

June 26, 2023

VIA ELECTRONIC FILING

Public Utility Commission of Oregon
Attn: Filing Center
201 High Street SE, Suite 100
Post Office Box 1088
Salem, Oregon 97308-1088

Re: UG 462 – Renewable Natural Gas Adjustment Mechanism—Dakota City

Northwest Natural Gas Company, dba NW Natural (“NW Natural” or the “Company”), files herewith its Reply Testimony in the above-captioned proceeding.

Please note that this filing contains confidential information subject to General Protective Order No. 23-069 and highly confidential information subject to Modified Protective Order No. 23-070.

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Respectfully submitted,

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Enclosures

BEFORE THE
PUBLIC UTILITY COMMISSION OF OREGON

UG 462

NW Natural
Reply Testimony of Anna K. Chittum

DAKOTA CITY RNG PROJECT
EXHIBIT 300

CONFIDENTIAL

June 26, 2023

EXHIBIT 300 – REPLY TESTIMONY– DAKOTA CITY RNG PROJECT

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1 **I. INTRODUCTION AND SUMMARY**

2 **Q. Are you the same Anna Chittum who filed Direct Testimony in this**
3 **proceeding on behalf of Northwest Natural Gas Company (“NW Natural” or**
4 **the “Company”)?**

5 A. Yes, I presented NW Natural/100, Chittum.

6 **Q. What is the purpose of your Reply Testimony in this proceeding?**

7 A. The purpose of my Reply Testimony is to provide an update on the Dakota City
8 RNG project and respond to the Opening Testimony filed on May 25, 2023, by the
9 Public Utility Commission of Oregon Staff (“Staff”), Oregon Citizens’ Utility Board
10 (“CUB”), and the Alliance of Western Energy Consumers (“AWEC”).

11 **Q. Do you respond to all of the issues raised by these parties?**

12 A. No. In my Reply Testimony, I discuss updates regarding the project, prudence,
13 RNG procurement, the parties’ testimony regarding the interplay of Senate Bill
14 (“SB”) 98¹ and the Climate Protection Plan (“CPP”), and the Company’s related
15 affiliated interest filing. AWEC’s proposal regarding rate spread and the
16 investment tax credit is addressed in the Reply Testimony of Lora Bourdo and Kyle
17 Walker.

18 **Q. Please summarize your testimony.**

19 A. In my Reply Testimony, I first explain that the Dakota City RNG project has
20 commenced operations, and that actual production based on the first five weeks

¹ ORS 757.390-398.

1 of operations (through the end of May 2023) has exceeded the estimates that were
2 provided with my Direct Testimony, filed on February 28, 2023.

3 Next, I respond to the parties' arguments regarding prudence in light of
4 reductions in production in comparison with available forecasts at the time of the
5 investment decision. I explain that, at the time of decision, the Dakota City RNG
6 project was the least-cost actionable project available, and that the incremental
7 cost of the project was evaluated using the Commission-approved UM 2030
8 methodology. The Company ran an RFP in 2021, but ultimately did not pursue
9 any resources identified in the RFP and selected the Dakota City RNG project
10 outside of the RFP. While Dakota City was not part of the 2021 RFP, the results
11 of the 2021 RFP informed the selection of the Dakota City project—and in fact, at
12 the time of the investment decision it was anticipated that the Dakota City RNG
13 project would have lower risk-adjusted incremental costs than the other projects
14 responding to the Company's RFP.

15 Although forecasted production has declined since NW Natural made the
16 investment decision, the updated risk-adjusted incremental cost is still lower than
17 all but one of 2021 RFP responses—demonstrating that even with the benefit of
18 hindsight, the Dakota City RNG project would still be competitive with the
19 resources identified in the Company's 2021 RFP. Thus, based on the information
20 available at the time of the investment and available now, Dakota City is a
21 reasonable and cost-competitive addition to the Company's RNG portfolio.

22 I also respond to Staff's comments regarding the Company's RNG
23 procurement process, noting the Company was not required to use a formal

1 competitive bidding process for Dakota City, but that the Company would be open
2 to considering modifications to its procurement approach in the future, and will
3 reflect such changes in its forthcoming decarbonized resource procurement policy.

4 In response to CUB's proposal that the Commission should address a legal
5 question regarding the interplay of Senate Bill 98 and the CPP, I explain that it is
6 NW Natural's position that SB 98 authorizes it to procure RNG up to the sales
7 targets in ORS 757.396 and it follows that this RNG should be used to comply with
8 the CPP. However, the interaction between SB 98 and the CPP is not squarely
9 before the Commission in this docket because the decision to pursue the Dakota
10 City RNG project predates the CPP.

11 Finally, I briefly explain that the Company filed its affiliated interest
12 agreement for Dakota City on June 5, 2023, which is docketed as UI 490.

13 **II. DAKOTA CITY RNG PROJECT UPDATE**

14 **Q. Was the Dakota City RNG project producing RNG as of the date of your Direct**
15 **Testimony—February 28, 2023?**

16 A. No. In my Direct Testimony, I stated that the Dakota City RNG project was
17 scheduled to begin start-up operations in March 2023 and fully commence service
18 the following month.²

19 **Q. When did the Dakota City RNG project begin start-up operations and**
20 **commence commercial operations?**

² NW Natural/100, Chittum/11.

1 A. The Dakota City RNG project began start-up operations by injecting RNG into the
2 MidAmerican Energy pipeline system on April 21, 2023. The project began
3 commercial operations on April 28, 2023 and is currently producing RNG.

4 **Q. Please describe the commercial operations of the Dakota City RNG project.**

5 A. The Dakota City RNG project has been producing RNG since April 2023. While
6 the project is still in its initial stages of operation, it produced over [BEGIN
7 CONFIDENTIAL] [REDACTED] [END CONFIDENTIAL] on average from the
8 initial injection date of April 21, 2023 through May 31, 2023.

9 **Q. How does the actual production through May 31, 2023 compare to the
10 production estimates in your Direct Testimony?**

11 A. Through May 31, 2023, the average actual production of [BEGIN
12 CONFIDENTIAL] [REDACTED] [END CONFIDENTIAL] exceeds the estimate in
13 my initial testimony of [BEGIN CONFIDENTIAL] [REDACTED] [END
14 CONFIDENTIAL] during the initial ramp-up period, which was expected for the first
15 two years of operations.³

16 **Q. Please explain why average actual production through May 31, 2023 has
17 exceeded the estimate in your Direct Testimony.**

18 A. As I stated in my Direct Testimony, the estimate of [BEGIN CONFIDENTIAL] [REDACTED]
19 [REDACTED] [END CONFIDENTIAL] was conservative. At that time, we decided
20 that a conservative estimate was appropriate based on the Dakota City monthly

³ NW Natural/100, Chittum/22.

