

**BEFORE THE
PUBLIC UTILITY COMMISSION OF OREGON
UG 462**

In the Matter of)
)
NORTHWEST NATURAL GAS)
CORPORATION, dba NW NATURAL,)
)
Renewable Natural Gas Adjustment)
Mechanism - Dakota City.)

**REBUTTAL AND CROSS-ANSWER TESTIMONY OF
BRADLEY G. MULLINS
ON BEHALF OF
ALLIANCE OF WESTERN ENERGY CONSUMERS**

July 31, 2023

[REDACTED]

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I. INTRODUCTION AND SUMMARY

Q. ARE YOU THE SAME WITNESS THAT PREVIOUSLY FILED TESTIMONY IN THIS DOCKET?

A. Yes. I previously filed Opening Testimony on behalf of the Alliance of Western Energy Consumers (“AWEC”) in this docket.

Q. WHAT IS THE PURPOSE OF YOUR REBUTTAL AND CROSS-ANSWERING TESTIMONY?

A. In my Rebuttal and Cross-Answering Testimony I respond to NW Natural’s Reply Testimony on the Dakota City Project (“Dakota Project”), a renewable natural gas (“RNG”) processing facility in Dakota City, Nebraska. Specifically, I respond to issues regarding the interplay of Senate Bill (“SB”) 98 and the Climate Protection Plan (“CPP”), as well as issues surrounding the Investment Tax Credit (“ITC”) and rate spread. Further, I provide Cross-Answering Testimony in response to recommendations of Commission Staff (“Staff”) regarding the application of a cost sharing for the Dakota Project.

Q. WHAT ARE YOUR PRINCIPAL RECOMMENDATIONS AND CONCLUSIONS?

A. Based on my review of the Reply Testimony of NW Natural and the Opening Testimony of Staff and the Oregon Citizens’ Utility Board (“CUB”), I have revised some of my recommendations in my Opening Testimony. I recommend the Commission:

1. *Find that the Dakota Project was prudent in the context of CPP compliance, subject to certain ratepayer protections discussed below;*
2. *Adopt a sharing mechanism that balances the risks between NW Natural and customers consistent with the sharing mechanism approved for the Lexington RNG Project;*
3. *Require NW Natural to include the rate base benefits of the ITC in the Dakota Project revenue requirement so that rate payers receive the full benefit of the ITCs;*

1 4. *Hold ratepayers harmless if any ITCs are allocated, directly or indirectly, to BiocarbN*
2 *or Cross River Infrastructure Partners LLC working together as BioCross LLC*
3 *("BioCross") so that rate payers receive the full benefit of the ITCs; and,*

4 5. *Adopt NW Natural's rate spread proposal with a commitment to reevaluate the rate*
5 *spread associated with CPP compliance in NW Natural's next general rate case.*

6 **II. PRUDENCE**

7 **Q. DO YOU CONTINUE TO RECOMMEND THAT THE COMMISSION FIND THE**
8 **DAKOTA PROJECT TO BE A PRUDENT CPP INVESTMENT?**

9 A. Yes. As AWEC noted in Opening Testimony, RNG is currently one of the only viable options
10 for complying with the CPP. While AWEC had some concerns over the RNG production
11 levels and NW Natural's decision to pursue an RNG development rather than an offtake
12 agreement, AWEC is not contesting the prudence of NW Natural's decision to pursue the
13 Dakota Project as a CPP resource.

14 **Q. WHAT POSITION DOES NW NATURAL TAKE WITH RESPECT TO THE**
15 **INTERPLAY BETWEEN THE CPP AND SENATE BILL 98 FOR THE DAKOTA**
16 **PROJECT?**

17 A. NW Natural believes that the prudence of the Dakota Project must be measured against Senate
18 Bill ("SB") 98, stating that "the interaction between SB 98 and the CPP is not squarely before
19 the Commission in this docket because the decision to pursue the Dakota City RNG project
20 predates the CPP."¹

21 **Q. IS THE DISTINCTION NW NATURAL MAKES MEANINGFUL?**

22 A. Not necessarily. Regardless of whether "the decision to pursue the Dakota City RNG project
23 predates the CPP", the CPP exists now and the CPP has mandatory compliance obligations.
24 While NW Natural's decision to pursue the Dakota Project occurred when SB 98 was in effect,
25 the project contracts only predated the issuance of the final CPP rule by a short period of time.

