, is not known at this time.¹²⁵ Any proceeds that the

119 UG 221/NWN/1500/Miller/19 lines 10-12.

120 UG 221/NWN 1500/Miller/19 lines 18-20.

¹²¹ UG 221/NWN/1400/Hart/3 lines 13-15. “Based on the language of its policies, controlling Oregon law and the underlying facts, NW Natural believes that each of its historical policies provide coverage for the costs related to the environmental damage that NW Natural is investigating and remediating.”

122 UG 221/NWN/1400/Hart/4 lines 9 – 19’ UG 221/NWN/1401/Hart/1-18.

123 UG 221/NWIGU-CUB/100/Larkin/50 lines 9-11.

124 UG 221/NWIGU-CUB/100 Larkin 50 lines 9 – 13.

125 The Company has not provided specific proposed charges for the rate schedules it proposes. Based on assumptions in the Company provided illustration Mr. Schoenbeck estimate that the Company proposal would recover about \$11.5 million per year over the first three years of operation from Oregon customers. Taken together, these estimates suggest an annual cost recovery of about \$15 million per year from the two proposed rate schedules.

UG 221/NWIGU/100 Schoenbeck 14 lines 4 – 14.

Company receives from insurance payments could, and should, reduce the cost significantly.^{126,127}

It is, and always has been, clear that the responsibility for remediation should flow to those who had responsibility for whatever pollutants were deposited on the land during its use by its owner.¹²⁸ In a competitive environment, owners of property who are required to make remediation investments cannot recover those costs automatically from their customers.¹²⁹ Owners of the land that was used in a manner which caused environmental damage are held responsible by the EPA and DEQ.¹³⁰ This is so because these owners are the ones who profited from the use of the land and were the only ones who could have affected the level of environmental damage incurred.¹³¹ Ratepayers never owned or operated the facilities which resulted in the environmental damage. They had no knowledge or input into the operation of these facilities. They were merely consumers of services without any control or knowledge of the possible effects on the environment of the operations taking place on these sites.^{132, 133} As for today's customers, the ones NW Natural is asking to pay for these costs, many were not even born when these facilities were in operation.

Notwithstanding all of the above, the Company's proposal would continue to defer costs that the Company determines are related to the environmental remediation of these properties to a deferred account. The Company would earn a full rate of return on these deferred funds during

126 UG 221/NWIGU-CUB/100/Larkin 52 lines 20-21.

127 The Company is seeking 100 percent recovery of all prudently incurred expenditures offset by any third parties contributions. UG 221/NWIGU/100 Schoenbeck 13 lines 12-13.

128 UG 221/NWIGU-CUB/200/Larkin/25 lines 16-21.

129 UG 221/NWIGU-CUB/100/Larkin/50 lines 15-17.

130 UG 221/NWIGU-CUB/100/Larkin/50 lines 17-18.

131 UG 221/NWIGU-CUB/100/Larkin/50 lines 18-20.

132 UG 221/NWIGU-CUB/100/Larkin/51 lines 1-4.

133 UG 221/NWIGU-CUB/200/Larkin/25 lines 13 – 21.

the period that they remained in the deferred account.¹³⁴ However, the Company avoids an earnings test on the amounts deferred by having them convert to an automatic adjustment clause, called “Site Remediation Recovery Mechanism,” which would take the balance in the deferred account at a specific date and remove one fifth of it for recovery through the mechanism proposed by the Company. That amount would then be subject to a prudence review by the Commission each year, but would notably not be subject to an earnings test. During the 12-month period that the recovery amount is being amortized through rates, the Company would collect a Modified Blended Treasury Rate (“MBTR”) on the balance being recovered through the mechanism.¹³⁵ The Company would still continue to earn a full rate of return on the balance reflected in the deferred remediation cost account during the period that amounts are being amortized and collected from ratepayers.¹³⁶

So to put numbers to this, as of September 30, 2011, the Company has deferred \$64.5 million in environmental costs (\$51.8 million in expenditures, \$18.1 million in interest, which have been offset by \$5.4 million expensed in prior years).¹³⁷ Going forward, the Company conservatively estimates that it will incur an additional \$58 million and likely more.¹³⁸ Currently the Company has recorded a \$122.5 million regulatory asset related to environmental costs (all MPG except \$1.1 million).¹³⁹ The proposed Rate Adjustment Mechanism would allow the Company to recover prudently incurred costs on a rolling basis, adjusted for future costs and receipt of insurance proceeds. It proposes to begin collecting in 2012 amounts already spent and deferred; ongoing costs would be collected until 5 years after the year in which the last

134 UG 221/NWIGU-CUB/100/Larkin/49 lines 15-18.

135 UG 221/NWIGU-CUB/100/Larkin 49 line 22 to 50 line 3.

136 UG 221/NWIGU-CUB/100/Larkin/50 lines 4-7.

137 UG 221/NWN/1500 Miller/2 lines 13-16.

138 UG 221/NWN/1300/Wyatt/17 lines 4-10; UG 221/1500 Miller/2 lines 19-20.

139 UG 221/1500 Miller/3 lines 1-4.

remediation costs were incurred.¹⁴⁰ Each year, 1/5 of deferred expenses (offset by insurance proceeds) would be put into a “Site Remediation Recovery Mechanism” (“SRRM”) for amortization during Nov. 1 through Oct. 31st period subject to a prudence review during the PGA. Any over/under collection would be retained and used to adjust subsequent periods.¹⁴¹ Each class would pay equal to the percentage of margin.¹⁴² The Company proposes to recover the costs of financing (a mixture of debt and equity) until amounts are collected from customers and therefore proposes that its authorized ROR be used to establish those financing costs for amounts remaining in the deferred account. For costs transferred to the SRRM, the Company would collect the Modified Blended Treasury Rate established in Order No. 08-263 as financing costs on the amounts being amortized that year.¹⁴³ If the Company were to receive insurance proceeds that would result in a negative SRRM balance, customers would receive a refund of 1/5 the negative amount in the SRRM account in the PGA year following the establishment of the account as a negative value.¹⁴⁴ The Company states that the Commission could determine that it would make more sense to apply the negative balance to subsequent years, or continue payment at a specific level to mitigate upcoming expenses.¹⁴⁵ The Company will allocate to its WA customers as well.¹⁴⁶

A careful review of the Company’s Reply Testimony evidences that the Company is proposing that the SRRM will be an automatic adjustment clause into which remediation costs will flow without an earnings test.¹⁴⁷ CUB does not agree that it is appropriate to convert