1 supply data that we were receiving from Tyson.⁴ That said, my Direct Testimony
2 also stated that [BEGIN CONFIDENTIAL] [REDACTED]

[REDACTED]

[REDACTED]

[REDACTED]

[REDACTED]

[REDACTED]

[REDACTED]

[REDACTED]

[REDACTED]

[REDACTED]

[REDACTED]

[REDACTED]

[REDACTED] [END CONFIDENTIAL] In order to produce a conservative estimate of
12 production, none of the above was factored into my estimate of [BEGIN
13 CONFIDENTIAL] [REDACTED] [END CONFIDENTIAL].⁶

14 However, since the project is still in its initial start-up phase, we have not
15 revised the project's production estimates from my Direct Testimony. RNG
16 production varies over the course of the year based on a number of factors,
17 including weather, ramping of production of certain cuts of meat for various
18 holidays or in response to market demands or personnel skills, as well as the total
19 number of personnel working at the meat processing facility. While we are pleased

⁴ NW Natural/100, Chittum/22.

⁵ NW Natural/100, Chittum/22-23.

⁶ NW Natural/100, Chittum/22-23.

1 to see that initial production has exceeded my Direct Testimony forecast, we are
2 still adhering to our conservative production estimates at this time based on these
3 uncertainties.

4 **III. PRUDENCE**

5 **Q. What are the parties' positions regarding prudence of the Dakota City RNG**
6 **project?**

7 A. AWEC observes that it has some concerns regarding the Dakota City RNG project,
8 but nonetheless recommends that the Commission find that the project is prudent.⁷
9 AWEC expresses concern with the changes to production estimates, notes that
10 costs are higher than what was assumed in the Company's 2022 Integrated
11 Resource Plan, and also comments that risk-sharing may be appropriate in light of
12 the fact that the Company is pursuing an RNG project rather than an offtake
13 agreement.⁸

14 CUB comments that it reviewed the Company's diligence and analysis and
15 agrees that the Company's decision to invest in the Dakota City RNG project was
16 a reasonable action.⁹ CUB does not propose any adjustments but reserves the
17 right to respond to other parties.¹⁰

18 Staff raises a number of questions regarding the Company's analysis, and
19 asserts that the Company has not yet demonstrated that the Dakota City RNG

⁷ AWEC/100, Mullins/2-3.

⁸ AWEC/100/Mullins/3-5.

⁹ CUB/100, Gehrke/2-3.

¹⁰ CUB/100, Gehrke/2-3.

1 project was the least cost/least risk project, and as a result, Staff does not yet
2 recommend the project costs are prudent.¹¹ In particular, Staff has concerns
3 regarding decreases in the Dakota City production volumes in comparison with the
4 Company's initial evaluation and regarding the RNG procurement process and
5 evaluation of the short list in the Company's 2021 RFP.¹² Staff does not propose
6 any adjustments associated with the costs of Dakota City RNG, but is still
7 reviewing this issue.¹³

8 **Q. How do you respond to Staff and AWEC's concerns regarding the changes**
9 **in production volumes?**

10 A. NW Natural has fully reflected its latest understanding of the expected production
11 from the Tyson Dakota City facility in its filings in this docket. The production at
12 Dakota City changed [BEGIN CONFIDENTIAL] [REDACTED] [END
13 CONFIDENTIAL] from the expectations reflected in the initial decision-making
14 analysis, but the updated incremental cost of [BEGIN CONFIDENTIAL] [REDACTED]
15 [REDACTED] [END CONFIDENTIAL] still compares very favorably to other RNG options
16 available to us today. As noted in the Company's response to OPUC DR 10,¹⁴ we
17 worked to gather updated data from Tyson during construction, to understand
18 whether [BEGIN CONFIDENTIAL] [REDACTED]
19 [REDACTED] [END

¹¹ Staff/100, Drennan/3, 32-34.

¹² Staff/100, Drennan/17-30.

¹³ Staff/100, Drennan/33.

¹⁴ See Exhibit 301, OPUC DR 10, at 1.

1 **CONFIDENTIAL**]. We continued to assess the gas production and worked with
2 external digester experts to gather data on all the factors that were impacting gas
3 production. For example, in November 2022, in the middle of construction, we
4 shared with our Decarbonization Committee that the average bundled cost of RNG
5 from the project had **[BEGIN CONFIDENTIAL]** [REDACTED]
6 **[REDACTED]**. **[END CONFIDENTIAL]**¹⁵ Given the cost of resources we were
7 observing in our portfolio, we knew the incremental cost **[BEGIN CONFIDENTIAL]**
8 **[REDACTED]** **[END CONFIDENTIAL]** would still leave the Dakota City
9 resource, as I demonstrated in my Direct Testimony, less expensive than
10 resources that are available to us today that we are working to pursue.¹⁶ In sum,
11 while the production volumes for the project have departed from the Company's
12 prior estimates, it nonetheless remains a cost-competitive resource for customers.

13 **Q. Staff comments that for Dakota City, it appears that [BEGIN CONFIDENTIAL]**
14 **[REDACTED]**
15 **[REDACTED]**
16 **[END CONFIDENTIAL]**. Please explain why this is the case.

17 **A.** On a per-unit basis, the costs of the project are up because the forecast production
18 is down **[BEGIN CONFIDENTIAL]** **[REDACTED]**. **[END CONFIDENTIAL]** Since
19 there is less production, the revenue received from the sale of RNG to NW Natural
20 has gone down, including the revenue related to the sale of brown gas. However,

¹⁵ See Exhibit 301, OPUC DR 15, Attachment 5 at 32.

¹⁶ NW Natural/100, Chittum/24-25.

1 on an absolute basis, the capital costs and operating costs are very similar to what
2 we initially projected.

3 **Q. Given the increase in costs on a per-unit basis, did it make sense for the**
4 **Company to still pursue the project?**

5 A. Yes. Dakota City is still a highly attractive resource on an incremental cost basis
6 relative to other RNG opportunities, including those received in the 2021 RFP. In
7 fact, even after accounting for the decline in production, only one resource in the
8 2021 RFP that met SB 98 requirements, **[BEGIN CONFIDENTIAL]** [REDACTED]
9 **[END CONFIDENTIAL]**, had a lower incremental cost than Dakota City.

10 **Q. Why is the Company focused on levelized incremental cost when making**
11 **RNG acquisition decisions?**

12 A. OAR 860-150-0200 requires NW Natural to use the levelized total incremental cost
13 to determine whether it has exceeded the 5 percent RNG cost cap in ORS
14 757.396(5). As I explained in my Direct Testimony, Appendix H is the incremental
15 cost methodology that NW Natural uses to evaluate all RNG projects and is what
16 the Company initially included in its 2018 IRP.¹⁷ In November 2020, the
17 Commission approved NW Natural's proposed Appendix H Renewable Gas
18 Supply Resource Evaluation Methodology in Docket UM 2030, which serves as
19 the Company's approach for determining cost-effectiveness in accordance with

¹⁷ NW Natural/100, Chittum/17-21.