¹ NW Natural/300, Chittam/3:8-10.

1 Presumably, NW Natural had been studying draft CPP rules for several months by that time
2 and should have been aware that the project it was planning may be necessary for CPP
3 compliance. Fundamentally, it makes little difference, however, which program is applied to
4 evaluate the prudence of the Dakota Project. Whether RNG is acquired under SB 98 or the
5 CPP, NW Natural still must demonstrate that the acquisition is prudent. Under both standards,
6 NW Natural is expected to procure the most cost effective RNG available, so whether the
7 acquisition is made voluntarily or not, the difference in the standard for judging prudence is not
8 necessarily meaningful. Notwithstanding, projects under SB 98 are compared to other SB 98
9 eligible projects in the prudence review, whereas CPP projects should be compared to all CPP
10 compliance instruments during a prudence review. As of the date of this testimony,
11 Community Climate Investments (“CCIs”) are not yet available for CPP compliance, and
12 therefore only other RNG projects should be used to judge the prudence of the Dakota Project.

13 **Q. ARE THE TWO STANDARDS CONTRADICTIONARY?**

14 A. No. The CPP is intended to cap emissions from natural gas on a declining scale, with the
15 primary compliance pathways being RNG, CCIs, and energy efficiency. This is a mandatory
16 program. In contrast, SB 98 allows, but does not require, NW Natural to procure RNG that
17 would otherwise not be allowed because it is not least cost least risk compared to traditional
18 natural gas. Also, SB 98 explicitly allows NW Natural to invest capital and own RNG
19 projects, rather than simply purchasing RNG commodity. Since SB 98 is voluntary and the
20 CPP is not, however, the requirements of the CPP must inherently be weighted more heavily
21 than SB 98 in NW Natural’s decision-making framework, and NW Natural must engage in a
22 least-cost / least-risk strategy for CPP compliance. It would be imprudent for NW Natural to

1 engage in a voluntary investment under SB 98, for example, when doing so would be an
2 imprudent means of complying with the CPP.

3 **Q. WHAT DO YOU RECOMMEND FOR THIS PROCEEDING?**

4 A. I recommend the Commission find that the Dakota Project is prudent in the context of CPP
5 compliance, subject to the ratepayer protections discussed below. While the prudence standard
6 could potentially be met under either program, AWEC recommends that the CPP be the basis
7 for any prudence finding, given its mandatory requirements.

8 **III. COST SHARING**

9 **Q. WHAT DID STAFF RECOMMEND WITH RESPECT TO COST SHARING?**

10 A. Staff states that in “Docket No. UI 451, the Commission approved multiple safeguards to
11 protect customers,” and that a “similar approach is warranted for the Dakota City Project.”²
12 While Staff did not propose a specific parameters, it generally recommended a cost-sharing
13 mechanism to “[p]rotect[] NWN customers in the event the facility underperforms.”³

14 **Q. WHAT COST SHARING MECHANISM WAS APPROVED IN UI 451 FOR THE**
15 **LEXINGTON RNG PROJECT?**

16 A. On April 1, 2022, Docket No. UI 451 Parties entered into a Comprehensive Settlement, which
17 among other things, established a cost sharing mechanism for the Lexington RNG Project.

18 Specifically, parties agreed to the following term:

19 Subject to a prudence review in a cost recovery proceeding, NW Natural may
20 seek recovery of all of its costs that do not exceed the average price per RTC of
21 the two lowest bids from NW Natural’s 2020 RFP that: i) meet all requirements
22 under ORS 757.390-398 and OAR Chapter 860, Division 150, and ii) could begin
23 deliveries in same timeframe as the Lexington RNG project. The Stipulating
24 Parties agree that this amount is equal to [Begin Confidential] [End Confidential].

² Staff/100, Drennen/4:2-3.