140 UG 221/NWN/1500 Miller/8 lines 18- 22 and 9 lines 1-4

141 UG 221/NWN/1500 Miller/9 lines lines 6-14.

142 UG 221/NWN/1500 Miller/11 lines 16- 17.

143 UG 221/NWN/1500 Miller/12 lines 16- 22 and 13 lines 1-3.

144 UG 221/NWN/1500 Miller/13 lines 4- 8.

145 UG 221/NWN/1500 Miller/13 lines 12- 16.

146 UG 221/NWN/1500 Miller/15 lines 20- 21.

147 UG 221/NWN/2600/Miller/18 lines 17 – 20 and 19 lines 1-7.

currently deferred costs into an automatic adjustment clause without an earnings test. All deferred costs are subject to an earnings test. The earnings test exists for a reason: if the Company is over-earning at a level that allows it to recover the deferred cost, then ratepayers are paying rates that allow the Company to recover its costs and earn a reasonable rate of return. NW Natural's use of automatic adjustment clauses allows for costs to be assigned to customers even when customers are already fully covering the Company's costs and paying it a reasonable return. This proposal is not equitable. This proposal illustrates the Company's apparent desire to protect its over-earnings through the rate basing of additional assets in order to ensure even more over-earning for shareholders at the expense of customers – the stark truth of this statement is evident when one considers the fact that NWN already has insurance policies to cover all of these costs but still wants to hold customers on the hook. As with regulatory lag, the Company does not want to be the one to wait with its hand outstretched. NW Natural wants current ratepayers to be held responsible for costs associated with providing *manufactured gas* decades ago to a group of unknown and unrelated ratepayers. Costs that are not in any way related to the provision of gas today, but are instead incurred by the Company because of its continued ownership of pieces of property.^{148, 149, 150,151}

And, contrary to the arrangements in several other states, NW Natural does not want shareholders to share in any of the costs of remediation.¹⁵² NW Natural claims that designing a mechanism that requires shareholders to bear the costs of “prudently incurred utility expenses” would undercut investors’ “reasonable expectations, and would undermine the regulatory

148 UG 221/NWIGU-CUB/100/Larkin/51 lines 6-11.

149 UG 221/NWIGU-CUB/200 Larkin/19 – page 28 line 6.

150 UG 221/NWIGU-CUB/200/Larkin/29 lines 1-10.

151 UG 221/NWIGU-CUB/200/Larkin/32 lines 7 – 13.

152 UG 221/NWN/1500 Miller/17 lines 12- 15.

compact, which gives a utility an opportunity to earn its regulated rate of return if it manages well.”¹⁵³ NW Natural would have the Commission believe that the current trend is to impose the entire cost of remediation on customers¹⁵⁴ when in fact several other state commissions have required a sharing of the costs, and in some cases, have even held that customers should not have to pay any costs.¹⁵⁵ NW Natural’s big concession to customers would be letting them have a longer time to pay all the costs so as to spread the burden over time.¹⁵⁶

CUB also notes that NWN makes several references in its testimony to how no one is challenging whether these costs are in fact prudent. This misstates CUB’s position. The Company is only entitled to recovery of prudent costs incurred for serving *current* customers. The costs at issue here were incurred because of ancient manufacturing practices and do not relate in any way to provision of service to *current* customers. Today’s customers did not benefit in any way from the manufacturing of gas, or the sale of MGP byproducts. And, they also did not cause the environmental damage that needs to be remediated and which has nothing to do with today’s distribution of gas.¹⁵⁷ In addition, CUB notes that when the Company receives a return on equity from its investments, that return reflects a risk factor. There are risks associated with the operation of any business, both competitive and regulated.¹⁵⁸ The equity return reflects a risk factor associated with the operation of a business.¹⁵⁹ This risk factor is related to unknown factors such as the assessment by the environmental agencies of remediation costs against the owners of the land which was contaminated.¹⁶⁰ Even though a regulated entity

153 UG 221/NWN/1500 Miller/17 lines 21-22 and 18 lines 1- 2.

154 UG 221/NWN/3700/Miller 5 lines 18- 21.

155 UG 221/NWN/1500/Miller/6, FN 5.

156 UG 221/NWN/1500/Miller/8 lines 9-10.

157 UG 221/NWIGU-CUB/200/Larkin/32 lines 7-13.

158 UG 221/NWIGU-CUB/100/Larkin/51 lines 15-16.

159 UG 221/NWIGU-CUB/100/Larkin/51 lines 16-17.

160 UG 221/NWIGU-CUB/100/Larkin/51 lines 17-19.

has substantially less risk than a competitive company, the return it receives still reflects a component related to risk, otherwise it would receive a return on its investment somewhat closer to government bonds.¹⁶¹ In the case of contaminated property, only the Company's management, who were employed by the shareholders, could have affected the outcome of the initial contamination of this property.¹⁶² The owners and operators of these facilities should have been, or could have been, aware that by-products were either being dumped or stored on site and only they could have affected the amount and type of contamination done to these properties.¹⁶³ It seems apparent that the Company's management accepted the risk from the operation of manufactured gas plants that was reflected in the rate of return that they received.^{164,}

It is likely not appropriate for ratepayers to bear any of the cost of remediation for these contaminated sites¹⁶⁵ and it is certainly not appropriate for ratepayers to bear the full cost of the remediation¹⁶⁶ and have the Company earn a full rate of return on those costs until they are reflected in the Company's proposed recovery mechanism.¹⁶⁷ The Company's argument that customers should pay for past contamination would be a real departure from the regulatory compact.¹⁶⁸ Utility companies accept a rate of return as part of the regulatory compact which includes compensation for unknown risks of running a utility. If it was not for this, utilities' rates of return would be the same as government securities.¹⁶⁹

161 UG 221/NWIGU-CUB/100/Larkin/51 lines 19-22.

162 UG 221/NWIGU-CUB/100/Larkin/51 line 22 to 52 line 2.

163 UG 221/NWIGU-CUB/100/Larkin/52 lines 2-5.

164 UG 221/NWIGU-CUB/100/Larkin/52 lines 5-7.

165 UG 221/NWIGU-CUB/200/Larkin/32 lines 1-6.

166 UG 221/NWIGU-CUB/200/Larkin 30 lines 13 – page 31 line 27.

167 UG 221/NWIGU-CUB/100/Larkin 52 lines 10-12.

168 UG 221/NWIGU-CUB/200/Larkin 27 lines 19-24.

169 UG 221/NWIGU-CUB/200/Larkin 28 lines 14-17.

Staff, contrary to the position of CUB and NWIGU, would accept a 90/10 sharing with shareholders with customers paying the 90 percent.¹⁷⁰ Staff's proposal is subject to an earnings test and would limit the amount to three percent of NWN's revenues for the preceding year.¹⁷¹ Staff also recommends to the Commission that on deferred accounts going forward, the Commission would agree to allow cost recovery subject to a prudence review and an earnings review.¹⁷² This being the case, Staff says it would only be appropriate to charge ratepayers the modified blended treasury rate as interest versus the Company's authorized ROE.¹⁷³ CUB does not think Staff's proposal is fair to customers or that it places enough risk and incentive upon the Company to appropriately manage its remediation costs while at the same time maximizing proceeds.

