BEFORE THE

PUBLIC UTILITY COMMISSION OF OREGON

UG 344

In the Matter of	)
NORTHWEST NATURAL GAS COMPANY, dba NW NATURAL,	)
Request for a General Rate Revision.	)

TESTIMONY IN OBJECTION TO THREE-PARTY STIPULATION OF

BRADLEY G. MULLINS

ON BEHALF OF THE ALLIANCE OF WESTERN ENERGY CONSUMERS

October 1, 2018

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I. INTRODUCTION

Q. ARE YOU THE SAME WITNESS THAT PROVIDED OPENING AND REBUTTAL TESTIMONY IN THIS MATTER?

A. Yes. I previously filed testimony in this matter on behalf of the Alliance of Western Energy Consumers ("AWEC").

Q. WHAT IS THE PURPOSE OF YOUR TESTIMONY?

A. On September 7, 2018, NW Natural, Staff and the Citizens' Utility Board ("CUB") entered into a Three-Party Stipulation (the "Contested Stipulation") making a number of new ratemaking proposals which were never addressed in the evidentiary phase of this docket. This is particularly problematic because rates are scheduled to go into effect just one month from today, leaving little time for AWEC and the Commission to explore whether the Contested Stipulation is in the public interest. My testimony provides AWEC's objections to the Contested Stipulation.

Q. PLEASE SUMMARIZE YOUR TESTIMONY.

A. Now, at the very last minute, the Contested Stipulation contains a proposal to begin amortizing in rates $94,600,000 in pension expense that has been recorded in the Pension Balancing Account ("PBA"), which has not been shown to be completely a ratepayer obligation. Just because NW Natural has recorded a regulatory asset on the books it uses for its financial statements does not mean the entire balances are due from customers. Indeed, account balances on a utility's books do not necessarily equate to a legal obligation to pay on behalf of ratepayers. The record does not contain any evidence demonstrating that such a legal obligation exists and, therefore, the Commission should accept the proposal in the Contested Settlement to freeze the PBA as of October 31, 2018, but open a new docket to explore

responsibility for these amounts. AWEC does not object to the proposal to recover future FAS 87 pension expense in base rates.

It is noteworthy that Paragraph 4 of the UM 1475 stipulation—the document that NW Natural suggests creates the ratepayers' obligation to pay the balances—explicitly provides that the balances could not be amortized in circumstances, such as these, where the balances fail to reverse and become negative. The UM 1475 stipulation was not ambiguous on this point.

To make the proposal even more untenable, the Contested Stipulation also provides that significant monies that are due to customers as a result of tax reform are used to satisfy the alleged PBA balances. To make matters worse, this unfair treatment applies predominantly to the tax reform items that are due to transportation customers, since sales customers get to keep the majority of their much larger tax reform savings.

The Contested Stipulation is neither reasonable nor fair from a ratepayer perspective.

Q. WHAT ARE AWEC'S SPECIFIC OBJECTIONS TO THE CONTESTED STIPULATION?

A. AWEC has four objections to the Contested Stipulation, which I discuss below.

First, applying valid tax refund amounts that are due to ratepayers to offset a regulatory account balance, where there is no evidence that customers are responsible for 100 percent of the PBA balances, is in no way an acceptable settlement term to AWEC. Ratepayers deserve to get the funds associated with tax reform in a timely and reasonable manner and not have them earmarked for a questionable regulatory account balance. The PBA and tax reform are two separate issues that AWEC recommends the Commission decide and consider on their own merits.

Second, AWEC objects to the proposal to amortize the PBA balances, since there has been no demonstration in this case that ratepayers are responsible for 100 percent of those amounts. The UM 1475 Stipulation explicitly stated that the balance could not be amortized in these circumstances. Accordingly, I recommend the Commission reject the proposal in the Stipulation to amortize $94,600,000 in connection with the PBA, and instead open a new docket to determine the appropriate ratepayer/shareholder responsibility.

Third, NW Natural's calculation of the Interim Period tax savings is materially flawed, and litigating all of the issues surrounding that calculation through a Contested Stipulation at this stage in the docket is not reasonable. Accordingly, I recommend that the Commission adopt the same approach that has recently been used in Portland General Electric Company's ongoing general rate case.[1] Rather than earmarking those funds to the PBA, I recommend that NW Natural begin refunding its estimate of the Interim Period tax savings over a two year period, subject to a true up in the second year based on further proceeding in the tax deferral docket.

Fourth, AWEC objects to NW Natural's purported use of the Average Rate Assumption Methodology ("ARAM") methodology. Based on my review, I have concluded that the calculation is not being done properly. Notwithstanding, AWEC does not object to the $3,260,000 amount of protected Excess Deferred Federal Income Tax ("EDFIT") amortization identified in the Contested Stipulation, since it is approximately in line with the amount AWEC recommended using the Alternative Method. Thus, AWEC recommends that the Commission accept the EDFIT reversal amount, but to also acknowledge that many issues remain

[1] In re Portland General Electric Company, Request for a General Rate Revision, Docket UE 355, Third Partial Stipulation, Paragraph 2.c. (Sep. 14, 2018).

outstanding with respect to the ARAM methodology being used by NW Natural, including whether it should be used at all, and that parties are not foreclosed from raising those issues in future proceedings.

II. AWEC'S OBJECTIONS

a. Earmarking Tax Reform Dollars Is Bad Policy and Not Justified in this Case

Q. WHY IS IT UNFAIR TO EARMARK TAX REFORM DOLLARS TO PAY OFF THE PENSION BALANCING ACCOUNT?

A. The Contested Stipulation takes several components of the tax savings associated with tax reform, and instead of giving the money back to customers, lets NW Natural keep the ratepayer monies and use the funds to offset a regulatory account balance, which has not been shown to be a ratepayer responsibility. The issues surrounding the PBA are appropriately resolved on their own merits, independent from the issues surrounding tax reform. Further, the tax reform dollars need to be refunded in an expedient manner. Accordingly, it is nether appropriate nor reasonable to comingle the two issues in the Contested Stipulation.

Q. WHY IS THIS NEW PROPOSAL TO EARMARK THE TAX REFORM FUNDS PROBLEMATIC FROM A PROCEDURAL PERSPECTIVE?

A. The Contested Stipulation was filed after NW Natural's Final Brief in this docket. The docket was nearly completed. Filing a Contested Stipulation on complex tax and pension related matters is hardly reasonable at this late stage of the proceeding especially since these are significant issues of policy and ratemaking. NW Natural now alleges that ratepayers are responsible for a staggering $94,600,000.00, yet AWEC had no opportunity to conduct discovery on the prudence of this amount or the Joint Testimony in Support of the Contested Stipulation which was filed on September 14, 2018, and only a limited ability to conduct

discovery on the Contested Stipulation itself—and NW Natural objected to some of AWEC's data requests.

Q. WAS THIS A PROPOSAL THAT WAS CONSIDERED IN THE EVIDENTIARY PHASE OF THIS DOCKET?

A. No. Up until the filing of the Contested Stipulation, NW Natural maintained that the PBA was not broken and should not be terminated early.[2] Accordingly, in the evidentiary phase of this docket, NW Natural never requested recovery or amortization of any amount associated with the PBA. As I understand it, a utility can only be granted amortization of a deferred amount if it files a request for amortization pursuant to the requirements of OAR 860-027-0300(9). NW Natural made no such request in this docket.

Other than a parenthetical reference to Mr. Borgeson's Sur-Rebuttal Testimony,[3] NW Natural's Opening Brief and Final Brief make no mention of NW Natural's proposal to earmark the tax reform monies for the alleged pension balancing account balances. Further, the concept of using tax reform savings was not developed in NW Natural's Direct Testimony, Rebuttal Testimony or Sur-Rebuttal testimony, except through oblique statements, such as in Mr. Borgeson's Sur-Rebuttal testimony that NW Natural "would *consider* applying all or a portion [of the tax reform savings] to the pension balancing account."[4]

In fact, up until the filing of the Contested Stipulation, NW Natural maintained that these tax reform monies associated with EDFIT and the Interim Period were not appropriately considered, at all, in this docket.[5] Those were two of the three remaining issues that were

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2 NW Natural Opening Brief at 20:10-21:11.
3 NW Natural Opening Brief at 38:20-39:1.
4 NW Natural/2500, Borgeson/31 3-12 *emphasis added*.
5 NW Natural Opening Brief at 33:1-36:13

being litigated in the case.[6] AWEC argued that these two tax reform items should be reflected in rates on November 1, 2018. NW Natural argued that those funds should not go back to customers in this docket.