1 OAR 860-150-0200.¹⁸ This methodology allows NW Natural to evaluate projects
2 with different characteristics, such as whether they are bundled, unbundled, on-
3 system, or off-system on a comparable basis.¹⁹

4 **Q. At the time of the investment decision in November 2021, did you compare**
5 **the Dakota City RNG project to the 2021 RFP responses using the**
6 **incremental cost methodology?**

7 A. Yes. After the 2021 RFP, the Dakota City project was found to have a risk-adjusted
8 incremental cost of [BEGIN CONFIDENTIAL] [REDACTED] [END
9 CONFIDENTIAL]. The lowest risk-adjusted incremental cost for any eligible²⁰
10 2021 RFP resource was proposed by [BEGIN CONFIDENTIAL] [REDACTED]
11 [REDACTED] [END CONFIDENTIAL]. The second lowest was [BEGIN
12 CONFIDENTIAL] [REDACTED] [END CONFIDENTIAL]. Thus, at the time of the
13 Company's investment decision, Dakota City was viewed as far less expensive
14 than any other options in the RFP.

15 **Q. Did NW Natural decide to acquire any RNG from its 2021 RFP?**

¹⁸ *In the Matter of Pub. Util. Comm'n of Or. Investigation Into the Use of Nw. Nat.'s Renewable Nat. Gas Evaluation Methodology*, Docket UM 2030, Order No. 20-403 (Nov. 5, 2020).

¹⁹ Dakota City was evaluated with risk-adjusters that were an improvement from the original Appendix H methodology. We began risk-adjusting the incremental cost, as explained in the 2022 IRP Appendix K, after the 2018 IRP Appendix H methodology was discussed in UM 2030. The 2022 IRP is the first time we were able to bring to stakeholders the update to the methodology that included the risk adjustments we had been using since 2021.

²⁰ One resource, [BEGIN CONFIDENTIAL] [REDACTED] [END CONFIDENTIAL], was not considered eligible because it was "behind the meter" (it was not injected into a common carrier pipeline as required in OAR 860-150-0050(7)) and therefore was not considered SB 98-eligible RNG.

1 A. No. In January 2022, NW Natural decided not to pursue [BEGIN CONFIDENTIAL]
2 [REDACTED] [END CONFIDENTIAL] because, in part, the Dakota City RNG project
3 had a lower incremental cost. In addition, as explained in my Direct Testimony,
4 two other potential RNG investments had a lower incremental cost than [BEGIN
5 CONFIDENTIAL] [REDACTED] [END CONFIDENTIAL] as well.²¹ NW Natural is
6 still pursuing one of these resources, [BEGIN CONFIDENTIAL] [REDACTED]
7 [REDACTED] [REDACTED]
8 [REDACTED] [END CONFIDENTIAL] has since changed owners and is not considered
9 an immediately available resource, but still may be pursued in the future.²³

10 Q. You stated that NW Natural made the decision to not pursue [BEGIN
11 CONFIDENTIAL] [REDACTED] [END CONFIDENTIAL] in January 2022. At that
12 time, had your analysis of the Dakota City RNG project changed?

13 A. No. At the time NW Natural decided to not pursue [BEGIN CONFIDENTIAL]
14 [REDACTED] [END CONFIDENTIAL], its Dakota City incremental cost analysis was
15 unchanged. It still showed that Dakota City had a lower incremental cost than
16 [BEGIN CONFIDENTIAL] [REDACTED] [END CONFIDENTIAL].

17 The Company began to revise its incremental cost analysis in the spring of
18 2022. At that time, the Company's first Tyson RNG project, Lexington, was in
19 operation for several months and did not produce as much RNG as forecasted.

²¹ NW Natural/100, Chittum/12.

²² NW Natural/100, Chittum/12.

²³ NW Natural/100, Chittum/12.

1 This unexpected underproduction caused the Company to re-evaluate its Dakota
2 City production forecast, subsequently increasing the incremental cost of the
3 project. Even with the benefit of hindsight, the increased incremental cost of
4 **[BEGIN CONFIDENTIAL]** ██████████ **[END CONFIDENTIAL]**, however, is cost
5 competitive with 2021 RFP results and is less expensive than all but **[BEGIN**
6 **CONFIDENTIAL]** ██████████ **[END CONFIDENTIAL]**.

7 **Q. Staff asserts that changes in the cost and volume of the Dakota City Project**
8 **were [BEGIN CONFIDENTIAL] ██████████ [END CONFIDENTIAL], and may**
9 **have warranted a reassessment of the Project.²⁴ How do you respond?**

10 **A.** NW Natural takes Staff's concerns very seriously. After the November 2021
11 investment decision, the Company continued to evaluate the Dakota City RNG
12 project as costs and production data became more clearly defined during
13 construction. These updates, even though they showed an increase in incremental
14 costs, did not lead to NW Natural to alter its investment decision given the other
15 opportunities that were—and are—available. As noted above, even with the
16 increase in incremental cost, Dakota City is still less expensive than all but the
17 **[BEGIN CONFIDENTIAL]** ██████████ **[END CONFIDENTIAL]** resource from the
18 2021 RFP. The Company made the decision to not pursue **[BEGIN**
19 **CONFIDENTIAL]** ██████████ **[END CONFIDENTIAL]** prior to determining
20 production issues with Dakota City. Further, as shown in my Direct Testimony, the
21 Dakota City RNG project compares very favorably to all RNG opportunities that we

²⁴ Staff/100, Drennan/29-30.

1 currently have available to us.²⁵ Therefore, even though the incremental cost of
2 Dakota City has increased, it did not trigger a reassessment of the project because
3 it was—and continues to be—a cost-effective resource relative to other acquisition
4 opportunities.

5 As a Company, we pursue a broad portfolio of RNG resource opportunities.
6 The costs and risks and terms of these all vary, but we build a portfolio that we
7 believe is the lowest total incremental cost to our customers and provides the
8 greatest benefit. Even as Dakota City production was projected to decrease, we
9 ascertained that the increasing and eventual incremental cost of **[BEGIN**
10 **CONFIDENTIAL]** [REDACTED] **[END CONFIDENTIAL]** was never high enough to
11 be less preferable when compared to other available resources.