CUB's evidence demonstrates, as does Staff's, that in the cases it has reviewed, in regard to the subject of environmental cost recovery, some level of sharing was authorized, and that in at least one state, the utility's shareholders were directed to pick up all of the costs.¹⁷⁴

NWN's arguments that it will suffer grave financial consequences as a result of the NWIGU-CUB proposals have no merit.¹⁷⁵ Utilities cannot recover imprudent costs; this does not increase their risk. Imprudent costs are never recoverable.¹⁷⁶

CUB recommends that the Commission allocate 50 percent of the total environmental remediation costs to shareholders.¹⁷⁷ In addition, the Company should only earn a debt rate of

170 UG 221/Staff/200/Johnson/7 lines 16-17.

171 UG 221/Staff/200/Johnson/7 lines 18-23.

172 UG 221/Staff/200/Johnson/8 lines 1-6.

173 UG 221/Staff/200/Johnson/8 lines 4-6.

174 UG 221/Staff/200 Johnson/11 lines 23; Staff Exhibit 202 pages 12-15; UG 221/NWIGU-CUB/200 Larkin 30 lines 12 – 22 and 31 lines 1-27; UG 221 NWIGU-CUB/200 Larkin 32 lines 1-6.

175 UG 221/NWIGU-CUB/200/Larkin/27 lines 12-18.

176 UG 221/NWIGU-CUB/200/Larkin/30 lines 11-12.

177 UG 221/NWIGU-CUB/100/52 lines 23-24.

return on the balance reflected in the Deferred Environmental Cost Account.¹⁷⁸ Once the Commission has issued an order stating what amount NW Natural would recover as a reimbursement for environmental remediation costs, that amount would be a guaranteed recovery amount.¹⁷⁹ There would be no risk associated with the recovery of this amount by the Company, and therefore no equity investment would be necessary.¹⁸⁰ The Commission's Order would guarantee the return of the environmental remediation costs and therefore only a debt return should be recovered by the Company, because no risk would be involved in the recovery of the authorized amount.¹⁸¹

In addition NWN offers some new ideas. The Company notes that it would be agreeable to participation in a follow-up docket in the future once there is clarity on the total amount it will owe. In such a proceeding, the Commission could set timelines for completion of work and an incentive mechanism to help NWN achieve those targets. But NWN notes that this option is in addition to and not in place of what it is asking for in this case. It also states that if the Commission will give it its requested carrying costs, then it would be willing to decrease the portion of the deferral balance that is amortized each year under its proposed SRRM and would accept a modification from one-fifth to one seventh of the balance. CUB finds nothing of interest in either of these suggestions other than to note that they are further proof of the Company's attempts to maintain its over-earning.

178 UG 221/NWIGU-CUB/100/52 lines 24-25.

179 UG 221/NWIGU-CUB/200/Larkin/30, lines 2-4

180 UG 221/NWIGU-CUB/200/Larkin 30 lines 2-7.

181 UG 221/NWIGU-CUB/100/53 lines 3-4

CUB notes, as one final piece related to environmental cost recovery that NWIGU has weighed in on the issue of rate spread related to these costs and that it argues that rather than allocate these costs of the basis of equal percentage of margin, the Commission should use “the Company’s base rate spread proposal” which assigns less of these costs to large industrial users.¹⁸² Typically cost allocation follows some level of cost causality – customers who cause a cost, should pay for it. But in this case, none of the current customers, residential or industrial caused these costs to be incurred. These costs derive from gas that was manufactured decades ago. The Company’s cost allocation between Washington and Oregon, is based on the volume of gas supplied to each state:

The Company believes that around 3.32 percent of its costs of remediation related to Gasco should be allocated to Washington customers. This percentage is the Company’s best estimate of the percentage of gas from the Gasco facility that was sold to Washington customer during the period from 1913 through 1956, when the plant ceased operations.¹⁸³

The Company’s proposal is to allocate costs between states based on gas usage during the time, GASCO was in operation and to allocate the Oregon costs between customer classes based on equal percent of margin, which excludes gas commodity costs. Because this is a commodity-related cost, traditional cost allocation principles would suggest that it should be allocated to customers based on the marginal cost of gas supply, not the cost of everything but the gas supply as the Company is proposing. But, of course, traditional cost allocation principles, assume that this cost is related to current service, not service that was provide more than 50 years ago. CUB does not believe there is a fair way to distribute these historic costs to current customers consistent with principles of cost-causality. Given there is no fair way to allocate the costs, CUB

182 UG-221/NWIGU/100\Schoenbeck 15

183 UG 221/NWN/1500/Miller/15, lines 20-22, 16, lines 1-2.

recommends that the Commission accept NW Natural's proposal because it ensures that all customers contribute to this cost recovery on a proportional basis.

6. Amortization of Out of Period State Tax Change – Deferred Taxes

In 2009, the State of Oregon increased its state tax rate from 6.6% to 7.9%.¹⁸⁴ As a result of the tax change, the Company recorded a regulatory asset of \$5,834,389.¹⁸⁵ In 2010, the state tax rate decreased from 7.9% to 7.6%.¹⁸⁶ The incremental change as a result of this was \$1,354,558.¹⁸⁷ The net of these two items is \$4,479,831, which the Company is proposing to amortize over five years and has reflected as a decrease of \$895,966 to miscellaneous revenues in the test year.¹⁸⁸ However, Data Request OPUC-DR 305 asked the Company why it reflected this adjustment as an offset to miscellaneous revenues. The Company's response stated:

Typically, an amortization of a revenue-related deferred account would appear in the rate adjustments area of our income statement, and would offset the billing effect coming through in revenues. In addition, typical amortizations would be considered during the PGA each year. This issue was set for consideration in a general rate case. In a general rate case, the rate adjustment section is not typically shown, so the amortization is needed as a reduction to miscellaneous revenue to generate the revenue requirement needed to ensure the amortization of the account.¹⁸⁹

Ms. Soires, on behalf of the Company, states that, “the Company does not believe that it was required to file for a deferral order in order to update its deferred tax balances, or to collect, through rates, tax expenses that would be appropriate in light of its appropriate deferred tax balance.”¹⁹⁰ The Company argues that the Commission has endorsed changes like this in prior

184 UG 221/NWIGU-CUB/100/Larkin/27 line 19.

185 UG 221/NWIGU-CUB/100/Larkin/27 lines 19-20.

186 UG 221/NWIGU-CUB/100/Larkin/27 line 21

187 UG 221/NWIGU-CUB/100/Larkin/27 line 21 to 28 line 1.

188 UG 221/NWIGU-CUB/100/Larkin/28 lines 1-3.

189 UG 221/NWIGU-CUB/100/Larkin/28 lines 6-17.

190 UG 221/NWN/3000/Soires/16/lines 8-11.

dockets and cites for support UM 55 (sic). But the facts in UG 55 were very different and the docket was resolved by a Stipulation and cannot, therefore, provide precedent here – NW Natural admits as much while continuing to push its argument.¹⁹¹ CUB strongly disagrees with the Company. Here, the Company did not have an Order from the Commission giving it the right to record the tax balance in question as a regulatory asset in 2009.¹⁹² NW Natural failed to submit an application so no other party could examine this regulatory asset and object to this regulatory asset prior to the Company requesting to recover on it in this rate case.¹⁹³ What the Company “believes” is of no import here. A utility cannot “update” a deferred tax balance if it has not filed for a deferral in the first place. The Company, therefore, has no legitimate basis on which to bring this issue before the Commission in this rate case.