³ Staff/100, Drennen/11:14-15

1 For any costs that exceed this average price per RTC, NW Natural may only
2 recover 75% of such costs.⁴

3 **Q. WOULD AWEC SUPPORT A SIMILAR MECHANISM IN THIS CASE?**

4 A. Yes. AWEC would support a similar 75%/25% sharing construct for costs that exceed the
5 average price per RTC of the two lowest bids from NW Natural's RFP. Based on the RFP bid
6 information supplied in Confidential Exhibit AWEC/103, AWEC recommends the sharing
7 mechanism take effect for costs exceeding \$[REDACTED]/RTC. This amount represents the average of
8 the 20-year bid price for "[REDACTED]" and the 15-year bid price for
9 "[REDACTED]" from that exhibit.⁵

10 **Q. WHY DOES AWEC THINK A COST SHARING MECHANISM IS APPROPRIATE?**

11 A. NW Natural will be spending heavily to comply with the CPP in the future, and this will
12 include CCIs, energy efficiency, RNG and investments in other emerging technologies. When
13 NW Natural decides to pursue an investment in an RNG project rather than an offtake
14 agreement, for example, this presents a risk to customers if the project does not perform as
15 expected. NW Natural has the opportunity to earn its rate of return on a project if it performs as
16 expected. But NW Natural should also share in the risk if a project fails to perform. A cost
17 sharing mechanism balances the risks/rewards between the company and its customers.

18 **IV. ITC NORMALIZATION**

19 **Q. WHAT DID YOU RECOMMEND IN OPENING TESTIMONY WITH RESPECT TO**
20 **INVESTMENT TAX CREDITS?**

21 A. In Opening Testimony, I made two recommendations related to the ITC. First, I recommended
22 that the ITC be included in the Dakota Project revenue requirement on a non-normalized basis

⁴ UI 451 Comprehensive Stipulation at ¶ 2.

⁵ Confidential Exhibit AWEC/103

1 to provide ratepayers with 100% of both the rate base and tax expense benefits of the ITC.

2 Second, I recommended that ratepayers be held harmless for any ITC's allocated to BiocarbN
3 or Cross River Infrastructure Partners LLC working together as BioCross. Both of these
4 recommendations are necessary to ensure that customers receive the full benefit of the ITC.

5 **Q. HOW DID NW NATURAL RESPOND TO YOUR RECOMMENDATION TO**
6 **CONSIDER THE ITC ON A NON-NORMALIZED BASIS?**

7 A. NW Natural responded that under its interpretation of the normalization requirements, the
8 Dakota Project ITCs [REDACTED]⁶ Accordingly, NW Natural

9 [REDACTED]

10 [REDACTED]

11 [REDACTED]

12 **Q. DID NW NATURAL INCLUDE ITCS ON NON-NORMALIZED BASIS FOR THE**
13 **DAKOTA PROJECT REVENUE REQUIREMENT?**

14 A. No. NW Natural states that its model captures 100% of the benefits of the ITC. I disagree.

15 NW Natural's model only captures the tax expense benefits associated with amortizing the ITC
16 over the life of the investment and does not capture the rate base benefits associated with the
17 unamortized portion of the ITC.⁷ Thus, irrespective of its position on normalization, NW
18 Natural is in fact modeling the ITC using the cost of service normalization method, which as I
19 stated in Opening Testimony, ignores the rate base benefits from the ITC. In other words, NW
20 Natural is not providing customers the full benefit of the ITC.

⁶ NW Natural/400, Bourdo-Walker/10:6-9.

⁷ See NW Natural/400, Bourdo-Walker/9:1-20.

1 **Q. IS THE EXAMPLE NW NATURAL PROVIDED IN EXHIBIT NW NATURAL/401**
2 **VALID?**

3 A. No. Exhibit NW Natural/401 demonstrates that ratepayers receive just a 1.7% return based on
4 the timing differences NW Natural identified. Even if this calculation was accurate, it by no
5 means provides ratepayers with 100% of the ITC rate base benefits at NW Natural's authorized
6 rate of return of 6.836%.

7 This modest return, however, is the result of an error in NW Natural's calculation. NW
8 Natural applied a gross up factor to the amortization benefit, but failed to similarly apply a
9 gross up to the up-front tax savings. Correcting for this error results in an overall return to
10 ratepayers of -0.2%.

11 **Q. WHAT DO YOU RECOMMEND WITH RESPECT TO NORMALIZATION?**

12 A. I continue to recommend that the accounting method be used to consider both the cost of
13 service and the rate base benefits of the ITC in the Dakota Project revenue requirement. The
14 1971 ITC normalization requirements provide a windfall to utilities and are punitive to rate
15 payers because they do not consider both the expense and rate base benefits of the ITC.

16 [REDACTED], such an unfair result should be avoided.