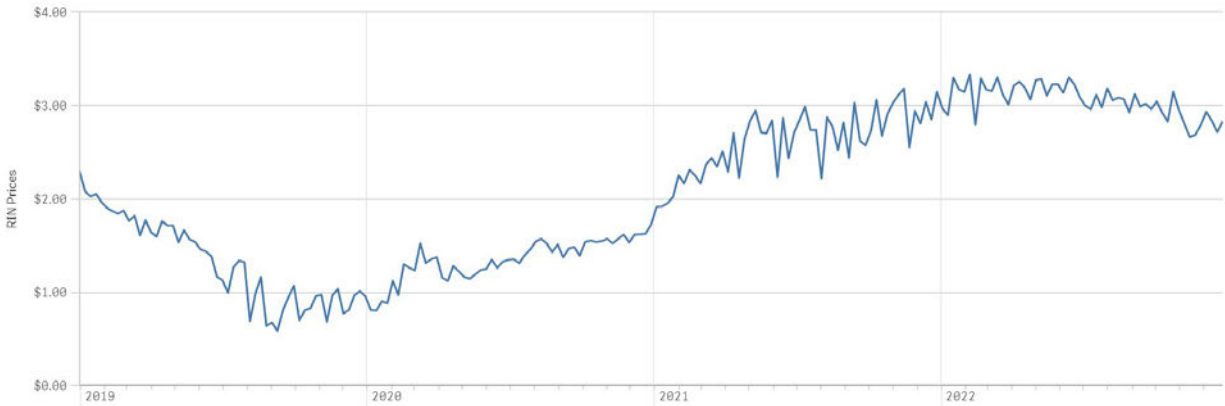
12 **Q. Did the Company consider other factors in deciding to continue to pursue**
13 **the Dakota City RNG project?**

14 A. Yes. The Company is regularly tracking RNG markets to ensure it is making
15 decisions about resources informed by broader market trends and policy changes.
16 In 2021, RIN prices were trending quite high, as can be seen in the graph below:

17 **Figure 1. RIN Prices 2019-2022²⁶**

²⁵ NW Natural/100, Chittum/25.

²⁶ United States Environmental Protection Agency, *RIN Trades and Price Information*, (last updated July 25, 2022) <https://www.epa.gov/fuels-registration-reporting-and-compliance-help/rin-trades-and-price-information>.



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The calculation for converting RINs to mmbtu of natural gas is 1 mmbtu = 11.72 RINs. Thus, throughout 2021, prices of around \$2.50/RIN were equating to over \$29/mmbtu for the environmental attributes (the equivalent of an RTC, without the brown gas component). These high prices suggested to us that developing projects ourselves, and owning the means of production of RNG, would be strategic investments that would insulate us from needing to compete with the very high RIN pricing. Similarly, California LCFS pricing had yielded credits at near and over \$200/ton for years leading up to the investment decision in Dakota City. While the credits vary considerably based on a project’s carbon intensity, the California LCFS market continues to drive high valuations for RNG resources. Therefore, our analysis demonstrates that owning our own resources helps protect customers from valuations influenced by the transportation fuel markets.

Q. How do you respond to AWEC’s comment that the Dakota City RNG project is [BEGIN CONFIDENTIAL] [REDACTED] [END CONFIDENTIAL] than the RNG costs assumed in the Company’s 2022 IRP?

1 A. The Dakota City RNG project was evaluated over a 20-year time span. Over 20
2 years, given our current conservative expectations of production, the projected
3 average cost of the resource is [BEGIN CONFIDENTIAL] [REDACTED].²⁷ [END
4 CONFIDENTIAL] The 2022 IRP used two assumptions for available RNG in its
5 modeling: Tranche 1, which represented a smaller amount of the available
6 resource, was modeled at \$14/mmbtu, +/- \$3/mmbtu bundled, while Tranche 2,
7 which represented a larger amount of available resource, was modeled at
8 \$19/mmbtu, +/- \$5 bundled.²⁸ We would expect larger projects, which can better
9 take advantage of economies of scale, to fall closer to the \$14/mmbtu band, and
10 smaller projects to fall closer to the \$19/mmbtu band. We find Dakota City, even
11 with its reduced production assumptions, to be [BEGIN CONFIDENTIAL] [REDACTED]
12 [REDACTED] [END CONFIDENTIAL] the RNG costs assumed in the 2022 IRP. The first
13 year of any RNG project would be expected to have higher \$/mmbtu costs, as the
14 project may experience variations such as start-up challenges, lower volumes,
15 additional costs, etc.

16 **Q. What is AWEC's concern regarding risk-sharing?**

17 A. AWEC expresses concern about the production levels and production risk, and
18 comments that it may be appropriate for the Commission to impose conditions
19 requiring NW Natural to share production risk to the extent that the actual

²⁷ Equivalent to [BEGIN CONFIDENTIAL] [REDACTED] [END CONFIDENTIAL].

²⁸ *In the Matter of Nw. Nat. Gas Co., dba Nw. Nat., 2022 Integrated Resource Plan*, Docket LC 79, 2022 Integrated Resource Plan at 217 (Sept. 23, 2022).

1 performance of Dakota City project significantly exceeds the cost of an alternative
2 source of RNG.²⁹ In particular, AWEC had noted that based on the Company's
3 RFP, there were several projects that were [BEGIN CONFIDENTIAL] [REDACTED]
4 [REDACTED] [END CONFIDENTIAL].

5 **Q. How do you respond to AWEC's concerns regarding risk-sharing?**

6 A. First, AWEC's forecast of [BEGIN CONFIDENTIAL] [REDACTED] [END
7 CONFIDENTIAL] is based off a 10-year levelized forecast. Using only a 10-year
8 levelized forecast to compare Dakota City to other resource options is
9 inappropriate because the Dakota City RNG project will produce RNG over 30
10 years. Second, as explained above, NW Natural continues to use incremental cost
11 methodology established in docket UM 2030 to calculate the impact a resource
12 has on the SB 98 incremental cost cap. Thus, the Company uses this methodology
13 to compare resources that have different characteristics and risks (i.e., bundled,
14 on-system, off-system, etc.). As I stated above and in my Direct Testimony, the
15 updated volume and risk-adjusted first year incremental cost of Dakota City
16 compares very favorably to all of the other RNG resources available to us today
17 that are actionable or near-actionable.³⁰ Third, while the Company agreed to risk
18 sharing for the Lexington RNG project, that was under different circumstances.
19 The Lexington RNG project risk sharing was incorporated through a settlement

²⁹ AWEC/100, Mullins/6.

³⁰ NW Natural/100, Chittum/25.

1 agreement during the affiliated interest proceeding,³¹ not during the cost recovery
2 proceeding. Also, the Lexington RNG project risk sharing was agreed to prior to
3 the start of project operations. Dakota City, by contrast, has a production forecast
4 informed by actual production data and our Lexington experience. In fact, Dakota
5 City is currently exceeding the production forecast. Due to timing, the cost of
6 service developed for the cost recovery proceeding in Lexington did not benefit
7 from the lessons learned from the initial operations of Lexington. In contrast, the
8 current Dakota City cost of service model has been informed by the Company's
9 experience with both Tyson projects.