Now, at this late stage in the proceeding, the Commission is being asked through the Contested Stipulation to accept, without evidentiary support, that ratepayers are responsible for $94,600,000 of alleged financial account balances associated with the PBA. Not only that, it asks the Commission to take monies that NW Natural previously argued against including in rates, and earmark those monies for the PBA. Relative to the positions of parties in the earlier phases of this proceeding, this is a radical, new proposal.

Q. WHY DO THE TWO ISSUES NEED TO BE CONSIDERED ON THEIR OWN MERITS, AND NOT COMINGLED?

A. There are a number of reasons why it is bad policy to comingle the two issues. Foremost, the treatment presumes $94,600,000 of customer responsibility with respect to PBA, which has not been demonstrated in this docket.

Further, even if one were to conclude that ratepayers are responsible for the $94,600,000 of alleged financial account balances, ratepayers are harmed as a result of this treatment due to the time value of money. Ratepayers would be exchanging tax reform funds that are due to them today, with amounts being amortized over 10 years. Thus, if it accepts the Contested Stipulation, not only would the Commission accept the $94,600,000 in customer liability associated with PBA, it would be spreading the ratepayers' moneys associated with tax reform over a ten-year period, without properly compensating for the time value of money.

[6] See e.g. AWEC Response Brief at 2.

Q. DOES THE CONTESTED STIPULATION USE THE SAME TREATMENT FOR SALES AND TRANSPORTATION CUSTOMERS?

A. No. The Contested Stipulation gives all of the unprotected dollars due to sales customers back to sales customers. AWEC does not oppose this, but it is unfair that sales customers get to keep the benefits of the tax reform, while each of the other tax savings items due to transportation customers are used to offset the PBA.

Q. WHAT DO YOU RECOMMEND?

A. As discussed further below, I recommend that the Commission require NW Natural to begin returning all items of ratepayer savings associated with tax reform beginning on the November 1, 2018 rate effective date in this docket, including both the Interim Period amount and EDFIT. As discussed below, other than this issue of comingling ratepayer tax reform monies with the PBA balance, the points of controversy with respect to tax reform are relatively narrow.

Further, as discussed in this testimony, I recommend the Commission reject the proposal to amortize the PBA.

b. <u>The New Proposal to Amortize $94,600,000 for the Pension Balancing Account Balances Is Not Supported by the Record nor the UM 1475 Stipulation</u>

Q. WHAT AMOUNT OF AMORTIZATION IS PROPOSED FOR THE PENSION BALANCING ACCOUNT IN THE THREE-PARTY STIPULATION?

A. For the first time in this docket, the Commission is confronted with a proposal to begin amortizing the residual balances associated with the broken PBA mechanism. The Contested Stipulation requests the Commission approve total amortization of $94,600,000 of the residual PBA account balance, without any evidentiary support of whether this is entirely a ratepayer responsibility. The sources of the $94,600,000 in amortization in the Contested Stipulation consist of: (1) $5,900,000 in immediate amortization using the Interim Period tax reform monies due to ratepayers; (2) $6,700,000 of immediate amortization using unprotected EDFIT

monies due to ratepayers; and (3) annual amortization of $8,200,000 for ten years (i.e. $82,000,000) through a separate tariff rider.[7]

AWEC objects to the amortization associated with the PBA being proposed in the Contested Stipulation. No evidentiary support has been offered by the settling parties to demonstrate that ratepayers are 100 percent responsible for these amounts associated with the broken regulatory mechanism. In the Joint Testimony supporting the Contested Stipulation, the only support for amortizing these amounts in rates was a superficial statement that "at the time the [UM 1475] Stipulation was entered into […] the parties to the [UM 1475] Stipulation agreed that NW Natural should fully recover its FAS 87 pension expense and the costs of financing, and that those costs were prudently incurred."[8]

As I discuss below, the UM 1475 Stipulation made no such sweeping statements; in fact, it explicitly prohibited NW Natural from recovering any residual balances in these circumstances, where the balance has failed to reverse as intended. In any event, a trivial statement such as this is not a reasonable basis to conclude that $94,600,000 is due from ratepayers.

Q. PLEASE PROVIDE SOME BACKGROUND ON THE PENSION BALANCING ACCOUNT.

A. As noted above, the PBA was created through a stipulation in Docket UM 1475. Under Paragraph 1 of the UM 1475 Stipulation, NW Natural was to collect $3,796,055 annually in rates for pension expenses over the term of the UM 1475 Stipulation. In addition, NW Natural was prohibited from requesting an increase in the amount of pension expense recovered in

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7 As noted above, the $14,640,000 in unprotected EDFIT funds due to sales customers were not earmarked in this way in the Contested Stipulation.

8 NW Natural-Staff-CUB/200

rates prior to the termination of the balancing account. When the parties signed the UM 1475 Stipulation, NW Natural agreed that an annual amount of $3,796,055 was a sufficient level of recovery to provide recovery of the pension expenses over an extended period of time. When it did so, NW Natural assumed the risk that the balance might not reverse as intended. The UM 1475 Stipulation was explicit on this point in Paragraph 4.

Q. WHAT DOES PARAGRAPH 4 OF THE UM 1475 STIPULATION SAY?

A. The term of the PBA was described in Paragraph 4 of the UM 1475 Stipulation as follows:

> The balancing account will terminate upon the effective date of the tariffs filed in connection with the first NW Natural 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.
>
> NW Natural is now seeking to amortize $94,600,000 in connection with the PBA.

Doing so, however, would plainly be inconsistent with Paragraph 4 of the UM 1475 Stipulation. NW Natural was not allowed to amortize the balancing account balance prior to the termination date of the balancing account and the termination date occurred in the first rate case after the balance became negative. Thus, if the balance did not become negative, as intended, NW Natural was not allowed to amortize the Pension Balancing account under the UM 1475 Stipulation.

Q. WHY IS IT NECESSARY TO TERMINATE THE PENSION BALANCING ACCOUNT PRIOR TO THE TERM IDENTIFIED IN PARAGRAPH 4 OF THE UM 1475 STIPULATION?

A. The PBA mechanism is broken and will never become negative. The annual interest accruing with respect to the mechanism exceeds the annual stipulated collections in rates. This means that the balance will never reverse as intended in the UM 1475 stipulation. As noted above, it also means that NW Natural will never be in a position of amortizing any amounts in

connection with the Pension Balancing Account under the UM 1475 Stipulation. Absent an early termination of the UM 1475 Stipulation, the balance will continue to accumulate interest and never be in a position to amortize.

Q. DO THE FUNDS ACCUMULATED IN THE PENSION ACCOUNT REPRESENT MONIES OWED BY RATEPAYERS?

A. It is clear that the mechanism is broken, and it would be unfair to hold NW Natural to the terms of the UM 1475 Stipulation since the mechanism will never reverse and therefore no funds are due from ratepayers for the residual amounts accumulated in the PBA. It is also unfair to assume that all of these amounts are the responsibility of ratepayers. Accordingly, the PBA should be frozen, and explored in a separate proceeding.

Q. DID THE UM 1475 STIPULATION REQUIRE AN EARNINGS TEST?

A. Yes. Under Paragraph 3 of the UM 1475 Stipulation, an earnings test was to be performed before any amortization of the balancing account balance was to begin. The earnings test was to be applied over the entire course of the PBA mechanism's term, for all periods up to the period when the mechanism began to reverse and the balance became zero.

Q. WAS AN EARNINGS TEST PERFORMED?

A. No. Staff was requested to provide the earnings test for the proposed PBA account amortization in AWEC Data Request 01 to Staff. Staff provided no such earnings test, and instead provided an earnings analysis that might be applied to the Interim Period tax reform funds due to ratepayers. Given the abbreviated process for litigating the Contested Stipulation, and the upcoming rate effective date, AWEC was unable to issue a follow up request for clarification. Whatever the case may be, however, there is no evidence that an earnings test

has been performed, another reason that it would be improper to amortize any funds in this docket, even if ratepayers are ultimately determined to be responsible for those funds.