17 Ratepayers should receive the maximum value of the ITCs to help reduce the cost of the
18 Dakota Project.

19 **V. ITC ALLOCATION**

20 **Q. HOW DID NW NATURAL RESPOND TO YOUR RECOMMENDATION TO HOLD**
21 **CUSTOMERS HARMLESS IF ANY ITCS ARE ALLOCATED TO BIOCROSS?**

22 A. NW Natural takes the position that customers should not "receive the benefit of 100% of the
23 anticipated ITC generated from the Dakota City project regardless of how much of the credit is

1 allocated to NW Natural.”⁸ NW Natural states that “the ITC credit for biogas property was not
2 yet law and was not part of the original decision.” Accordingly, it concludes that it is
3 reasonable for BioCross to receive a windfall with respect to the ITCs funded by rate payers. I
4 disagree. Customers are funding 100% of the investment and providing the funds that give rise
5 to the ITC. Therefore, I continue to recommend that ratepayers be held harmless in the event
6 any ITCs are allocated to Biocross, either directly or indirectly.

7 **Q. WILL ITCS BE ALLOCATED TO BIOCROSS?**

8 A. [REDACTED],⁹ the rules and facts are not so clear.
9 [REDACTED]. NW Natural cites an IRS
10 regulation that states “a member’s share of the investment tax credit and the qualified property
11 basis adjustment should be determined in accordance with how the partnership allocates its
12 general profits, while also considering special allocations.”¹⁰ The partnership agreement
13 allocates [REDACTED]% of profits to BioCross, therefore, [REDACTED]% of the ITC benefit will be allocated
14 (directly or indirectly) to BioCross. The basis reduction, NW Natural identified, for example,
15 may not be limiting in the amount of ITCs that are allocated to BioCross. If the basis reduction
16 is applied prior to the allocation of other losses, for example, it is likely that BioCross’ capital
17 account will be sufficient to allocate its full share of the ITC. At a minimum, the ITC will
18 reduce the partnership’s tax basis, resulting in future depreciation deductions being allocated to
19 BioCross to the detriment of ratepayers.

8 NW Natural/400, Bourdo-Walker/13:16-25

9 NW Natural/400, Bourdo-Walker/13:16-25.

10 IRS Reg § 1.46-3

1 Because the ITC was enacted after the partnership agreement was put into place, this
2 was not contemplated or addressed.

3 **Q. IS IT REASONABLE TO INCLUDE THE INVESTMENT IN RATE BASE IF RATE**
4 **PAYERS ARE NOT RECEIVING ALL OF THE BENEFITS?**

5 A. No. If ratepayers do not receive the full benefits of the investment, including the ITC and all
6 associated tax deductions, then the portion of the investment allocated to BioCross should not
7 be included in rate base. Stated differently, if █% of the ITCs are allocated to BioCross, then
8 it is reasonable to allocate █% of the capital costs to BioCross as well.

9 **Q. IS BIOCROSS' █% PROFITS INTEREST REASONABLE?**

10 A. No. Compared to the total investment, a profits interest at that level amounts to a development
11 fee of approximately \$█ million. BioCross does not need an additional windfall through the
12 ITC to align its interest with the Company when managing the Dakota Project. The contracts
13 with BioCross predate the existence of the ITC. Accordingly, BioCross determined that the
14 deal it made with NW Natural was beneficial and profitable without consideration of the ITCs,
15 and its unreasonable to provide BioCross additional and unanticipated profits from the ITCs
16 rather than providing the ITCs to ratepayers.

17 **Q. WHAT DO YOU RECOMMEND?**

18 A. For the reasons described above, I continue to recommend that the Commission impose a
19 condition which would hold ratepayers harmless in the event that ITCs are allocated (directly
20 or indirectly) to BioCross.

1 **VI. AFFILIATED INTEREST FILING**

2 **Q. DID NW NATURAL FILE AN AFFILIATED INTEREST FILING ASSOCIATED**
3 **WITH THIS DOCKET?**

4 A. Yes. In Docket UI 490 NW Natural filed a request to approve its affiliated interest agreement
5 with Dakota City Renewables, LLC. AWEC will be filing comments in UI 490 with some
6 specific recommendations along with a recommendation for the Commission to adopt many of
7 the conditions contained in the affiliated interest filing associated with the Lexington RNG
8 project.

9 **VII. RATE SPREAD**

10 **Q. HOW DID NW NATURAL RESPOND TO YOUR RECOMMENDATION ON RATE**
11 **SPREAD?**

12 A. In Opening Testimony, I recommended that NW Natural use a rate spread that allocates costs
13 in proportion to customer classes' contribution to CPP compliance obligations, consistent with
14 how the CPP actually works. In response, NW Natural made statements such as “[t]he CPP
15 does not impose an emissions cap by rate schedule.” It argued that an equal cents per therm
16 allocation is consistent with cost causation, promotes stable and consistent rates, and is simpler
17 to apply.