10 **Q. Please describe Staff's concern with the average price NW Natural used to**
11 **develop the RFP short list.**

12 A. Relying on our response to OPUC DR 11,³² Staff states that NW Natural incorrectly
13 calculated the average prices used to develop the RFP short list.

14 **Q. Did the Company use the incorrect price to calculate the RFP short list?**

15 A. No. While Staff is correct that NW Natural's response to OPUC DR 11
16 inadvertently provided an incorrect average price, the Company did not use the
17 incorrect price to calculate its RFP short list at the time of proposal evaluation. NW
18 Natural's response to OPUC DR 23,³³ demonstrates an average price of **[BEGIN**

³¹ *In the Matter of Nw. Nat. Gas Co., dba Nw. Nat., Request for Approval of an Affiliated Interest Agreement with Lexington Renewables, LLC*, Docket UI 451, Order No. 22-211 (June 6, 2022).

³² Staff/103, Drennan/2.

³³ See Exhibit 301, OPUC DR 39, at 37.

1 **CONFIDENTIAL** [REDACTED] **[END CONFIDENTIAL]** and NW Natural used that price
2 to calculate the short list. We regret the error in our response to OPUC DR 11.

3 **Q. Did the response to DR 11 cause Staff to have any other concerns?**

4 A. Yes. Based on our response to DR 11, Staff is concerned that **[BEGIN**

5 **CONFIDENTIAL]** [REDACTED]

6 [REDACTED] **[END**

7 **CONFIDENTIAL]**. As explained in our response to DR 39, which was submitted

8 after Staff's Opening Testimony,³⁴ **[BEGIN CONFIDENTIAL]** [REDACTED]

9 [REDACTED]

10 [REDACTED]

11 [REDACTED]

12 [REDACTED] **[END CONFIDENTIAL]** that was

13 below the average calculated for all proposals. Although NW Natural did not

14 update the short list, which was established at a snapshot in time, it nonetheless

15 moved **[BEGIN CONFIDENTIAL]** [REDACTED] **[END CONFIDENTIAL]** to

16 the next step in the process and calculated the incremental cost. In short, NW

17 Natural treated **[BEGIN CONFIDENTIAL]** [REDACTED] **[END**

18 **CONFIDENTIAL]** like any other proposal that made the short list.

19 The risk-adjusted first year incremental cost of Dakota City at the time of

20 decision-making was **[BEGIN CONFIDENTIAL]** [REDACTED] **[END**

21 **CONFIDENTIAL]**, while the MPPA revised bid's first year risk-adjusted

³⁴ See Exhibit 301, OPUC DR 39, at 40.

1 incremental cost was [BEGIN CONFIDENTIAL] [REDACTED].[END
2 CONFIDENTIAL]

3 **Q. How do you respond to Staff’s concern that using an average price does not**
4 **consider the time value of money?**

5 A. We acknowledge that the 2021 RFP reliance on the average price to establish the
6 short list did not consider the time value of money and, in that respect, was
7 somewhat of a blunt instrument for evaluating RNG opportunities. However, it did
8 not affect the resource selection of Dakota City. We did not pursue any resources
9 out of the 2021 RFP, and, at the time of the investment decision, the Dakota City
10 RNG project had a lower first year risk-adjusted incremental cost than any 2021
11 RFP response. We have improved our evaluation processes, and for the 2023
12 RFP, the incremental cost was calculated for all proposals, which adequately
13 reflects the time value of money. Those proposals with the lowest 33 percent of
14 incremental cost were advanced to the next step in the evaluation process (i.e.,
15 short-listed).

16 **Q. Please respond to Staff’s concern that NW Natural included a [BEGIN**
17 **CONFIDENTIAL] [REDACTED] [END CONFIDENTIAL] adder for unbundled**
18 **projects.³⁵**

19 A. NW Natural does not believe that the adder in question affected the selection of
20 Dakota City. Staff states that [BEGIN CONFIDENTIAL] [REDACTED]
[REDACTED]

³⁵ Staff/100, Drennan/22-23.

█ [REDACTED] END

2 **CONFIDENTIAL**]. Therefore, Staff appears to suggest that RFP unbundled
3 resources would, all things being equal, appear to be more **[BEGIN**
4 **CONFIDENTIAL]** [REDACTED] **[END CONFIDENTIAL]** than bundled projects, like
5 Dakota City. NW Natural, however, selected Dakota City, which it found to be least
6 cost/least risk even using a **[BEGIN CONFIDENTIAL]** [REDACTED] **[END**
7 **CONFIDENTIAL]** for RFP unbundled projects, which Staff appears to claim would
8 have disadvantaged Dakota City even more.

9 **Q. Did use of the fixed price adder affect the Company's short list as**
10 **contemplated by Staff?**

11 A. Yes. Had NW Natural used the discounted average as outlined in Staff Exhibit 104,
12 three additional proposals would have been included in the short list. However, the
13 addition of these proposals to the short list would not have affected the selection
14 of Dakota City as detailed above, because Dakota City had a lower first year risk
15 adjusted incremental cost than all these proposals. Dakota City's First Year
16 Incremental Cost was **[BEGIN CONFIDENTIAL]** [REDACTED] **[END**
17 **CONFIDENTIAL]** at investment decision. The lowest First Year Incremental Cost
18 of all the SB 98-compliant RFP responses was **[BEGIN CONFIDENTIAL]**
19 [REDACTED], **[END CONFIDENTIAL]**, which made the short list, as
20 explained above.

21 **Q. Staff noted concerns with the Company's response to OPUC DR 13, which**
22 **stated "NW Natural developed a single cost-of-service model shortly before**
23 **its initial filing in this docket for ratemaking purposes," and questions**

1 **whether the Company’s approach to compiling the short list used the cost-**
2 **effectiveness calculation.³⁶ Please explain how the Company uses the term**
3 **“cost-of-service” model and respond to Staff’s concern regarding the use of**
4 **a cost-effectiveness calculation.**

5 A. NW Natural uses the term “cost-of-service model” in two different contexts, which
6 unfortunately led to confusion in this instance. In one context, it means the
7 ratemaking model that NW Natural completes shortly before making a cost
8 recovery filing. The Company assumed that Staff was referring to this model and
9 provided it in response to OPUC DR 13,³⁷ along with an explanation that it
10 completes a single model that shows how the Company proposes to recover the
11 cost of the project in rates.

12 NW Natural now understands that Staff was referring to the cost-of-service
13 model that is part of the Company’s incremental cost calculation. For Dakota City,
14 the Company completed such an evaluation as part of its investment decision,
15 which was provided to Staff in OPUC DR 14.³⁸ As more information became
16 known, the Company continued to update the model, but did not save these
17 incremental updates as they occurred. These updates culminated in Confidential
18 NW Natural/104, Chittum, which includes the updated cost-of-service at the time
19 of our initial filing in this docket—February 28, 2023.

³⁶ Staff/100, Drennan/24-25.