Q. WHAT OTHER FACTORS SHOULD BE CONSIDERED TO DETERMINE RESPONSIBILITY FOR THE BALANCES?

A. To consider the responsibly for these balances, it is necessary to perform an analysis for each year to analyze the prudence of historical pension contribution levels, interest rate assumptions, and other actuarial assumptions, which give rise to the year-to-year balances.[9] If, for example, the higher than expected expenses were caused by an imprudent pattern of contributions, then it would not be appropriate for NW Natural to recover those amounts. Further, if the interest rate assumptions have declined based on actions taken by NW Natural to reduce the risk of its pension portfolio, that may be an indication of imprudence.[10]

Q. WHAT DO YOU RECOMMEND?

A. The Joint Parties have not provided any evidence upon which the Commission may reasonably conclude that ratepayers are responsible for $94,600,000 in amortization associated with the PBA, as proposed in the Contested Stipulation. Accordingly, I recommend that the Commission reject the proposal in the Contested Stipulation to amortize the PBA in this docket, freeze the PBA and open a new docket to consider the extent that ratepayers bear responsibility for the residual balances.

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9 AWEC/500, Mullins/4:16-19; *See* ORS 757.259(5) (providing that "the Commission's determination on the amount of deferrals allowable in the rates of the utility is subject to a finding by the Commission that the amount was prudently incurred by the utility").

10 AWEC/500, Mullins/5:3-5.

c. Calculation of the Interim Period Tax Reform Funds Due to Ratepayers is Improper and Not Supported in the Record

Q. PLEASE SUMMARIZE AWEC'S OBJECTION TO NW NATURAL'S CALCULATION OF THE INTERIM PERIOD TAX SAVINGS.

A. AWEC objects to NW Natural's calculation of $5,900,000 for the Interim Period tax savings associated with tax reform. AWEC recommends the Commission adopt an approach similar to the approach that is being used for Portland General Electric Company.[11] Specifically, AWEC recommends that the Commission require NW Natural to begin amortization of the Interim Period tax savings through a supplemental rate schedule, beginning November 1, 2018, over a two year period.[12] The amortization of the Interim Period deferral should be established on a provisional basis, and subject to a true up in the second year of the amortization schedule based upon the outcome of supplemental process in the tax reform deferral docket.

Q. WHAT PROVISIONAL AMOUNT OF AMORTIZATION DO YOU RECOMMEND?

A. The analysis I prepared suggests that $13,890,000 is the total amount of funds due customers in connection to the Interim Period, implying annual amortization of $7,735,000. I have detailed this calculation on Pages 1-3 of Exhibit AWEC 602.

Notwithstanding, I recommend that the provisional amortization be set at $5,000,000, which is a value that is less than both my calculation and the calculation provided by NW Natural. This way customers would begin see the benefits associated with the Interim Period tax savings, and the Commission would still be free to adopt either approach, without requiring

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11 In re Portland General Electric Company, Request for a General Rate Revision, Docket UE 355, Third Partial Stipulation, Paragraph 2.c. (Sep. 14, 2018).

12 In contrast to the proposal in the Contested Stipulation to earmark the Interim Period tax reform funds for the Pension Balancing Account.

a corresponding reduction in the second year. In addition, my recommendation of using a lower value in the first year provides significant upside for ratepayers in the second year.

Q. HOW WAS NW NATURAL'S PROPOSED INTERIM PERIOD AMOUNT CALCULATED?

A. It is not entirely clear. The $5,890,160 amount was first presented in NW Natural's Final Brief; but otherwise I have found no evidentiary support in the record. The stipulating parties provide a table on Page 2 of NW Natural-Staff-CUB/201, but the table provided no clarity surrounding the calculation, other than that the calculation is some sort of "with and without" analysis.

Further, the testimony supporting the Contested Stipulation does not contain any discussion of how that value was calculated, nor were workpapers provided along with the Contested Stipulation.

AWEC even issued discovery requests for those workpapers prior to the filing of the supporting testimony, but those workpapers only arrived a few days prior to the filing due date of this testimony. AWEC has had only limited opportunity to review NW Natural's calculation of the Interim Period tax savings and has already identified a significant number of issues, hence the recommendation to address the final balance through supplemental proceeding in the tax reform deferral docket, similar to Portland General Electric.

Q. WHY IS YOUR CALCULATION SO MUCH DIFFERENT THAN THAT OF NW NATURAL?

A. Based on my limited review of the workpapers, NW Natural appears to be using an entirely different approach than I recommended in testimony. In its Rebuttal and Sur-Rebuttal testimony, NW Natural denied that the Interim Period tax monies should go back to customers

in this docket. Accordingly, NW Natural never attempted to present or justify an approach different than what I recommended in Opening Testimony.

AWEC, on the other hand, provided a detailed approach for calculating the Interim Period tax reform monies in Direct Testimony. To determine the impact of tax reform, my approach determines the amount of normalized revenues collected in the rates on January 1, 2018.

It appears that NW Natural is using actual tax expenses as the basis for determining the impact of tax reform, rather than using the amount of revenues that have been collected for income taxes. The difference may be subtle, but it is very important to the calculation. From AWEC's perspective, the Interim Period deferral is concerned with the revenues the utility is collecting in rates for federal income taxes. The actual federal tax expenses of the utility in the Interim Period is irrelevant because rates are not based on actual tax expenses.

Q. WHY IS IT CRITICAL TO FOCUS ON REVENUES, RATHER THAN ACTUAL TAXES?

A. It is important to recognize that the Interim Period deferral is concerned with the normalized revenue requirement impact of the Tax Cut and Jobs Act ("TCJA") on rates, and not the actual taxes that the utility is paying in the Interim Period.

Administratively, it was impossible for the Commission to require every utility to file for new rates taking into consideration the TCJA on January 1, 2018, within the ten days or so from when the legislation was signed. Thus, working under the assumption that a utility's current rates provided it with the opportunity for a reasonable return, the Interim Period deferral measures the rate change that would have been necessary to provide the utility with the same return on equity as if the tax rate had not been enacted.

Basing the deferral on actual taxes paid is arbitrary because those actual taxes paid depend on non-normal conditions, as well as the efficacy with which the utility operates its business, and a myriad of other factors that are not considered for ratemaking. For example, some utilities may, for a variety of reasons, pay little or no federal income taxes.

Q. HOW DID YOU DETERMINE THE INTERIM IMPACT OF TAX REFORM IN YOUR OPENING TESTIMONY?

A. I used a rate base approach to determine the amount of revenues necessary to provide the utility with the same return on equity as if the tax rate had not been enacted. The tax impact on current rates is determined using NW Natural's current level of rate base and cost of capital. Under this method the "pre-tax" return on equity is used to determine the portion of revenues dedicated to paying federal income taxes, as show in the following formula:

RB * ROE / (1-T) * E% = Revenues for Taxes

Where: RB = Rate Base; ROE = Return on Equity;

T = Marginal Composite Tax Rate, and; E% = Equity %.

The above calculation is performed first based on the old 35% federal tax rate, and then again based on the new 21% federal tax rate.[13] The difference represents the estimate the revenue requirement savings associated with the lower rate.

Q. HAVE YOU UPDATED THAT CALCULATION?

A. Yes. On pages 4 and 5 of Exhibit AWEC/602, I have updated that calculation. Using the rate base methodology, my analysis supports an Interim Deferral Balance of $15,908,000, with annual amortization of $8,859,000.

[13] These equate to composite tax rates of 39.9% and 27.0%, after considering Oregon state federal income taxes.

Q. ARE THERE OTHER WAYS TO PERFORM THE CALCULATION?

A. Yes. I am aware of at least two other methods that have been used.

First, the federal income taxes in the revenue requirement calculation from utility's most recent rate case has been used in Washington for both Avista Utilities and Cascade Natural Gas Corporation to determine the amount of monies to return for the Interim Period.

Second, in Idaho the Commission has determined the amount of monies to return using the utility's 2017 results of operations. Using the 2017 results of operations, the Idaho Commission effectively determined the rate change that would have been necessary to provide the utility with the same return on equity as if the tax reform had been enacted 2017. I have performed the Idaho analysis on Pages 1-3 of Exhibit AWEC/602. The analysis produces a result that is in line with the rate base approach, supporting a total balance of $13,890,000 and amortization of $7,735,000. This is the amount and approach that I believe is the most reasonable for purposes of this proceeding and that I recommend above.

Q. WHY IS IT APPROPRIATE TO CONSIDER THIS ISSUE FURTHER IN THE DEFERRAL DOCKET?

A. There is still significant controversy surrounding the treatment of the Interim Period tax amounts. Accordingly, exploring these issues further in the deferral docket, while beginning provision amortization on November 1, 2018, is appropriate.

d. <u>The Commission Should Not Accept the Average Rate Assumption Methodology for Excess Deferred Federal Income Taxes</u>

Q. DOES AWEC OBJECT TO THE AMOUNT OF EDFIT AMORTIZATION IDENTIFIED IN THE STIPULATION?

A. I continue to have concerns with the methodological assumptions used to calculate Excess Deferred Federal Income Taxes. Notwithstanding, AWEC is in general agreement with the

EDFIT balances and amortization amounts that have been identified in the Contested Stipulation.