Furthermore, this is an example of single issue ratemaking, where the Company has singled out an item and is requesting special cost recovery for this item.¹⁹⁴ The Company could have petitioned the Commission to issue an Accounting Order regarding the treatment of this issue when it occurred.¹⁹⁵ It is not appropriate to now set aside this one single issue for future recovery. The Company should not be permitted to single out and charge ratepayers for this effect of the state tax change, which may have occurred during a period when the Company was otherwise earning a reasonable return.¹⁹⁶

This is also an example of retroactive ratemaking, and to state otherwise “flies in the face of common sense.”^{197, 198} All Cost of Service components, i.e., revenues, expenses, and cost of

191 UG 221/NWN/1900/Soires/28 lines 5-19.

192 UG 221/NWIGU-CUB/200 Larkin/2 lines 6-8; ORS 757.259(2)(e).

193 UG 221/NWIGU-CUB/200 Larkin/3 lines 7- 10.

194 UG 221/NWIGU-CUB/200 Larkin/7 lines 8-21 and 8 lines 1-20 and 9 lines 1-12.

195 UG 221/NWIGU-CUB/100/Larkin/28 lines 20-21; *See also* UG 221/Staff/1800/Garcia/11 lines 14-16.

196 UG 221/Staff/1800/Garcia/12 lines 8- 9.

197 UG 221/NWIGU-CUB/200 Larkin 3 lines 12-14.

198 UG 221/NWIGU-CUB/200 Larkin 10 lines 11 – 22 and 11 lines 1-2.

capital, change over time. However, contrary to arguments by the Company the "matching principle" dictates that all of the cost of service components should be considered and evaluated in relation to the specific test year.¹⁹⁹ That is why a test year is chosen and utilized, so that a proper relationship is established between revenues, expenses, and the cost of capital.²⁰⁰ The Company, however, claims that because deferred tax balances reflect timing differences that the tax balances pertain to future expectations of taxes due.²⁰¹ And on this basis the Company is requesting that current ratepayers fund the cost for an event which occurred in a prior period outside the test year.²⁰² The adjustment that the Company made on its books was to adjust deferred taxes for 2007 and 2008 as a result of these state tax rate changes.²⁰³ This is clearly retroactive ratemaking, which is a violation of ratemaking principles, and should be disallowed.

The Company also tries to legitimize this regulatory asset by claiming that it meets the requirements of Statement of Financial Accounting Standards No. 109, Accounting for Income Taxes ("FAS 109") and a Commission-approved stipulation in 1986 but neither of these items provides a legitimate basis on which to establish a regulatory asset related to tax rate change in 2009.²⁰⁴ And we also point out that the Company cannot claim to have paid any increased state tax as a result of the change in the 2009 state tax rate.²⁰⁵ The Company's request in this rate case is based entirely upon accounting entries and not upon any cash payment to the state of Oregon.²⁰⁶ If it is awarded what it is asking it would be a double recovery.²⁰⁷ And, for NWN to pay the deferred income tax balance it shows on its books, its rate base would have to decline so

199 UG 221/NWIGU-CUB/100/Larkin/29 lines 2-4.

200 UG 221/NWIGU-CUB/100/Larkin/29 lines 4-6.

201 UG/NWN/3000/Soires/14 lines 7-11.

202 UG 221/NWIGU-CUB/100/Larkin/29 lines 6-7.

203 UG 221/NWIGU-CUB/100/Larkin/29 lines 7-9.

204 UG 221/NWIGU-CUB/200 Larkin 3 lines 15-20 et seq.

205 UG 221/NWIGU-CUB/200 Larkin 4 lines 4-17.

206 UG 221/NWIGU-CUB/200 Larkin 4 lines 18-20.

207 UG 221/NWIGU-CUB/200 Larkin 5 lines 11-13.

that no future accelerated depreciation or tax timing differences existed. This is highly unlikely but if it did the Company could go to the Commission and request to collect those taxes from rate payers.²⁰⁸ Also of note is the fact that the Company earned close to or over its authorized return on equity in the majority of the years since 2001 and especially in 2009, the year of the tax change, when the Company had record earnings. Clearly the Company had the financial capability to absorb the effect of the non-cash tax change in that year.²⁰⁹

CUB and NWIGU's expert witness, Hugh Larkin Jr., is recommending disallowing the Company's proposed \$895,966 reduction to miscellaneous revenues.^{210,211} Staff is also recommending disallowance of this adjustment.²¹²

Between rate cases, expenses normally fluctuate. CUB recommends the Commission deny NWN's proposal to selectively collect past expenses from customers while retaining the benefit of reduced expenses in other categories. CUB agrees with Staff that, absent a Commission-approved balancing account, the collection from, or refund to, customers of these fluctuating expenses is not consistent with the Commission's deferred accounting policy.²¹³

The Company also notes that given Staff's and the Intervenor's objections, it would also be "agreeable to extending the amortization period of the deferred tax balance change. This would have the effect of reducing the annual revenue impact associated with recovery of the deferred tax balance, but still allow the Company recovery of the appropriate balance over time."²¹⁴ CUB does not support this proposal. The Company should have filed for a deferral in

208 UG 221/NWIGU-CUB/200 Larkin 10 lines 5-10.

209 UG 221/NWIGU-CUB/200 Larkin 11 lines 8-14.

210 UG 221 NWIGU-CUB/100 Larkin 27 lines 16 – 21, 28 lines 1 – 26, 29 lines 1-13.

211 UG 221/NWIGU-CUB/200 Larkin 2 lines 6 to page 13 line 10.

212 UG 221/Staff/500 Garcia/9 lines 1-14.

213 UG 221/Staff/500 Garcia/9 lines 8-14.

214 UG 221/NWN/3000/Soires/16 lines 21-23 and 17 lines 1-3.

this matter and did not. The Company is not entitled to have these funds deferred and therefore is not entitled to have them amortized no matter the amortization period.

VII. CONTRARY TO NWN'S PRONOUNCEMENTS STAFF AND THE INTERVENORS' PROPOSALS ARE UNLIKELY TO IMPOSE ANY FINANCIAL HARM ON THE COMPANY

Throughout its testimony, the Company argues that the adjustments proposed by Staff and the Intervenor will cause financial harm to the Company and increase its risk profile.²¹⁵ Mr. Anderson recites a litany of immediate write offs that will be necessitated by a finding in Staff and the Intervenor's favor²¹⁶ but nowhere does Mr. Anderson, Mr. Miller or anyone else testifying on behalf of the Company discuss in any way fairness to customers. CUB thinks this is indicative of the Company's attitude to its customers versus its much loved shareholders.