³⁷ Staff/102, Drennan/16.

³⁸ Staff/102, Drennan/17.

1 The 2021 RFP did not use the incremental cost methodology to evaluate all
2 RFP responses, but instead used the incremental cost methodology to evaluate
3 the responses that were selected for the short list discussed above. The Company
4 now uses the incremental cost methodology to evaluate all RFP responses.

5 **Q. AWEC states that using incremental revenue requirement is not a valid way**
6 **to evaluate the Dakota City RNG project, because there is no avoided cost**
7 **associated with the project. What is your response?**

8 A. NW Natural respectfully disagrees. NW Natural is not evaluating the Dakota City
9 RNG project in a vacuum. Instead, it is evaluating projects with a number of
10 different characteristics (bundled, unbundled, on-system, off-system, etc.) and NW
11 Natural's risk-adjusted incremental cost methodology compares all of these
12 resources on an apples-to-apples basis. Given that the Commission approved the
13 Company's incremental cost methodology in docket UM 2030, as explained above,
14 the Company still believes it is important to utilize it in making RNG acquisition
15 decisions.

16 **Q. AWEC also comments that they are unsure as to whether NW Natural's**
17 **avoided cost calculation included a [BEGIN CONFIDENTIAL] [REDACTED] [END**
18 **CONFIDENTIAL] avoided cost of gas.³⁹ How do you respond?**

19 A. The avoided cost calculation includes no avoided cost associated with brown gas,
20 since the net amount customers are paying for Dakota City does not include brown
21 gas. The overall cost of the project, however, includes revenue associated with

³⁹ AWEC/100, Mullins/4.

1 brown gas sales locally at Dakota City, and the incremental cost includes costs
2 associated with buying brown gas for delivery to NW Natural customers.

3 **Q. Staff has concerns with how NW Natural initially modeled the brown gas**
4 **sales. Please explain Staff's concern and respond.**

5 A. Staff is concerned that NW Natural will sell the brown gas at the **[BEGIN**
6 **CONFIDENTIAL]** [REDACTED] **[END CONFIDENTIAL]**, but modeled
7 such sales occurring at **[BEGIN CONFIDENTIAL]** [REDACTED] **[END**
8 **CONFIDENTIAL]**.⁴⁰ NW Natural uses **[BEGIN CONFIDENTIAL]** [REDACTED] **[END**
9 **CONFIDENTIAL]** as a proxy when it does not yet know the exact hub where brown
10 gas sales will occur, or the exact terms of the brown gas sale deal. Since **[BEGIN**
11 **CONFIDENTIAL]** [REDACTED] **[END CONFIDENTIAL]** is often trading at a discount
12 relative to other hubs, the Company considers its approach to be conservative,
13 although the selection of **[BEGIN CONFIDENTIAL]** [REDACTED] **[END**
14 **CONFIDENTIAL]** did not impact the incremental cost evaluation of the project.

15 After NW Natural made the investment decision and entered into contracts
16 to sell the gas indexed at a specific basin, the Company updated its forecasts
17 (reflected in the latest cost of service model) to reflect a more up-to-date **[BEGIN**
18 **CONFIDENTIAL]** [REDACTED] **[END CONFIDENTIAL]** price. While the current
19 contract with Symmetry to sell brown gas indicates pricing based on the **[BEGIN**
20 **CONFIDENTIAL]** [REDACTED] **[END CONFIDENTIAL]**, the contract is
21 only for one year, and any number of different hubs could be used for an index

⁴⁰ Staff/100, Drennan/25.

1 when reselling the brown gas throughout the project life. We therefore determined
2 using [BEGIN CONFIDENTIAL] [REDACTED] [END CONFIDENTIAL] as the base
3 case hub was reasonable. We note that using the [BEGIN CONFIDENTIAL]
4 [REDACTED] [END CONFIDENTIAL] would not have changed its
5 decision to pursue the Dakota City RNG project.

6 **Q. Staff also expresses concern with how NW Natural determines the level of**
7 **risk with potential RNG acquisitions, noting that the Company relies on**
8 **subject matter experts (“SMEs”) to determine the level of risk with potential**
9 **RNG acquisitions, and the Company’s methodology does not have clearly**
10 **defined rules and is not easily replicable.⁴¹ Please respond.**

11 A. The risk adjustment the Company uses reflects an improved approach to
12 evaluating the risk of various RNG projects since the UM 2030 docket, which did
13 not contemplate such risk factors. We believe subject matter experts are well
14 equipped to input these risk adjusters, because they are closest to the project and
15 understand how resources are contracted, how construction agreements are
16 structured, etc. Since our use of these adjustments for Dakota City, we now
17 routinely ask our third-party engineering experts to help us with the risk inputs as
18 part of our diligence work. Risk adjustments for development projects will always
19 make the potential investment projects have higher risk-adjusted incremental costs
20 than offtakes, all costs being the same, because development projects have more
21 variables to consider. The acquisition policy that we are developing later this year

⁴¹ Staff/100, Drennan/26.

1 for decarbonized resources will elaborate on how the risk-adjusters are to be
2 developed that will be more easily replicable.

3 **Q. Staff also comments that the Company’s risk assessment related to the**
4 **probability that Tyson would stop producing biogas at Dakota City seems**
5 **“impossibly precise.”⁴² Please explain how the Company arrived at the**
6 **value identified in its risk assessment.**

7 A. During the diligence phase of the project, we discussed the history and future of
8 the Dakota City facility with Tyson to understand potential risk around the facility
9 closing. Tyson executives repeatedly shared information with us about how the
10 Dakota City facility was the best-performing beef facility, and how they had recently
11 made additional investments in the facility. We learned that there were about
12 **[BEGIN CONFIDENTIAL]** **[END CONFIDENTIAL]** facilities that were similar to
13 the Dakota City facility (in terms of breadth of processes) and calculated **[BEGIN**
14 **CONFIDENTIAL** **[END CONFIDENTIAL]** “facility-years” total over the
15 evaluation period. That is, how many years of operation of an individual facility
16 would occur during the 20 years evaluation period **[BEGIN CONFIDENTIAL]**
17 **[END CONFIDENTIAL]** So in any given year, there would be a
18 **[BEGIN CONFIDENTIAL]** **[END CONFIDENTIAL]** chance of the Dakota
19 City facility closing in that year. This is admittedly a somewhat simplistic analysis,
20 but Tyson suggested that the net number of facilities would likely remain

⁴² Staff/100, Drennan/26.

1 unchanged during the project life, and so we tried to develop a view of the risk,
2 given that they assumed no facility closure.