As discussed earlier in testimony, AWEC does recommend that all items of EDFIT—including the amounts associated with customer margins—be returned to ratepayers beginning on November 1, 2018, and not earmarked to pay down the PBA balances.

Notwithstanding, one issue remains with respect to NW Natural's purported use of the Average Rate Assumption Methodology ("ARAM"). Utilities that use composite depreciation rates to calculate accumulated book reserves lack the sufficient vintage data to perform the ARAM. NW Natural's calculation is based on manufactured book depreciation reserve values, which do not tie to the book depreciation reserves calculated in the depreciation study. AWEC recommends that the Commission acknowledge that, by accepting the EDFIT amortization values identified in the Contested Stipulation, it is not endorsing the methodology NW Natural used to calculate the ARAM, nor any other methodological assumptions that were employed when arriving at the stipulated amounts.

Q. WHY DOES AWEC SUPPORT THE STIPULATED PROTECTED EDFIT VALUES?

A. For plant-related EDFIT, I calculated $3,421,941, using the Alternative Method. The Contested Stipulation provides for $3,263,000 of plant-related EDFIT amortization, which is within a range of reasonableness of the value I had calculated.

Q. HOW SHOULD THE UNPROTECTED EDFIT AMOUNT DUE TO TRANSPORTATION CUSTOMERS BE RETURNED?

A. The $6,700,000 of unprotected EDFIT funds NW Natural proposes to earmark for the PBA balance should be refunded to transportation customers, in the same way that the $14,640,000 of unprotected EDFIT due to sales customers is being refunded to sales customers. Treating

these two items differently is discriminatory towards transportation customers, who would not receive the same treatment as sales customers with respect to EDFIT. Further, AWEC would accept a five-year amortization, which is the same period used for the refunds due to sales customers. In my Opening Testimony, I had recommended a four-year amortization for these items, but five years is also reasonable.

Q. WHY DOES AWEC RECOMMEND THE COMMISSION NOT ACCEPT THE ARAM FOR CALCULATING EDFIT?

A. Paragraph 19 of the Contested Stipulation contains the normal disclaimer language, disclaiming any methodological assumptions used to arrive at the stipulated result. Notwithstanding, the representation in the Contested Stipulation specifically identifies the ARAM methodology; it is therefore appropriate for the Commission to acknowledge that the issues surrounding the use of the ARAM have not been resolved in this case, and that parties are not foreclosed from proposing a different methodology in the future. To support this recommendation, I offer a brief synopsis of AWEC's concerns, which I believe continue to warrant future consideration.

Q. WHAT ARE EXCESS DEFERRED FEDERAL INCOME TAXES?

A. The TCJA codifies several normalization provisions surrounding the treatment of EDFIT, which prescribes specific treatment of the balance sheet impacts of the tax law change for public utilities. Similar provisions were put into place when the Tax Reform Act of 1986 was enacted.[14]

Effectively, EDFIT represents a financial gain to the utility, and absent the TCJA normalization provisions surrounding EDFIT, a utility might have claimed that it was entitled

[14] See, e.g., PLR 200743030.

to retain those benefits. Or, perhaps ratepayers might have claimed that they should receive those gains through a single lump-sum payment. The TCJA, however, simplifies the ratemaking treatment surrounding the tax changes by prescribing the specific methods that must be used by regulators to account for the EDFIT benefits associated with plant balances, avoiding some controversy over the way that those amounts get returned to ratepayers.

Under Generally Accepted Accounting Principles ("GAAP"), the general rule is that when a change in the tax rate is enacted into law, the effects of the change must be reported in the period that includes the "enactment date."[15] The normalization requirements for EDFIT in IRC § 168(i)(9), however, provide an exception to that general rule for public utilities.

For business enterprises other than a public utility, the change in tax rate results in material balance sheet impacts. For a non-utility business enterprise, deferred tax liabilities and assets must be revalued at the new tax rate. Most utilities have net deferred tax liability balances, which represent funds in the utility's possession being held in reserve to pay for taxes the utility must pay in the future. Thus, if the tax rate declines, the tax liability balance declines, resulting in the recognition of a gain, similar to the gain that occurs when the principal balance of a loan is forgiven. For non-utilities, this gain flows through the income statement in the current period, in one lump-sum.

For public utilities, however, the treatment is different. When implementing the normalization requirements of IRC § 168(i)(9)—a rare instance where the Internal Revenue Service may exercise authority over the specific ratemaking methodology that state regulatory

[15] See Financial Accounting Standards Board ("FASB"), Statement of Financial Accounting Standards No. ("SFAS") 109, Accounting for Income Taxes ¶ 27; See also FASB Accounting Standards Codification ("ASC") 740-25-47.

commissions use to establish public service rates—the balance sheet gains associated with the change in tax rate must remain on the public utility's balance sheet and be considered in rate base as an excess tax reserve, i.e., EDFIT. Further, rather than recording those benefits in one lump-sum, as required under GAAP, this ratemaking treatment requires the utility to recognize the financial gains associated with the lower tax rate over an extended period of time.

The amortization schedule is generally intended to correspond to the period over which the book-tax differences underlying EDFIT are expected to reverse, and two general methods are available to amortize the excess reserves—the Average Rate Assumption Methodology ("ARAM") and an Alternative Method.[16] The ARAM methodology is computationally detailed and requires the utility to amortize the EDFIT reserve by plant vintage, ratably in proportion to the reversal of the book-tax differences underlying the EDFIT reserve. Provided the utility possesses the vintage data necessary to perform the ARAM method, the utility must use the ARAM when establishing rates. If the vintage data is not available, the utility must use the Alternative Method. Under the Alternative Method, EDFIT is reversed based on the weighted average life or composite rate used to compute depreciation for, or ratably over, the remaining regulatory life of the property.

Q. DO THE IRS NORMALIZATION REQUIREMENTS APPLY TO ALL DEFERRED TAX BALANCES?

A. No. The IRS normalization requirements apply only to deferred tax balances associated with the use of accelerated depreciation—both the Modified Accelerated Cost Recovery System ("MACRS") and bonus depreciation—in IRC § 168k. Accordingly, normalization accounting

[16] The IRS has historically referred to the "Reverse South Georgia Method," although I used a generic term, Alternative Method, as used in the TCJA.

methods outlined in the TCJA only apply to deferred tax balances associated with utility plant. Those deferred tax balances are often referred to as being *protected.*

With respect to the other deferred tax balances, those are often referred to as *unprotected*, since state Commissions, through the use of regulatory accounting, have greater leeway in determining how the gains on those EDFIT balances get returned to ratepayers.

Q. DOES NW NATURAL HAVE THE DATA NECESSARY TO SUPPORT ITS CALCULATION OF THE ARAM?

A. No. NW Natural has not provided the data necessary to support the calculation of the ARAM, which I understand is being done using the PowerTax software. NW Natural uses composite depreciation rates to determine the amount of reserves to carry on its books. The composite rates are applied by FERC account and are not meant to assign any particular amount of accumulated depreciation to any particular vintage. The reserves are assigned to the surviving vintages on a theoretical basis using the shape of the survivor curve to determine the portion of each vintage that has been reserved. The PowerTax modules appear to be making a number of assumptions that reserves have accumulated to the vintages in proportion to book values, which is not how the depreciation study operates. The TCJA provided utilities with the ability to use the Alternative Method explicitly in recognition of the fact that utilities.

Q. DID YOU REQUEST FOR NW NATURAL TO PROVIDE THE DATA NECESSARY TO SUPPORT THE CALCULATION OF THE ARAM?

A. Yes. To perform the ARAM properly, one must be able to calculate the amount of book-tax reversals by FERC account and vintage. When asked again to supply this data to Support NW Natural's calculation of $3,263,000, NW Natural objected and was not willing to provide the data. NW Natural stated that to calculate the EDFIT by FERC account would require 150

hours of work, presumably because NW Natural would have to manufacture the data based on the programming logic used in the PowerTax software.

When considering the Contested Stipulation, much of this controversy is moot, since NW Natural's calculation is very close to the amount I calculate using the Alternative Method. This issue, however, may become more significant in future rate proceedings; accordingly, I think it is appropriate for the Commission to acknowledge that AWEC is not prohibited from raising these, and potentially other, points of controversy in future proceedings.