In making this argument, Mr. Anderson decries the, "lower credit ratings, higher borrowing costs, less access to capital markets, less liquidity, higher working capital requirements and more difficult time responding to the challenges of the current environment . . ." that he is sure the Company is going to suffer.²¹⁷ But this is starkly juxtaposed with some of the Company's own exhibits and other testimony. In Mr. Feltz's Direct Testimony, he stated that, "the Company's current ratings for each type of debt security from Moody's Investor Service ("Moody's") and Standard and Poor's Ratings ("S&P") . . . of the Company's long-term and short-term debt are in the single "A" category, with a stable outlook. The Company's debt ratings have not changed since January 2012."²¹⁸ He also said that, "[s]ince the 2002 Rate Case, the Company's long-term secured debt ratings were upgraded twice and downgraded once by S

215 UG 221/NWN/1800/Anderson/9 lines 1-2; UG 221/NWN/2600/Miller/5 lines 25-29.

216 UG 221/NWN/1800/Anderson/9-11; UG 221/NWN/2600/Miller/6 lines 11-17.

217 UG 221/NWN/1800/Anderson/11 line 23 and 12 lines 1-3.

218 UG/221/NWN/400/Feltz/14 lines 1-5.

& P, and upgraded once by Moody's."²¹⁹ The downgrade was a correction of its default rating score.²²⁰

Most recently, in a report issued on June 29, 2011, S & P affirmed the Company's ratings and outlook, stating that the ratings for NW Natural 'reflect the Company's *excellent business risk profile and intermediate financial risk profile.*' (*emphasis in the original*) (citation omitted) S & P goes on to say, '*[S]upportive regulation, a high-growth service area with a mostly residential customer base, reliable gas supplies provided by significant storage capacity, access to three major gas supply basins, and low operating risk characterize the utility's excellent business profile. Its interconnection with only one major pipeline somewhat moderates these strengths.*'" (*emphasis added*)²²¹

And the latest Moody's report cited in the Direct testimony states that the Company's:

A3 senior unsecured rating reflects the predictability and stability of its earnings and cash flows from low business risk LDC operations in jurisdictions that provide supportive regulatory treatment. The rating also considers NWN's relatively high reliance on residential and commercial customers, a characteristic that can help mitigate risks associated with the current economic downturn, and incorporates its effective cost controls and attention to liquidity.²²²

Moreover, much of the Company's arguments about what should and should not be done to its ROE were based on what happened to decoupling, SIP, WARM etc.²²³ The Company, however, is keeping all of those programs with minor tweaks, assuming the stipulations are approved by the Commission. Thus, the Company should no longer be heard to argue that it needs a higher ROE because it might not have those programs.

The Company also argues loud and long about the "turmoil in the country and the world."²²⁴ But in that same sentence, Mr. Anderson is pointing out what is clear to all of us from a review of what Moody's and others have said about the Company: "NW Natural has been able

219 UG/221/NWN/400/Feltz/18 lines 18-19.

220 UG/221/NWN/400/Feltz/15 lines 3-5 *see also* UG 221/NWN/406/Feltz/1.

221 UG/221/NWN/400/Feltz/19 lines 5-12.

222 UG221/400/Feltz/19 lines 19-21 and 20 lines 1-4.

223 UG 221/NWN/1800/Anderson/13 lines 4-14.

224 UG 221/NWN/200/Anderson/21 lines 10-11; UG 221NWN/500/Hadaway/7 lines 10-18.

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to access markets at favorable rates despite the economic turmoil in the country and the world.”²²⁵ Given that NW Natural was able to access favorable rates with the over-earnings that it had in prior years, and the fact that, under Staff’s and the Intervenors’ proposal NW Natural’s over-earnings will not be allowed to further increase, should not affect NW Natural’s ability to access markets at favorable rates. Even the Company recognizes that “interest rates are currently near all-time lows . . . [t]he 30-year treasury rate even dipped below three percent in October of 2011. But NW Natural still argues for a higher ROE because of “uncertainty” caused by government intervention.²²⁶ And other information it gives states that investors are more interested in utilities because of the uncertain market.²²⁷ NW Natural cannot have it both ways. Either investors want utilities or they don’t. Everything NW Natural has presented to us suggests that investors love NW Natural and nothing that we are requesting in this rate case is going to change that.

NWN wants the Commission to set its rates so as not to reflect “unsustainably low interest rates.”²²⁸ CUB wants the Commission to set NW Natural’s ROE so as not to allow continued unsustainably high over-earning by NW Natural.

VIII. ADDITIONAL RECOMMENDATIONS.

Notwithstanding that CUB and NWN have now settled both rate design and the requested increase to the customer charge, CUB respectfully requests that the Commission outline a requirement that any future rate design proposals must be vetted in IRP proceedings if those proposals are expected to have a significant effect on energy efficiency.²²⁹ This is necessary to

225 UG 221/NWN/200/Anderson/21 lines 10-11.

226 UG 221/NWN/200/Anderson/22 lines 1-12.

227 UG/221/NWN/500/Hadaway/10 lines 1-3.

228 UG 221/NWN200/Anderson/23 lines 9-11.

229 UG 221/CUB/100 Jenks-Feighner/2 at 11-13.

ensure that any proposed rate design is vetted for its effects on supply and demand before it is considered in a rate case.

IX. CONCLUSION.

In conclusion, CUB does not support any of the requests being made by the Company in the remaining to be resolved “unsettled issues”. From CUB’s point of view all of these items are being requested by the Company for one simple reason – to beef up its already large over-earning. NWN is not Oliver Twist and it does not deserve any more.

CUB’s specific requests to the Commission in regard to this docket are as follows:

- That the Commission set the Company’s ROE at 9.4 percent.
- That the Commission set the Company’s capital structure at 50 percent equity and 50 percent debt.
- That the Commission adopt Staff’s position as to hedging.
- That the Commission find that the Company was not prudent in moving forward with either the Monmouth Reinforcement or Perrydale to Monmouth sections of the Mid Willamette Valley Feeder project at this time and that the costs of those projects should be removed from the test year.
- That the Commission find that to include past pension contributions in future rates would constitute retroactive ratemaking and that these costs may not be included in the test year. And that the Commission find that removal of the unrecovered investor contribution of \$21,929,876 from rate base and the removal of the entire \$4,568,724 from amortizable expenses on an Oregon basis is appropriate.
- That the Commission find that the Company has failed to meet the burden of proof that its proposals for environmental remediation costs are prudent. The request for GASCO

pumping station is being made for a plant that is not yet used and useful let alone the fact that the request is retroactive in nature because it seeks recovery based on damages caused long ago which have no relation to provision of service to current rate payers. The SRRM proposal fails for the same reason the costs relate to damage from long ago with no connection to current ratepayers. And in the case of the SRRM the Commission should find it is not appropriate for a deferral to be converted to an automatic adjustment clause in order to avoid an earnings test. The Commission should find that it is more than equitable for NW Natural's shareholders to have to share 50/50 with its customers the costs of environmental damage caused decades ago which have no relation to the present provision of gas service to the Company's current customers.

- That the Commission find the Company's out of period tax adjustments are not prudent because they are both examples of single issue rate making and retroactive ratemaking – the Company needed to file for a deferral if it wanted to recover these costs. The Commission should therefore find that the Company's proposed \$895,966 reduction to miscellaneous revenues should be disallowed.

Dated this 20th day of August, 2012.

Respectfully submitted,



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July 9, 2012

VIA ELECTRONIC FILING AND FIRST CLASS MAIL

PUC Filing Center
Public Utility Commission of Oregon
PO Box 2148
Salem, OR 97308-2148

Re: Docket UG 221 – Northwest Natural Gas Company Application for a General Rate Revision

Attention Filing Center:

Attached for filing in the above captioned docket are the original and five copies of Partial Stipulation of the parties. A copy of this filing has been served on all parties to this proceeding as indicated on the attached Certificate of Service.