3 **Q. Please respond to AWEC's comment that there were several projects in the**
4 **2021 RFP that were less expensive than the Dakota City RNG project on a**
5 **levelized basis.⁴³**

6 A. As described above and in docket UM 2030, the Company evaluates RNG
7 resources on a levelized incremental cost basis. This ensures that the lifetime
8 costs of various RNG resources are evaluated on an apples-to-apples basis as
9 much as possible. The costs cited in the AWEC testimony represent the average
10 cost of the resource, rather than the levelized incremental cost. The costs also are
11 not based on a full project lifetime. In addition, the lowest cost proposal cited by
12 AWEC was determined to not be compatible with SB 98 because it would not be
13 injected into a common carrier pipeline as required by OAR 860-150-0050(7). As
14 noted earlier, at the time of the investment decision, the Dakota City RNG project
15 had a risk-adjusted incremental cost that was well below any of the 2021 RFP
16 responses and subsequent analysis has determined that it remains a cost
17 competitive project.

18 **Q. Please summarize the Company's response regarding prudence of the**
19 **Dakota City RNG project.**

20 A. The Dakota City RNG project was the least-cost actionable project available to
21 pursue at the time when the project was ready for a decision, using the

⁴³ AWEC/100, Mullins/5-6.

1 Commission-approved UM 2030 methodology. Although forecasted production
2 has declined since NW Natural made the investment decision, the updated risk-
3 adjusted incremental cost is still lower than all but one of 2021 RFP responses—
4 demonstrating that even with the benefit of hindsight, the Dakota City RNG project
5 would still be competitive with the resources identified in the Company's 2021 RFP.
6 Thus, based on the information available at the time of the investment and
7 available now, Dakota City is a reasonable and cost-competitive addition to the
8 Company's RNG portfolio.

9 **IV. RNG PROCUREMENT PROCESS**

10 **Q. Please briefly summarize the procurement process that led the Company to**
11 **select the Dakota City RNG project in November 2021.**

12 A. As explained in my Direct Testimony, at the time of investment decision, NW
13 Natural compared the Dakota City RNG project to all other opportunities, including
14 other investment opportunities and 2021 RFP results. NW Natural compared each
15 of these opportunities using its risk-adjusted incremental cost methodology (also
16 called the Renewable Gas Supply Resource Evaluation Methodology) to evaluate
17 both RNG offtake agreements and investment opportunities. As stated above, the
18 Commission has approved the methodology to calculate the incremental cost of
19 RNG as required per OAR 860-0150-200 and NW Natural has since adopted a
20 risk-adjustment metric for evaluating resources to better reflect the risks
21 associated with potential development projects, as opposed to RNG purchases
22 from third parties. At the time of the investment decision, the Dakota City RNG
23 project was the least cost/least risk project that it could pursue at that time and that

1 could begin delivery in the very near term (i.e., within the first 5-year tranche of
2 ORS 757.396 RNG sales procurement targets).

3 **Q. Is NW Natural required to use competitive bidding for RNG procurement?**

4 A. No. As provided in OAR 860-150-0500, a competitive bidding process is required
5 for NW Natural's RNG qualified investments that are upstream of conditioning
6 equipment and that exceed \$25 million. In establishing the \$25 million threshold
7 (instead of a \$10 million threshold), the Commission noted,

8 Raising the dollar threshold for application of some of the rule's
9 safeguards to better align with similar requirements in the electricity
10 market as a primary means to provide leeway for large natural gas
11 utilities to be nimble in a nascent market is appropriate[.]⁴⁴

12 **Q. Was NW Natural required to use competitive bidding for Dakota City RNG
13 project?**

14 A. No. The assets in the Dakota City RNG project are not upstream of conditioning
15 equipment and, with total project costs of \$12.5 million, the project as a whole is
16 well below the threshold established in Commission rules.

17 **Q. For context, what is the size threshold in the competitive bidding rules for
18 electric utilities?**

19 A. The size threshold is much higher for the electric utilities, as it requires competitive
20 bidding for resources over 80 MW (including smaller projects that aggregate to
21 over 80 MW) and five years in length.⁴⁵ NW Natural understands such projects

⁴⁴ *In the Matter of Rulemaking Regarding the 2019 Senate Bill 98 Renewable Nat. Gas Programs*, Docket AR 632, Order No. 20-227 at 17 (July 16, 2020).

⁴⁵ OAR 860-089-0100(1).

1 may cost in the hundreds of millions of dollars.⁴⁶ Recent resource acquisitions by
2 electric utilities that are subject to competitive bidding—though larger than the 80
3 MW threshold—are more than ten times the cost of Dakota City. For example,
4 based on public filings, it appears that PGE expected to invest \$160 million in the
5 Wheatridge Project in 2019⁴⁷ and \$415 million in the Clearwater Wind Project in
6 2022.⁴⁸

7 **Q. Did Staff also provide testimony commenting on the use of competitive**
8 **bidding for RNG procurement?**

9 A. Yes. Staff observes that NW Natural’s procurement process differs from the
10 process used by electric utilities and suggests that elements from the electric utility
11 competitive bidding framework should be applied to NW Natural’s RNG
12 procurement.⁴⁹

13 **Q. Please summarize Staff’s comments suggesting that NW Natural’s RNG**
14 **procurement should more closely follow the process used by electric**
15 **utilities.**

⁴⁶ Order No. 20-227 at 15.

⁴⁷ Portland General Electric Company, *Portland General Electric and NextEra Energy Resources to develop nation’s first major energy facility co-locating wind, solar and battery storage* (Feb. 13, 2019) <https://portlandgeneral.com/news/2019-02-13-portland-general-electric-and-nextera-energy-resources-to-develop>.

⁴⁸ Portland General Electric Company, *Portland General Electric Earnings Conference Call Third Quarter 2022 Presentation* at 9, <https://investors.portlandgeneral.com/static-files/b781ad16-56c8-41df-b071-7267b2b3dfe5>.

⁴⁹ Staff/100, Drennan/29.

1 A. Staff appears to express some level of concern that the Dakota City RNG project
2 was not evaluated as part of the RFP.⁵⁰ Staff recommends that NW Natural move
3 towards what it considers “a more open process, with scoring rules for both price
4 and non-price factors set in place prior to receipt of bids.”⁵¹ It also recommends
5 that the Company “set rules to direct scorers on how to account for risks with the
6 RNG workbook,” and that “the Company contact an Independent Evaluator (IE)
7 who could help establish a consistent system to accurately evaluate bids,” similar
8 to electric utilities.⁵²

9 **Q. Please respond to Staff’s general concern that the Dakota City RNG project**
10 **was not evaluated as part of the RFP.**

11 A. Since the RNG market is nascent and illiquid, NW Natural constantly receives
12 proposals for potential RNG acquisitions from project developers throughout the
13 year on a rolling basis, not just when it issues an RFP. The market for RNG is also
14 competitive, meaning that the Company often cannot wait for an RFP to make an
15 acquisition decision. Larger portfolios of landfills, for instance, have in recent years
16 contracted with investment banks to run formal bidding processes to bid on
17 purchasing the landfill gas rights. The Company has proactively responded to
18 these processes outside of the RFP process. For this reason, NW Natural has
19 chosen to evaluate all potential RNG acquisitions using a common methodology

⁵⁰ Staff/100, Drennan/18-19.