III. CONCLUSION

Q. PEASE SUMMARIZE YOUR CONCLUSION.

A. Fundamentally, it is too late in this proceeding to address complicated issues of ratemaking and policy such as the tax and pension issues addressed in the Contested Stipulation. For the reasons identified above, the ratemaking treatment outlined in the Contested Stipulation is not fair, just, reasonable or supported by the evidence. AWEC respectfully requests that the Commission consider the four objections identified above and accept AWEC's proposed remedies to those objections.

Q. DOES THIS CONCLUDE YOUR OBJECTIONS TESTIMONY?

A. Yes.

NW Natural

Rates & Regulatory Affairs
UG 344
2017 General Rate Revision
Data Request Response

Request No.: UG 344 AWEC (fka NWIGU) DR 49
Reference the Multi-Party Second Partial Stipulation, Paragraph 1: Please provide a description of the methodology used to calculate the respective Excess Tax Reserve amounts for Plant, Other Non-Plant, and Non-Plant Gas Reserves.

Response:

Federal accumulated deferred income taxes (ADIT) were remeasured in December of 2017, the enactment period of the TCJA, using the newly lowered income tax rate. The change in ADIT was determined by measuring the federal temporary differences using a 21 percent federal statutory income tax rate and comparing this result to the federal ADIT balance existing immediately prior to the remeasurement.

Please see document identified below which was previously provided in response to AWEC (fka NWIGU) DR 38. This document includes all calculations supporting the remeasurement of accumulated deferred income taxes, including utility excess deferred income taxes, in an electronic spreadsheet with all formulas intact.

CONFIDENTIAL UG 344 NWIGU DR 38 – Attachment 1.xlsx

NW Natural

Rates & Regulatory Affairs
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Data Request Response

Request No.: UG 344 AWEC (fka NWIGU) DR 50
Reference the Multi-Party Second Partial Stipulation, Paragraph 1: Please provide workpapers detailing the calculation of the $140.62 million in excess tax reserves for plant by FERC account.

Response:

NW Natural objects to this data request as unduly burdensome. The Company maintains tax and book accounting detail in separate data systems and preparing the analysis at this level of detail would be a significant effort. The Company estimates that it would take in excess of 150 hours to fully respond to this request.

Without waiving its objection, NW Natural states that it did not perform the remeasurement of accumulated deferred income taxes, including utility excess deferred income taxes, at a FERC account level. Instead, the remeasurement of deferred income taxes was a GAAP / Regulatory financial statement exercise performed in December of 2017, and as such it was performed at the general ledger account level. The workpapers supporting the remeasurement of deferred taxes was previously provided as attachment to NWIGU DR 38. See **CONFIDENTIAL UG 344 NWIGU DR 38 – Attachment 1.xlsx.**

NW Natural

Rates & Regulatory Affairs
UG 344
2017 General Rate Revision
Data Request Response

Request No.: UG 344 AWEC (fka NWIGU) DR 51
Reference the Multi-Party Second Partial Stipulation, Paragraph 1. Does the $140.62 million of excess tax reserves for plant reflect actual depreciation expenses claimed on NW Natural's 2017 tax return, if no please recalculate the figure based on actual depreciation expenses claimed on NW Natural's 2017 Tax return, which was presumably filed before Sept 17, 2018.

Response:

NW Natural's 2017 calendar year corporate income tax return is due to be filed on or before October 15, 2018 (see IRS Publication 509 (v2018), page 5, for the corporate income tax return due date). The tax return is still being prepared, and as such, there is no additional data available at this time.

NW Natural

Rates & Regulatory Affairs
UG 344
2017 General Rate Revision
Data Request Response

Request No.: UG 344 AWEC (fka NWIGU) DR 52
Does the NW Natural agree that, for book accounting purposes, it uses a "group" system of depreciation accounting, based on FERC account groups. If no, please explain.

Response:

NW Natural's annual book depreciation rates are developed for each FERC plant account classification, of which there are many. The depreciation rate developed for each FERC plant account is then applied to the assets within that respective FERC plant account to determine depreciation expense and accumulated depreciation. In other words, the development of an annual rate may be performed at a FERC plant account, or "group" level, but the actual depreciation accounting is performed and tracked at a more granular level.

NW Natural

Rates & Regulatory Affairs
UG 344
2017 General Rate Revision
Data Request Response

Request No.: UG 344 AWEC (fka NWIGU) DR 53
Does NW Natural track accumulated depreciation vintage within each FERC account? If yes, please provide accumulated depreciation by vintage and by FERC account as of 12/31/2017.

Response:

NW Natural maintains plant records with sufficient detail to determine accumulated depreciation by vintage and FERC account. We previously provided AWEC with accumulated depreciation by vintage, for the calendar years ending 2017, 2018, and 2019, in document UG 344 NWIGU DR 42 Attachment 8 - Accumulated Depreciation.xlsx. The response to DR 42 also noted that this was the same information used by NW Natural to determine the average rate assumption method (ARAM) amortization.

Included with this response is CONFIDENTIAL UG 344 AWEC DR 53 Attachment 1.xlsx, which includes accumulated depreciation by vintage and by FERC account as of December 31, 2017. The total vintage accumulated depreciation figures provided in this document tie to the vintage data included in the response previously provided to DR 42 referenced above.

Please note the vintage and FERC data provided is for the vintage years from 1981 through 2017. As previously discussed in the response to UG 344 NWIGU DR3, benefits from accelerated income tax depreciation in years before 1981 was previously flowed through to customers on an annual basis during those periods.

NW Natural

Rates & Regulatory Affairs
UG 344
2017 General Rate Revision
Data Request Response

Request No.: UG 344 AWEC (fka NWIGU) DR 54
Does NW Natural agree that, for book accounting purposes, it does not use a unit system of depreciation accounting, through which it can determine the precise amount of depreciation expenses attributed to each individual asset on its balance sheet. If no, please explain.

Response:

No, NW Natural's book accounting system maintains asset level records, including accumulated depreciation.

For reference, please refer to document CONFIDENTIAL AWEC DR 54 Attachment 1.xlsx, which details the accumulated book depreciation for all of the individual assets comprising vintage year 2016 in FERC account 361.11. This detail ties to the vintage and FERC level detail provided in document CONFIDENTIAL UG 344 AWEC DR 53 Attachment 1.xlsx.

NW Natural

Rates & Regulatory Affairs
UG 344
2017 General Rate Revision
Data Request Response

Request No.: UG 344 AWEC (fka NWIGU) DR 55
Does the NW Natural agree that, for tax accounting purposes, it uses system of depreciation that is different than used for tax accounting purposes, grouped by vintage and MACRS (or other relevant tax depreciation system) life. If no, please explain in detail the grouping that is used to calculate tax depreciation expenses.

Response:

Although this DR inquiry refers to a comparison between "tax accounting" and "tax accounting", we interpret the question to be inquiring if plant balances are tracked for income tax depreciation purposes by MACRS classification rather than by FERC classification. If this interpretation is incorrect, please resubmit or clarify the inquiry.

The income tax depreciation is generally tracked by vintage and by FERC account, consistent with the annual FERC account additions as reported for book accounting purposes. FERC plant accounts are very specific as to the nature of the underlying assets. As a result, individual FERC plant accounts can be matched to a specific income tax method and life under MACRS.

NW Natural

Rates & Regulatory Affairs
UG 344
2017 General Rate Revision
Data Request Response

Request No.: UG 344 AWEC (fka NWIGU) DR 56
Reference the Multi-Party Second Partial Stipulation, Paragraph 2: In performing the Average Rate Assumption Method ("ARAM"), did NW Natural calculate the timing differences, and the corresponding reversals, by FERC account and Vintage? If no, please provide an explanation of the granularity and the grouping used in the ARAM calculation.

Response:

The Average Rate Assumption Method (ARAM) schedule was prepared by NW Natural on a vintage by vintage level as required. The calculation was not expanded to detail individual FERC account detail by vintage. It's anticipated that performing the calculation at a vintage level would result in an identical result as performing the calculation by FERC vintage account first and then summing at the vintage level. The vintage by vintage analysis was clarified in Internal Revenue Service Private Letter Ruling 200743030, which AWEC attached as an exhibit to its previous testimony in this proceeding (see AWEC 503, excerpted below).

ARAM is a vintage by vintage analysis and the IRS warns not to circumvent this approach.