Please contact this office with any questions.

Very truly yours,



Wendy McIndoo
Office Manager

Enclosure

cc: Service List

**BEFORE THE PUBLIC UTILITY COMMISSION
OF OREGON**

UG 221

In the Matter of
NORTHWEST NATURAL GAS COMPANY
Application for a General Rate Revision.

**PARTIAL
STIPULATION**

This Partial Stipulation is entered into for the purpose of resolving specific issues among all parties to UG 221, Northwest Natural Gas Company's ("NW Natural" or "the Company") 2011 general rate case.

PARTIES

1. The parties to this Partial Stipulation are NW Natural, Commission Staff ("Staff"), the Citizens' Utility Board of Oregon (CUB), and the Northwest Industrial Gas Users (NWIGU) (collectively, "Parties"). Northwest Energy Coalition (NVEC) participated in settlement discussions, is not a party to this stipulation, but does not oppose the stipulation. Community Action Partnership of Oregon, Northwest Pipeline GP, and Portland General Electric Company are parties to this case but did not participate in settlement discussions.

BACKGROUND

2. On December 30, 2011, NW Natural filed revised tariff sheets to be effective February 1, 2012, seeking a general rate increase of approximately \$43.7 million, or 6.2 percent. In its filing, NW Natural used an historic base period of the 12 months ended December 31, 2011, with adjustments to calculate a future test period of the 12 months ending October 31, 2013 ("Test Year").

3. In Order No. 12-011, issued on January 19, 2012, the Public Utility Commission of Oregon ("Commission") suspended the Company's application for a general rate revision

for a period of nine months. Based on the suspension, the effective date of the revised tariff sheets will be November 1, 2012.

4. Pursuant to Administrative Law Judge Hardie's Prehearing Conference Memorandum of January 23, 2012, the parties to this docket convened settlement conferences on April 4 and 5, 2012. NW Natural, Staff, CUB, NWIGU, and NWECC participated in those settlement conferences.

5. On May 3, 2012, Staff, CUB, NWIGU, and NWECC filed Opening Testimony responding to the Company's Initial Filing.

6. The Parties again convened settlement conferences on May 22 and 23, 2012.

7. As a result of those settlement conferences, the Parties have reached a settlement resolving some of the issues in this case. This Partial Stipulation reduces NW Natural's proposed rate increase and resolves certain issues raised by Staff, CUB, and NWIGU. The final amount of NW Natural's rate increase, if any, will be determined following Commission resolution of the issues unresolved by this Partial Stipulation.

AGREEMENT

The Parties agree to settle the issues in this Partial Stipulation consistent with the numbers provided in Attachment A. Specifically, the issues settled in this Partial Stipulation are:

Capital Projects

8. In their testimony, Staff, CUB, and NWIGU raised concerns as to whether certain construction projects included in Test Year rate base, but not completed as of the date the rate case was filed, would be used and useful by the rate effective date or in the Test Year. Specifically, in Opening Testimony, these parties questioned whether the following capital projects would be used and useful: Corvallis Reinforcement; Nertec meters; Perrydale to Monmouth; Tualatin Replacement training facility and land; Unified Communication (Phase 1 and Phase 2); Westside Transmission Re-rate; Portland System Optimization (Phase 1 and

Phase 2); Tualatin Bioswale; Sunset Sheds; Generators 2012 and 2013; Coos Bay Retrofit; and Astoria Retrofit.

9. In addition, Staff, CUB, and NWIGU raised concerns regarding the prudence of the Monmouth Reinforcement (\$8,087,000) and Perrydale to Monmouth (\$18,131,000) projects. Finally, CUB and NWIGU questioned whether the costs associated with the Corvallis Reinforcement, Parkrose Retrofit, Portland System Optimization (Phase 1 and Phase 2), Nertec Replacement, Unified Communication Phase 1 and Salem Retrofit were known and measurable.

10. The Company has confirmed that the following projects have been cancelled or delayed past the rate effective date: Corvallis Reinforcement; Westside Transmission Re-rate; Portland System Optimization (Phase 2); Unified Communication Phase 2; Tualatin Bioswale; Sunset Sheds; Coos Bay Retrofit; and Astoria Retrofit. NW Natural agrees to remove the amounts that were included in rate base for these projects in the Test Year, consistent with Attachment A.

11. Further, the Company clarified that the Monmouth Reinforcement, Perrydale to Monmouth, Tualatin Replacement, Unified Communication Phase 1, Portland System Optimization Phase 1, and 2012 Generators projects will all be used and useful by the rate effective date. To remove any continuing concerns, however, the Company agrees that by October 1, 2012 it will file an attestation from senior management confirming that these projects either are or will be used and useful by the rate effective date. The attestation filing will also confirm the amount that the Company has invested in each of those projects as of the date of the filing, and, if the project is not yet complete, the Company's reasonable expectation of costs that will be incurred up to the rate effective date.

12. Except as discussed in paragraph 13 below, if the attestation described in paragraph 11 demonstrates that a project is, or will be, used and useful by the rate effective date, the Parties agree that the lower of the forecast or the actual amount expended on that

project as of the rate effective date may be added to rate base and recovered through the revenue requirement. Nothing in this paragraph precludes the Company from filing a deferral application in the event that the Company believes it will incur additional costs related to the project after the rate effective date, or if the amounts that have been incurred or will be incurred by the rate effective date are greater than the amount included in the Company's original filing for that project and are eligible for deferral. And, nothing precludes other Parties from taking any position (supporting or opposing) on the deferral application and application for amortization.

13. If the Company's attestation demonstrates that the Monmouth Reinforcement and the Perrydale to Monmouth projects will be used and useful by the rate effective date, there remains an issue of whether or not these two projects were prudent. The Parties may argue that these projects either were or were not prudent in this proceeding. To the extent the Commission finds that such projects were prudent, the lower of the forecast or actual costs of such projects, incurred as of the rate effective date, will be added to rate base for purposes of the Company's revenue requirement. Nothing in this paragraph precludes the Company from filing a deferral application in the event that the Company believes it will incur additional costs related to a project after the rate effective date, or if the amounts that have been incurred or will be incurred by the rate effective date are greater than the amount included in the Company's original filing for that project and are eligible for deferral. And, nothing precludes other Parties from taking any position (supporting or opposing) on the deferral application and application for amortization.

14. In the case of the Nertec project, the Parties understand that it is possible that not all of the Nertec meters will be installed by the rate effective date. For the purposes of this settlement, the Parties agree that, provided that the Company attests that all of the Nertec meters will be received by the rate effective date and installed by the end of the Test Period, 50% (fifty percent) of the Test Year costs of the meters will be added to rate base.

15. In regards to the Salem Retrofit, to remove any continuing concerns, the Company agrees that by October 1, 2012 it will file an attestation confirming that the project either is or will be used and useful by the rate effective date. The filing will also confirm the amount that the Company has invested in the project as of the date of the filing, and, if the project is not yet complete, the Company's reasonable expectation of costs that will be incurred up to the rate effective date.