18 **Q. DO YOU AGREE WITH NW NATURAL’S ARGUMENT ON THE EQUAL CENTS**
19 **PER THERM ALLOCATION?**

20 A. No. NW Natural misses the mark. While I concede that an equal cents per therm allocation
21 may be *easier* for NW Natural to implement, it is not consistent with cost causation and
22 certainly does not promote stable and consistent rates. NW Natural also conveniently ignores
23 the fact that many rate schedules are priced at rates well above the costs of service and others
24 are below priced below the cost of service.

1 **Q. DO YOU AGREE THAT THIS ISSUE WOULD BE BETTER CONSIDERED IN A**
2 **RATE CASE?**

3 A. While I am concerned with the disproportionate rate impact from the Dakota Project and other
4 CPP compliance instruments on certain customers, I agree that this issue would be better
5 considered in NW Natural's next general rate case when the costs and benefits of all aspects of
6 cost of service are under consideration. As mentioned above, it is problematic that certain
7 customer classes are paying rates that are several multiples of their cost of service, while still
8 being subject to significantly higher proportions of the costs associated with the CPP.
9 Allocating cost on an equal cents per therm basis while ignoring the subsidies embedded in
10 rates ignores cost causation and principles like gradualism and rate shock. Despite these
11 concerns, AWEC proposes to withdraw its recommendation but reserves the right to raise these
12 issues for the Dakota Project and other CPP compliance costs in NW Natural's next rate case.

13 **Q. DO YOU AGREE THAT THE CPP DOES NOT IMPOSE AN EMISSIONS CAP BY**
14 **RATE SCHEDULE?**

15 A. Yes. This is precisely the reason AWEC made its recommendation. Allocating costs to rate
16 schedules on an equal cents per therm basis is not consistent with how the cap is imposed on
17 NW Natural, and therefore, results in improper price signals for the individual customer
18 classes. Relative to their overall impact on NW Natural's compliance obligations, an equal
19 cents per therm approach benefits those customer classes that are growing rapidly and fails to
20 credit those with declining loads.

21 **Q. IS YOUR RECOMMENDATION CONSISTENT WITH COST CAUSATION?**

22 A. Yes. Mirroring the application of the CPP to NW Natural, to its customer classes, will result in
23 an allocation that accurately reflects how each customer class is causing CPP compliance
24 obligations. NW Natural states "each therm of conventional natural gas consumed generates

1 the same emissions as another.”¹¹ From this premise, NW Natural concludes that each therm
2 “should bear the same CPP compliance costs.” This logic is faulty because it assumes that
3 compliance costs are established by the total therms delivered by NW Natural—ignoring how
4 the CPP was actually designed to work. As I demonstrated in Opening Testimony, however,
5 the compliance costs are driven by the difference between actual therms consumed and the
6 2017-2019 CPP baseline. Therefore, it is the change relative to the baseline that is driving the
7 costs, not the quantity of total therms delivered.

8 **Q. DOES AN EQUAL CENTS PER THERM RATE RESULT IN STABLE AND**
9 **CONSISTENT RATES?**

10 A. No. This is especially true for larger customers, who are experiencing dramatic rate increases
11 from the equal cents per therm allocation method. Further, the compliance costs, themselves,
12 are unpredictable based on weather sensitive customer loads, which is further justification for
13 such an approach.

14 **Q. IS YOUR METHOD OVERLY COMPLICATED?**

15 A. No, in fact it is quite simple. It compares actual therms used to the 2017-2019 baseline therms
16 using a straight-forward calculation.

17 **Q. DOES THIS CONCLUDE YOUR REBUTTAL AND CROSS-ANSWER TESTIMONY?**

18 A. Yes.

¹¹ NW Natural/400, Bourdo-Walker/3:5-7.

CERTIFICATE OF SERVICE

I HEREBY CERTIFY THAT I HAVE THIS 31ST DAY OF JULY 2023, SERVED THE FOREGOING **CONFIDENTIAL REBUTTAL AND CROSS EXAMINING TESTIMONY**, IN DOCKET UG 462, BY E-MAILING A COPY THEREOF, TO THE FOLLOWING:

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