> AWEC/503, Mullins/5:
>
> "Rev. Proc. 88-12, 1988-1 C.B. 637, provides further guidance as to the application of the ARAM to the excess tax reserve. Section 2.04 of Rev. Proc. 88-12 provides that under the ARAM, excess tax reserves pertaining to a particular vintage or vintage account are not flowed through to ratepayers until such time as the timing differences in the particular vintage account reverse. Moreover, it is a violation of section 203(e) of the Act for taxpayers to adopt any accounting treatment that, directly or indirectly, circumvents the rule set forth in the previous sentence."

NW Natural

Rates & Regulatory Affairs
UG 344
2017 General Rate Revision
Data Request Response

Request No.: UG 344 AWEC (fka NWIGU) DR 57
Reference the Multi-Party Second Partial Stipulation, Paragraph 2: Please provide a table showing the derivation of the ARAM and the reversals by FERC account and by vintage, or the greatest level of granularity employed by NW Natural in the ARAM calculation.

Response:

Please see CONFIDENTIAL UG 344 AWEC DR 57 Attachment 1.xlsx.

NW Natural

Rates & Regulatory Affairs
UG 344
2017 General Rate Revision
Data Request Response

Request No.: UG 344 AWEC (fka NWIGU) DR 58
Please explain how book depreciation reserves, which are not recorded by vintage, were allocated to vintages when of performing the ARAM and determine the timing of the reversal of those reversals of timing differences with respect to depreciation. When calculating the 3.2 million, please describe how book depreciation reserves, which are calculated on a group basis, were allocated the vintages with respect to each FERC account.

Response:

This DR inquiry includes certain assumptions, stated as though they were facts by AWEC, that are not supported by the record in this proceeding. Book depreciation reserves are not 'allocated.' As noted in the response to AWEC DR 54, NW Natural's book accounting system maintains asset level records, including accumulated depreciation.

NW Natural maintains plant records with sufficient detail to determine accumulated depreciation by vintage and FERC account. As a result, NW Natural is required to utilize the average rate assumption method (ARAM) to determine the excess deferred income tax amortization speed limit.

We previously provided AWEC with accumulated book and tax depreciation by vintage, for the calendar years ending 2017, 2018, and 2019, in document UG 344 NWIGU DR 42 Attachment 8 - Accumulated Depreciation.xlsx. The response to DR 42 also noted that this was the same information used by NW Natural to determine the average rate assumption method (ARAM) amortization.

Included with the response to UG 344 AWEC DR 53 is CONFIDENTIAL UG 344 AWEC DR 53 Attachment 1.xlsx, which includes accumulated book depreciation by vintage and by FERC account as of December 31, 2017. The total vintage accumulated depreciation figures provided in this document tie to the vintage data included in the response previously provided to DR 42 referenced above.

In addition, NW Natural provided CONFIDENTIAL AWEC DR 54 Attachment 1.xlsx, which details the accumulated book depreciation for all of the individual assets comprising vintage year 2016 in FERC account 361.11. This detail ties to the vintage and FERC level detail provided in document CONFIDENTIAL UG 344 AWEC DR 53 Attachment 1.xlsx.

NW Natural

Rates & Regulatory Affairs
UG 344
2017 General Rate Revision
Data Request Response

Request No.: UG 344 AWEC (fka NWIGU) DR 59
Please provide book depreciation reserves used in the ARAM calculation by FERC account and vintage as of 12/31/2017.

Response:

This inquiry appears to request information identical to that requested in AWEC DR 53. Please see the response to AWEC DR 53. If AWEC intended to solicit different information, please resubmit or clarify the inquiry.

NW Natural

Rates & Regulatory Affairs
UG 344
2017 General Rate Revision
Data Request Response

Request No.: UG 344 AWEC (fka NWIGU) DR 60
Reference the Multi-Party Second Partial Stipulation, Exhibit A: Please provide workpapers used to calculation $3.26 million Plant EDFIT amortization and explain why the dollar figure does not change year to year.

Response:

Please see joint testimony in support of the second partial stipulation filed on September 14, 2018 for a detailed description of the calculation of the $3.26 million (NW Natural-Staff-CUB/200, Borgerson, Wilson, Gardner, and Jenks/10:18-21 and 11:1).

Please also see the joint testimony in support of the second partial stipulation filed on September 14, 2018 for a discussion of why the amount is fixed on an annual basis for a maximum of five years (NW Natural-Staff-CUB/200, Borgerson, Wilson, Gardner, and Jenks/11:1-6 and 12:1-7).

Providing customers with a consistent and level amount of annual benefit from plant related excess deferred income taxes is consistent with Internal Revenue Service Private Letter Ruling 200743030, which AWEC attached as an exhibit to its previous testimony in this proceeding (see AWEC 503).

The average rate assumption method (ARAM) of amortization is a speed limit test and it is not the required schedule for amortizing EDIT:

> See AWEC/503, Mullins/5 (attached IRS document):
>
> Section 203(e) of the Act limits the rate at which the excess tax reserve may be reduced and flowed through to the utility's customers in setting rates. It does not require the utility to flow through the excess tax reserve to its customers, but permits the utility to do so provided the reduction to cost of service is not more rapidly than would be under the ARAM. Thus, section 203(e) of the Act imposes a limitation on when the excess tax reserve may be returned to the utility's customers in the form of reduced rates.

NW Natural

Rates & Regulatory Affairs
UG 344
2017 General Rate Revision
Data Request Response

Request No.: UG 344 AWEC (fka NWIGU) DR 61
Reference the Multi-Party Second Partial Stipulation, Paragraph 10: Please provide workpapers supporting the calculation of the $5.9 million interim tax savings, along with a detailed description of how that value was calculated.

Response:

Each quarter NW Natural prepares forecasted regulatory earnings. The $5.9 million interim tax savings utilized this forecasted earnings model for the first ten months of 2018 (the interim period).

The model uses many inputs from actual data (January 2018 through June 2018) and forecast data (July 2018 through October 2018) from our most recent financial forecast. Actual results are taken from our accounting records and financial forecast from our UI Planner model. The UI Planner model also takes actual data and re-forecasts future periods. The inputs are compiled on a monthly basis and included within the model template. Below is a list of inputs that were included within the model:

Sales Revenue	Gas Costs	WARM Revenues	Decoupling Revenue	Other Amortization Revenue/Expense	Transportation Revenue
Misc. Revenue	Property Tax Expense	Franchise Taxes	Payroll Taxes	Regulatory Fee	DOE Fee
Other Taxes	Depreciation Expense	O&M Expense	SRRM Expense	Uncollectible Accrual Expense	Capital Structure
Gross Plant	Accumulated Depreciation	Other Rate Base Items	Long Term Debt Rate	Permanent Tax Differences	Tax Credits and Adjustments
Deferred Income Taxes	Allocation Factors				

The process of gathering data and updating the model template are analogous to our results of operations (RG 40) report. Allocation factors were taken from the 2017 results of operations for state allocation.

The model dynamically calculates tax expense using statutory tax rates. Once the model template was fully updated with the forecasted ten month period, we simply changed the federal tax rate from 35% to 21%, holding everything else equal. The difference in the net operating revenues, $4,331,000, were then grossed up to arrive at $5,933,000.

We do not expect the net operating revenues to change significantly due to predictable earnings during the summer and early fall months.

Please see “Confidential UG 344 AWEC (fka NWIGU) DR 61 Attachment 1.xlsx” for the full model.

NW Natural

Rates & Regulatory Affairs
UG 344
2017 General Rate Revision
Data Request Response

Request No.: UG 344 AWEC (fka NWIGU) DR 62
Reference the Multi-Party Second Partial Stipulation, Paragraph 9: In NW Natural/2600 at 9, in response to AWEC's position to terminate the pension balancing account and transition to FAS 87 expense, NW Natural stated that "NW Natural does not believe it is appropriate to terminate the Pension Balancing Account in this docket." Please explain why NW Natural now believes that it is appropriate to terminate the pension balancing account in this docket and transition to FAS 87 expense.

Response:

NW Natural believes that the settlement represents a reasonable compromise of the parties' positions, and that the settlement package as a whole represents a reasonable way forward with respect to the pension balancing account. NW Natural's position was, and still is, that the termination of the balancing account, absent the other provisions of the settlement, would not be appropriate.

NW Natural

Rates & Regulatory Affairs
UG 344
2017 General Rate Revision
Data Request Response

Request No.: UG 344 AWEC (fka NWIGU) DR 63
Reference the Multi-Party Second Partial Stipulation, Paragraph 9: Does NW Natural agree that the pension balancing account did not function as intended and as designed in the Stipulation in UM 1475? If yes, please explain why it is reasonable for ratepayers to bear all of the cost associated with the failed mechanism.