16. The Parties agree that the lower of the forecast or actual costs of the project, incurred as of the rate effective date, will be added to rate base for purposes of the Company's revenue requirement. Nothing in this paragraph precludes the Company from filing a deferral application in the event that the Company believes it will incur additional costs related to the project after the rate effective date, or if the amount that has been incurred or will be incurred by the rate effective date is greater than the amount included in the Company's original filing for that project and are eligible for deferral. And, nothing precludes other Parties from taking any position (supporting or opposing) on the deferral application and application for amortization.

17. The Company also agrees to remove the following projects, which are scheduled to be completed during the Test Year but after the rate effective date: Portland System Optimization Phase 2; and Unified Communications Phase 2. The Parties agree that the 2013 Generators will be averaged into rate base such that 50% of the associated costs are reflected in rate base in the Test Year.

18. In the event that the Company's attestation demonstrates that one or more projects described above will not be used and useful by the rate effective date, the revenue requirement in the case will be offset by the effect of removing the costs of such project or projects from rate base.

19. Regarding those projects that will not be used and useful in time to be included in rates by the rate effective date, the Parties are aware that the Company may ask the

Commission to consider including those costs in rates through a tracker or at the time of a Purchased Gas Adjustment, but the impartation of this knowledge is not intended in any way to limit the Parties participation in future dockets or to prejudge the Parties' positions on such requests.

Revenue Adjustment related to the Company's Proposed Rate Design

20. In its Opening Testimony, Staff argued that the Company had understated its projected revenues for the Test Year by overstating the amount it would lose through customer attrition in the event that its rate design proposal is adopted (the "Company's Proposed Revenue Adjustment"). As a result, in its Opening Testimony, Staff recommended that the Company's Proposed Revenue Adjustment should be removed, and estimated a downward adjustment of \$5.356 million. After discussion, Staff agreed that the Company's Proposed Revenue Adjustment should be \$2.3 million, and the Parties agree that an adjustment of \$2.3 million of revenues should be made in the event that the Commission adopts the Company's proposed rate design (as proposed in the Company's Initial Filing). The parties agree that if the Commission does not adopt the Company's proposed rate design, then the Company should increase expected revenues by \$2.3 million.

Parkrose Retrofit

21. In its Opening Testimony, Staff recommended that the Company's proposed recovery for the Parkrose Retrofit be reduced by \$0.621 million. The Parties agree that Staff will withdraw this recommendation, and that the Company should recover its costs related to the Parkrose Retrofit as proposed.

Rate Case Amortization

22. In its Opening Testimony, CUB/NWIGU recommended that the Company's Rate Case Expense be amortized over five instead of the three years assumed in the Company's proposal, resulting in a downward adjustment to Operating and Maintenance Expense (O&M)

of \$0.093 million. The Parties agree that CUB/NWIGU will withdraw this recommendation and that the Company should recover its Rate Case Expense as proposed.

Uncollectibles Adjustment

23. In its Opening Testimony, CUB/NWIGU recommended that the Company's proposal for recovery of uncollectible expense be reduced by \$0.448 million. The Parties agree that CUB/NWIGU will withdraw this recommendation, and that the Company should recover its uncollectibles as proposed.

Injuries and Damages Expense

24. In its Opening Testimony, CUB/NWIGU recommended that the Company's proposed recovery for Injuries and Damages Expense be reduced by \$0.126 million. The Parties agree that CUB/NWIGU will withdraw that recommendation and that the Company should recover its Injuries and Damages Expense as proposed.

Directors and Officers Insurance

25. In Opening Testimony, Staff recommended that NW Natural be allowed to recover only 50% of the costs of Directors and Officers Insurance above the first layer of coverage. CUB/NWIGU made a different but similar recommendation. The Parties agree that the Company's O&M expense should be adjusted by a reduction of \$0.272 million to remove that portion of the costs of D&O insurance consistent with Staff's recommendation.

Incentive Pay

26. In its Opening Testimony, Staff and CUB/NWIGU both recommended that the Commission make a downward adjustment to the Company's proposal for recovery of incentive pay. The Parties agree the Company's proposed recovery for incentive pay should be adjusted by an amount that represents a 25% reduction to Staff's original recommendation. This amount will vary from the adjustment proposed in Staff's testimony to the extent required to match the Commission's ultimate determination on full-time employees (FTEs), such that the adjustment will represent the application of the Commission precedent described in Staff's

testimony to the number of FTEs determined by the Commission to be includable in revenue requirement, and then reduced by 25%.

Administrative and General

27. In its Opening Testimony, Staff recommended that the Company's proposed Administrative and General (A&G) expense should be reduced by \$1.982 million, and CUB/NWIGU has specifically proposed that the Company's proposed recovery for American Gas Association dues (which is included in A&G expense) should be reduced by \$148,114 . After discussions the Parties agreed that the Company's A&G expense should be adjusted by (\$1.212 million).

Miscellaneous Revenue

28. In its Opening Testimony, and later corrected through an errata filing, Staff recommended that the Company's Miscellaneous Revenue proposal be adjusted by \$0.658 million. After discussion, the Parties agreed that the Commission should adopt an adjustment of \$0.494 million, which represents a reduction of 25% of Staff's adjustment proposed in its corrected Opening Testimony.

Advertising

29. In its Opening Testimony, Staff recommended that the Company's advertising expense for Category A advertising expenditures be reduced by \$0.930 million to match the level presumed prudent under OAR 860-026-0022(3)(a). The Parties agree that the Company should be allowed to recover Category A expense commensurate with the per-customer level of \$2.19 allowed in the Company's last rate case and applied to Test Year customer levels. Additionally, the Parties agree that NW Natural should recover \$510,000 of costs for Category B expenses.

Research and Development

30. In its Opening Testimony, Staff recommended that the Company's proposal for Research and Development expense be reduced by \$0.006 million. The Parties agree that

the Commission should accept this adjustment, and that the Company should be allowed to collect \$0.743 million of expenses related to Research and Development.

Materials and Supplies

31. In its Opening Testimony, CUB/NWIGU recommended that the Company's proposal for Materials and Supplies included in rate base should be reduced by \$0.633 million. The Parties agree that this recommendation should be accepted.

Contributions in Aid of Construction (CIAC)

32. In its Opening Testimony, CUB/NWIGU recommended that the Company's rate base be reduced by \$0.069 million to account for its adjustment related to CIAC. The Parties agree that the Company's rate base should be adjusted by this recommendation.

Customer Deposits

33. In its Opening Testimony, CUB/NWIGU recommended that the Company's rate base be reduced by \$5.1 million to account for the Company's possession of customer deposits. All Parties, including the Company agree to accept this recommendation. In addition, as an offset to this reduction, the Company's O&M expense should be increased by \$.005 for interest expense on the customer deposits.

Injuries and Damages Reserves

34. The Parties agree that the Company's proposed rate base should be reduced by \$0.211 million in recognition of the CUB/NWIGU recommendation on this issue.

35. This Partial Stipulation will be offered into the record as evidence pursuant to OAR 860-001-0350(7). The Parties agree to support this Partial Stipulation throughout this proceeding and any appeal, provide witnesses to sponsor this Partial Stipulation at hearing, if needed, and recommend that the Commission issue an order adopting the Partial Stipulation.