Response:

The pension balancing account functioned as intended in terms of its ability to hold the amount of FAS 87 expense in rates constant, and collect in the account the difference between the amount in rates and the amount of annual expense. However, the balance that remains in the account at this time was not as expected by the parties to the stipulation, and the timeframe in which the balance was expected to reverse was not realized. It is reasonable for ratepayers to bear the costs associated with the mechanism for the reasons described in the joint testimony supporting the stipulation.

Date: September 17, 2018

TO:
CHAD STOKES
ALLIANCE OF WESTERN ENERGY CONSUMERS
CABLE HUSTON LLP
1001 SW FIFRTH VE SUITE 2000
cstokes@cablehuston.com

FROM: John Fox
Senior Financial Analyst
Energy Rates, Finance and Audit Division

OREGON PUBLIC UTILITY COMMISSION
Docket No. UG 344 – AWEC's Data Request filed September 13, 2018

AWEC's Data Request DR 01:
Reference the Multi-Party Second Partial Stipulation, Paragraph 10: Did Staff perform an earnings test period to prior to determining the reasonableness of the amounts identified for amortization against the Pension Balancing Account balance? If yes, please provide a copy of such analyses.

Staff Response to AWEC's DR 01:
Yes. Referencing the most recent results of operations filed by the Company, the threshold for earnings sharing is 10.66%.[1]
Staff identified the change in federal tax expense that would have been necessary to trigger earnings sharing for 2017 using the goal seek function in the underlying excel model. The required decrease in tax would be $22,100 – 31,655 = ($9.555) million.

The results of this analysis are presented on the following page.

The sum of the Company's reported interim tax savings, protected EDIT Plant Amortization, and unprotected EDIT Non-Plant Amortization for 2018 is $9.761 million (including gross up).[2] Accordingly 98% these savings, had they been realized in 2017, would have been below the earnings threshold.

[1] *See In the Matter of Northwest Natural Gas Company, dba NW Natural, 2018 Spring Earnings Review*, Docket No. UM 903, Order No. 18-254, Appendix A, page 4 of 5 (Jul. 03, 2018).
[2] *See In the Matter of NORTHWEST NATURAL GAS COMPANY, dba NW NATURAL, Application for Authorization to Defer Certain Expenses Associated with the 2018 US Tax Cuts and Jobs Act.*, Supplemental Application filed 7/16/2018 and NW Natural/2501, Borgerson/1.

2017 Reported Results Order 18-254 (UM 903)	2017 Reported Results Proforma at 10.66% ROE
Results after Type II	Results after Type II
(g) = (c) + (f)	(g) = (c) + (f)
$652,927	$652,927
0	0
(6,188)	(6,188)
0	0
17,987	17,987
3,609	3,609
668,336	668,336
287,282	287,282
752	752
142,291	142,291
430,325	430,325
31,655	22,100
7,511	7,511
20,118	20,118
23,978	23,978
71,062	71,062
584,650	575,095
$83,686	$93,241
$2,765,246	$2,765,246
(1,227,221)	(1,227,221)
1,538,025	1,538,025
(2,852)	(2,852)
(4,446)	(4,446)
61,966	61,966
336	336
(431,266)	(431,266)
0	0
0	0
$1,161,763	$1,161,763
7.20%	8.03%
8.998%	10.665%

Interim Period Deferral Calculation (Using the Idaho Method)

In Thousands

		2017 Results	Type 1 Adjustments	Results after Type I	Type II Adjustments	Results after Type II	AMA	Results after AMA	Impact of Tax Reform	Results w/ Tax Reform	Revenue for Same Return	Interim Per. Results
		(a)	(b)	(c)	(d)	(e) = (c) + (d)	(f)	(g) = (e) + (f)	(h) See Note	(i) = (g) + (h)	(j)	(l) = (i) + (j)
	Operating Revenues											
1	**Sale of Gas**	671,195	-18,268	652,927	0	652,927		652,927		652,927	-16,049	636,878
2	**WARM Revenues**	-16,870	16,870	0	0	0		0		0		0
3	**Revenue & Technical Adjustments**	-6,188	0	-6,188	0	-6,188		-6,188		-6,188		-6,188
4	**Decoupling Adjustments**	8,638	-8,638	0	0	0		0		0		0
5	**Transportation**	17,987	0	17,987	0	17,987		17,987		17,987		17,987
6	**Miscellaneous Revenues**	3,609	0	3,609	0	3,609	2,442	6,051		6,051		6,051
7	**Total Operating Revenues**	678,371	-10,036	668,335	0	668,335	2,442	670,777	0	670,777		654,728
	Operating Revenue Deductions											
8	**Gas Purchased**	295,366	-8,085	287,282	0	287,282		287,282		287,282		287,282
9	**Uncollectible Accrual for Gas Sales**	771	-19	752	0	752		752		752		752
10	**Other Operating & Maintenance Expenses**	146,326	-4,035	142,291	0	142,291		142,291		142,291		142,291
11	**Total Operating & Maintenance Exp.**	442,463	-12,139	430,325	0	430,325	0	430,325	0	430,325		430,325
12a	**Federal Income Tax**	30,467	1,188	31,655	0	31,655	790	32,445	-12,905	19,540		19,540
12b	**Protected EDFIT Amort**	0		0		0		0	-3,263	-3,263		-3,263
13	**State Excise**	7,231	280	7,511	0	7,511	186	7,697		7,697		7,697
14	**Property Taxes**	20,386	-268	20,118	0	20,118		20,118		20,118		20,118
15	**Other Taxes**	24,016	-38	23,978	0	23,978		23,978		23,978		23,978
16	**Depreciation & Amortization**	71,062	0	71,062	0	71,062		71,062		71,062		71,062
17	**Total Operating Revenue Deductions**	595,625	-10,977	584,649	0	584,649	976	585,625	-16,168	569,457		569,457
18	**Net Operating Revenues**	82,746	941	83,686	0	83,686	1,466	85,152	16,168	101,320		85,272
	Average Rate Base											
19	**Utility Plant in Service**	2,766,558	-1,312	2,765,246	0	2,765,246		2,765,246		2,765,246		2,765,246
20	**Accumulated Depreciation**	-1,227,221	0	-1,227,221	0	-1,227,221		-1,227,221	1,632	-1,225,590		-1,225,590
21	**Net Utility Plant**	1,539,337	-1,312	1,538,025	0	1,538,025	0	1,538,025	1,632	1,539,657		1,539,657
22	**Aid in Advance of Construction**	-2,852	0	-2,852	0	-2,852		-2,852		-2,852		-2,852
23	**Customer Deposits**	-4,446	0	-4,446	0	-4,446		-4,446		-4,446		-4,446
24	**Materials & Supplies**	61,966	0	61,966	0	61,966		61,966		61,966		61,966
25	**Leasehold Improvements**	336	0	336	0	336		336		336		336
26	**Accumulated Deferred Income Taxes**	-431,266	0	-431,266	0	-431,266		-431,266		-431,266		-431,266
27	**Total Rate Base**	1,163,075	-1,312	1,161,763	0	1,161,763	0	1,161,763	1,632	1,163,395		1,163,395
28	**Rate of Return**	7.11%		7.20%		7.20%		**7.33%** (y)		8.71%		**7.33%** (z)

Note: EDFIT is from Multi-Party Settlement and impact on tax expense was calculated as follows:

Line 12a Federal Tax Expense	32,445
Old Tax Rate	35%
Taxable Income	92,700
Less: Loss of Meals Deduction	346
Adjusted Taxable Income	93,046
New Tax Rate	21%
Tax Expense with Tax Reform	19,540
Delta	12,905

Proof (y) - (z): **0.00%**

Northwest Natural Gas Corporation
Calculation of the Interim Period Deferral Balance
Using the Idaho Method
In Thousands