36. If this Partial Stipulation is challenged by any other party to this proceeding, the Parties agree that they will continue to support the Commission's adoption of the terms of this Partial Stipulation. The Parties reserve the right to cross-examine witnesses and put in such

evidence as they deem appropriate to respond fully to such issues presented including the right to raise issues that are incorporated in the settlements embodied in this Partial Stipulation.

37. The Parties have negotiated this Partial Stipulation as an integrated document. If the Commission rejects all or any material portion of this Partial Stipulation or imposes additional material conditions in approving this Partial Stipulation, any Party shall have the right to withdraw from the Partial Stipulation, along with any other rights provided in OAR 860-001-0350(9), including the right to present evidence and argument on the record in support of the Partial Stipulation, and shall be entitled to seek reconsideration pursuant to OAR 860-001-0720.

38. By entering into this Partial Stipulation, no Party shall be deemed to have approved, admitted, or consented to the facts, principles, methods, or theories employed by any other Party in arriving at the terms of this Partial Stipulation, other than as specifically identified in the body of this Stipulation. No Party shall be deemed to have agreed that any provision of this Partial Stipulation is appropriate for resolving issues in any other proceeding, except as specifically identified in this Partial Stipulation.

39. This Partial Stipulation may be executed in counterparts and each signed counterpart shall constitute an original document.

This Partial Stipulation is entered into by each Party on the date entered below such Party's signature.

SIGNATURE PAGE TO FOLLOW

NW NATURAL

By: Lisa Rackner
Printed Name: Lisa Rackner
Date: 7-9-12

STAFF

By: _____
Printed Name: _____
Date: _____

CUB

By: _____
Printed Name: _____
Date: _____

NWIGU

By: _____
Printed Name: _____
Date: _____

NW NATURAL

By: _____

Printed Name: _____

Date: _____

CUB

By: _____

Printed Name: _____

Date: _____

STAFF

By:  _____

Printed Name: Jason Jones

Date: 7/6/12

NWIGU

By: _____

Printed Name: _____

Date: _____

NW NATURAL

STAFF

By: _____

By: _____

Printed Name: _____

Printed Name: _____

Date: _____

Date: _____

CUB

NWIGU

By:  _____

By: _____

Printed Name: G. Patricia McGracken

Printed Name: _____

Date: 7-6-2012

Date: _____

NW NATURAL

By: _____

Printed Name: _____

Date: _____

CUB

By: _____

Printed Name: _____

Date: _____

STAFF

By: _____

Printed Name: _____

Date: _____

NWIGU

By: Paula E. Pyron

Printed Name: Paula E. Pyron

Date: 7/6/12

UG 221 Northwest Natural

First Stipulation

Dollars (000s)

UG 221 CUB Pre-hearing Brief Attachment A
16 of 17

ATTACHMENT A

Staff & Intervenors
Adjustments
Oregon
Allocation

S-2	Corvallis Reinforcement	(8,370)
S-4	Nertec Replacement	(844)
S-5	Parkrose Retrofit	0
S-7	Tualatin replacement, training facility & land	0
S-8	Unified Communication Phase 1 (PBX Switch)	0
S-9	Westside Transmission Rerate	(1,800)
S-10	Directors and Officers Insurance	(272)
S-11	Incentive Compensation	(2,573)
S-13	Various Customer Service, G&A Expenses	(1,212)
S-15	Research & Development	(6)
S-19	Advertising	(382)
S-21	Miscellaneous Revenue	494
C-1	Portland Optimization Phase II	(563)
C-2	United Communication Phase II	(450)
C-3	Tualatin Bio Swale	(540)
C-4	Sunset Sheds	(603)
C-5	Coos Bay Retrofit	(625)
C-6	Astoria Retrofit	(400)
C-7	Materials and Supplies (M&S)	(633)
C-8	Contributions in Aid of Construction (CIAC)	(69)
C-9	Customer Deposits	(5,101)
C-9	Customer Deposits - Interest Expense	5
C-10	Injuries & Damages Reserves	(211)
C-11	Portland System Optimization Phase I	0
C-12	2012 Generator	0
C-13	Salem Retrofit	0
C-14	2013 Generators	0

CERTIFICATE OF SERVICE

I hereby certify that I served a true and correct copy of the foregoing document in UG 221 on the following named person(s) on the date indicated below by email addressed to said person(s) at his or her last-known address(es) indicated below.

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Dated: July 9, 2012

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DEPARTMENT OF JUSTICE
GENERAL COUNSEL DIVISION

August 14, 2012

Lisa Hardie
Administrative Law Judge
Public Utility Commission of Oregon
550 Capitol St NE – Suite 215
Salem OR 97301

RE: UG 221 - Settlement in principle

Dear ALJ Hardie,

The parties to this proceeding have reached a settlement in principle on many of the issues in this proceeding. The settlement in principal covers the following items:

- Rate design;
- Decoupling and the Weather Adjusted Mechanism;
- LRIC;
- Rate Spread, with the exception of rate spread related to an environmental cost recovery mechanism;
- Cost of Long Term Debt, except that NW Natural's interest rate hedging activity remains an issue;
- The level of full-time employees to be included in rates;
- Other issues related to FTE: medical benefits, workers' compensation, overtime, payroll tax, and depreciation expense;
- Payroll capitalization;
- Working gas inventory;
- Schedule 31 and Schedule 32 rate design;
- Interstate Storage;
- System Integrity Program;
- Service window guarantee; and
- Reconnection Charges

The settlement in principle does not resolve the following issues:

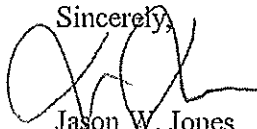
- Cost of Capital, including NW Natural's interest rate hedging activity;

Lisa Hardie Administrative Law Judge
August 14, 2012
Page 2

- Environmental cost recovery mechanism;
- Pensions;
- State Taxes;
- The prudence of Mid-Willamette Valley Feeder projects – the Monmouth to Perrydale and Monmouth Reinforcement projects.

The parties to this settlement in principle intend to file a formal stipulation on these issues before the hearing scheduled on August 23-24, 2012.

If you have any questions, please do not hesitate to contact me.

Sincerely,

Jason W. Jones
Assistant Attorney General
Business Activities Section

JWJ:nal/3570795-v1

CERTIFICATE OF SERVICE

I certify that on August 14, 2012, I served the foregoing Letter upon the parties in this proceeding by electronic mail only as all parties waive paper service.

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11 Business Activities Section
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UG 221 – CERTIFICATE OF SERVICE

I hereby certify that, on this 21st day of August 2012, I served the foregoing **CITIZENS' UTILITY BOARD OF OREGON'S PRE-HEARING BRIEF** in docket UG 221 upon each party listed in the UG 221 Service List by email and, where paper service is not waived, by U.S. mail, postage prepaid, and upon the Commission by email and by sending one original and five copies by U.S. mail, postage prepaid, to the Commission's Salem offices.

(W denotes waiver of paper service)

(C denotes service of Confidential material authorized)

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Respectfully submitted,



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