1 Annual Revenues To Hold Return Constant		**(16,049)**										
Monthly Deferral Calculation		**1/1/2018**	**2/1/2018**	**3/1/2018**	**4/1/2018**	**5/1/2018**	**6/1/2018**	**7/1/2018**	**8/1/2018**	**9/1/2018**	**10/1/2018**	**Total**
2 Total Deferred Amounts	Line 1 / 12	(1,337)	(1,337)	(1,337)	(1,337)	(1,337)	(1,337)	(1,337)	(1,337)	(1,337)	(1,337)	(13,374)
3 Carrying Charge (Per Mo. at Pre-tax ROR)		0.75%	0.75%	0.75%	0.75%	0.75%	0.75%	0.75%	0.75%	0.75%	0.75%	
4 Balance												
5 Beginning Balance		-	(1,342)	(2,695)	(4,058)	(5,431)	(6,814)	(8,208)	(9,613)	(11,028)	(12,453)	-
6 Deferral	Line 2	(1,337)	(1,337)	(1,337)	(1,337)	(1,337)	(1,337)	(1,337)	(1,337)	(1,337)	(1,337)	(13,374)
7 Interest	Line 3 * (Line 4 + Line 5 / 2)	(5)	(15)	(25)	(36)	(46)	(56)	(67)	(78)	(88)	(99)	(516)
8 Ending Balance	∑ Lines 5:7	(1,342)	(2,695)	(4,058)	(5,431)	(6,814)	(8,208)	(9,613)	(11,028)	(12,453)	(13,890)	(13,890)

Northwest Natural Gas Corporation
Interim Period Deferrral (Idaho Mehod) Amortization
In Thousands

Month	Beg Balance	Amortization	Interest Rate	Interest	Ending Balance	
5/1/2018	(13,890)	**645**	0.75%	(115)	(13,359)	
6/1/2018	(13,359)	*645*	0.75%	(111)	(12,825)	
7/1/2018	(12,825)	*645*	0.75%	(107)	(12,287)	
8/1/2018	(12,287)	*645*	0.75%	(102)	(11,745)	
9/1/2018	(11,745)	*645*	0.75%	(98)	(11,199)	
10/1/2018	(11,199)	*645*	0.75%	(94)	(10,648)	
11/1/2018	(10,648)	*645*	0.75%	(90)	(10,094)	
12/1/2018	(10,094)	*645*	0.75%	(86)	(9,535)	
1/1/2019	(9,535)	*645*	0.75%	(82)	(8,972)	
2/1/2019	(8,972)	*645*	0.75%	(77)	(8,405)	
3/1/2019	(8,405)	*645*	0.75%	(73)	(7,834)	
4/1/2019	(7,834)	*645*	0.75%	(69)	(7,258)	
5/1/2019	(7,258)	*645*	0.75%	(64)	(6,678)	
6/1/2019	(6,678)	*645*	0.75%	(60)	(6,093)	
7/1/2019	(6,093)	*645*	0.75%	(56)	(5,504)	
8/1/2019	(5,504)	*645*	0.75%	(51)	(4,911)	
9/1/2019	(4,911)	*645*	0.75%	(47)	(4,313)	
10/1/2019	(4,313)	*645*	0.75%	(42)	(3,711)	
11/1/2019	(3,711)	*645*	0.75%	(38)	(3,104)	
12/1/2019	(3,104)	*645*	0.75%	(33)	(2,492)	
1/1/2020	(2,492)	*645*	0.75%	(29)	(1,876)	
2/1/2020	(1,876)	*645*	0.75%	(24)	(1,256)	
3/1/2020	(1,256)	*645*	0.75%	(19)	(630)	
4/1/2020	(630)	*645*	0.75%	(14)	(0)	<-Goal Seek to Zero
Annual Amortization (Pre-tax):		**7,735**				

Northwest Natural Gas Corporation
Calculation of the Interim Period Deferral Balance
Using the Rate Base Approach
In Thousands

Line				
1	**Restating Adjustment Calculation Using Gross-up Method:**			
2	Rate Base	Un-adjusted Base Year	$1,088,556	
3	Equity %		50.00%	
4	Equity Portion of Rate Base	Line 2 * Line 3	544,278	
5	Return On Equity	2012 GRC	9.40%	
6	Pretax Return On Equity (35% Rate)	Line 5 * (1 - 39.9%)	15.65%	
7	Pretax Equity Returns Required (35% Rate	Line 4 * Line 5	85,185.05	
8	Pretax Return on Equity (21% Rate)	Line 7 * (1 - 27.0%)	12.88%	9.06%
9	Pretax Equity Return (21% Rate)	Line * Line 7	70,088.97	
10	**Annual Equity Return Differential (35% to 21% Rate)**	Line 9 * Line	**(15,096)**	
11	Less Incremental Revenues on permanent Differences		835	
12	R&D Creidt		11	
13	**Deferred Tax Expense**		**(14,250)**	

14	**Monthly Deferral Calculation**		**1/1/2018**	**2/1/2018**	**3/1/2018**	**4/1/2018**	**5/1/2018**	**6/1/2018**	**7/1/2018**	**8/1/2018**	**9/1/2018**	**10/1/2018**	**Total**
	Monthly Return Diff. at Restated 21 %												
15	Tax Rate	Line 10 / 12	(1,188)	(1,188)	(1,188)	(1,188)	(1,188)	(1,188)	(1,188)	(1,188)	(1,188)	(1,188)	(11,875)
16	Monthly EDFIT Amortization	Tab 11	(272)	(272)	(272)	(272)	(272)	(272)	(272)	(272)	(272)	(272)	(2,719)
17	Monthly EDFIT Amortization (Pretax)	Line 16 / (1-21%)	(344)	(344)	(344)	(344)	(344)	(344)	(344)	(344)	(344)	(344)	(3,442)
18	Total Deferred Amounts	Line 16 + Line 17	(1,532)	(1,532)	(1,532)	(1,532)	(1,532)	(1,532)	(1,532)	(1,532)	(1,532)	(1,532)	(15,317)
19	Carrying Charge (Per Mo. at Pre-tax ROR)		0.75%	0.75%	0.75%	0.75%	0.75%	0.75%	0.75%	0.75%	0.75%	0.75%	
20	Balance												
21	Beginning Balance		-	(1,538)	(3,087)	(4,647)	(6,220)	(7,804)	(9,401)	(11,009)	(12,630)	(14,263)	-
22	Deferral	Line 18	(1,532)	(1,532)	(1,532)	(1,532)	(1,532)	(1,532)	(1,532)	(1,532)	(1,532)	(1,532)	(15,317)
23	Interest	Line 19 * (Line 20 + Line 21 / 2)	(6)	(17)	(29)	(41)	(53)	(65)	(77)	(89)	(101)	(113)	(591)
24	Ending Balance	∑ Lines 21:23	(1,538)	(3,087)	(4,647)	(6,220)	(7,804)	(9,401)	(11,009)	(12,630)	(14,263)	(15,908)	(15,908)

Northwest Natural Gas Corporation
Interim Period Deferrral (Rate Base Mehod) Amortization
In Thousands

Month	Beg Balance	Amortization	Interest Rate	Interest	Ending Balance	
5/1/2018	(15,908)	**738**	0.75%	(131)	(15,301)	
6/1/2018	(15,301)	*738*	0.75%	(127)	(14,689)	
7/1/2018	(14,689)	*738*	0.75%	(122)	(14,073)	
8/1/2018	(14,073)	*738*	0.75%	(117)	(13,452)	
9/1/2018	(13,452)	*738*	0.75%	(113)	(12,826)	
10/1/2018	(12,826)	*738*	0.75%	(108)	(12,196)	
11/1/2018	(12,196)	*738*	0.75%	(103)	(11,561)	
12/1/2018	(11,561)	*738*	0.75%	(98)	(10,921)	
1/1/2019	(10,921)	*738*	0.75%	(94)	(10,276)	
2/1/2019	(10,276)	*738*	0.75%	(89)	(9,626)	
3/1/2019	(9,626)	*738*	0.75%	(84)	(8,972)	
4/1/2019	(8,972)	*738*	0.75%	(79)	(8,312)	
5/1/2019	(8,312)	*738*	0.75%	(74)	(7,648)	
6/1/2019	(7,648)	*738*	0.75%	(69)	(6,979)	
7/1/2019	(6,979)	*738*	0.75%	(64)	(6,304)	
8/1/2019	(6,304)	*738*	0.75%	(59)	(5,624)	
9/1/2019	(5,624)	*738*	0.75%	(54)	(4,940)	
10/1/2019	(4,940)	*738*	0.75%	(48)	(4,250)	
11/1/2019	(4,250)	*738*	0.75%	(43)	(3,555)	
12/1/2019	(3,555)	*738*	0.75%	(38)	(2,855)	
1/1/2020	(2,855)	*738*	0.75%	(33)	(2,149)	
2/1/2020	(2,149)	*738*	0.75%	(27)	(1,438)	
3/1/2020	(1,438)	*738*	0.75%	(22)	(722)	
4/1/2020	(722)	*738*	0.75%	(17)	0	<-Goal Seek to Zero

Annual Amortization (Pre-tax): **8,859**