⁵¹ Staff/100, Drennan/29.

⁵² Staff/100, Drennan/29-30.

1 regardless of project intake, called the Renewable Gas Supply Resource
2 Evaluation Methodology, which evaluates all such resources on an apples-to-
3 apples basis. As stated above, this approach, which was approved by the
4 Commission in 2020 and ensures that all potential RNG opportunities are
5 evaluated in the same manner, even if we are unable to review all requests within
6 the RFP process timeline.

7 **Q. You mentioned that there are circumstances where the Company cannot wait**
8 **for an RFP to make an acquisition decision. Is there an analogous exception**
9 **in the Commission’s competitive bidding rules for electric utilities?**

10 A. Yes. The Commission’s competitive bidding rules in OAR Chapter 860, Division
11 89 contemplate that there may be an exception to the competitive bidding rules for
12 a time-limited opportunity to acquire a resource of unique value to the electric
13 company’s customers, and provide that after acquiring a resource in such
14 circumstances, the electric utility must file a report with the Commission.⁵³ Given
15 the current state of the RNG market, many of the opportunities presented to NW
16 Natural are available for a limited period of time due to competition from other
17 parties. The Commission has long-recognized the importance of flexibility for such
18 time-limited opportunities--and importantly, the utility pursuing the resource must
19 still demonstrate prudence of the resource acquired outside of the RFP.

20 **Q. Are there other reasons why NW Natural does not evaluate all potential**
21 **acquisitions in its RFP process?**

⁵³ OAR 860-089-0100(3)(b), (4).

1 A. Yes. Evaluating all potential RNG acquisitions in the RFP process may make more
2 sense when there is an identified need for a certain amount of RNG to be acquired
3 at a certain time, but the Company was not facing this circumstance when it
4 decided to pursue Dakota City in late 2021. Rather, NW Natural was focused on
5 developing a portfolio of resources that can produce RNG in the near-term while
6 also pursuing RNG acquisitions with a longer lead time. In other words, since the
7 SB 98 authorizes—but does not require—the Company to meet RNG sales
8 targets, it can consider a variety of resources on different timelines. As such, NW
9 Natural does not believe it would have been advisable to issue a single RFP with
10 a pre-defined need and evaluate all responses to it in a single process. Instead, it
11 was more important to ensure all resources were evaluated using the same
12 methodology, even if some of these evaluations were performed outside the RFP.
13 Such an approach also ensures that more resources were considered, such as
14 those that were offered outside the RFP timeframe.

15 The CPP, which was adopted after NW Natural made the decision to pursue
16 the Dakota City RNG project, may ultimately change this approach, as NW Natural
17 may need to acquire a certain amount of RNG within a certain timeframe for CPP
18 compliance purposes, as well as to meet SB 98 sales targets.

19 **Q. How do you respond to Staff’s recommendation that NW Natural consider “a**
20 **more open process, with scoring rules for both price and non-price factors**
21 **set in place prior to receipt of bids?”⁵⁴**

⁵⁴ Staff/100, Drennan/29.

1 A. NW Natural is constantly seeking to improve its RNG procurement process, as
2 evidenced by the changes it has already made since its 2021 RFP. For instance,
3 it now uses its incremental cost methodology to both ascertain the RFP short list,
4 as well as evaluating those projects that made the short list using both price and
5 non-price factors. NW Natural is willing to explore Staff's recommendation and to
6 consider incorporating it into future RNG procurement processes.

7 **Q. How were non-price factors evaluated for the Dakota City RNG project?**

8 A. Non-price factors were not evaluated quantitatively, but we did factor in the fact that
9 the Tyson project partners were committed to building a portfolio of low-cost
10 projects and that we were satisfied with our partners and the diligence conducted
11 on the project. The RFP process that the Company uses includes non-price factors
12 as a tie-breaker for projects of a similar price. At the time of the investment
13 decision, Dakota City was determined to be the least cost/least risk project, so the
14 tie-breaker components and rankings were not used.

15 **Q. How did the Company evaluate risk in selecting the Dakota City RNG
16 project?**

17 A. NW Natural relies on its subject matter expertise in evaluating the risks of each
18 project and, as explained below, updated these risks as more became known (e.g.,
19 when production did not bounce back from the COVID-19 interruption as
20 anticipated). Specifically, NW Natural quantified the risks of the project to the best
21 of its ability given the information that it had at the time, especially concerning the
22 effect of COVID-19 on production, which, at the time of the investment decision,

1 the Company reasonably believed would abate by the time Dakota City
2 commenced service in 2023.

3 As noted in initial testimony, NW Natural also evaluates counterparties,
4 credit exposure, technical risk, legal risks, etc. of all agreements and partners. NW
5 Natural has an entire team diligence workstream that is managed by the
6 Renewables group that brings in many internal subject matter experts to evaluate
7 these different risks. We also contract with engineering and other technical experts
8 as well as permitting experts, etc., to evaluate risks.

9 **Q. Please respond to Staff’s recommendation that the Company “set rules to**
10 **direct scorers on how to account for risks with the RNG workbook.”⁵⁵**

11 A. The Company agrees that the goal of ensuring the risk scoring is easily replicable
12 is a laudable one, and one that we are also interested in pursuing. For Dakota City
13 we considered information provided to us by Tyson, by our engineering partners,
14 the structure of contracts, and our internal understanding of costs for things like
15 membranes and electricity. We sought input from many into the risk values we
16 used, but did not have set rules for how to select input values.

17 **Q. Please respond to Staff’s recommendation to contract with an IE who could**
18 **help establish a consistent system to accurately evaluate bids.**

19 A. NW Natural does not believe that contracting with an IE would have been
20 appropriate for the RNG acquisitions the Company has made to date. The OAR
21 Chapter 860, Division 150 RNG rules do not contemplate the use of an IE, and the

⁵⁵ Staff/100, Drennan/29.

1 Company's only RNG investments, Lexington and Dakota City, have been quite
2 small and are in no way comparable to the much larger 80 MW projects that require
3 a more formal RFP process and IE for electric utilities. Therefore, for projects of
4 this scale, the Company does not believe that contracting with an IE would be
5 worth the additional cost. In particular, in the Commission's 2018 Order No. 18-
6 324 in the AR 600 proceeding (addressing the competitive bidding rules for electric
7 utilities), the Commission observed that Staff's estimated average cost for an IE
8 was \$254,000-\$329,000 per project.⁵⁶

9 **Q. Would the Company consider working with an IE for a larger RNG**
10 **procurement?**

11 A. Yes, the Company is open to this possibility. The Company recognizes that
12 involving an IE could have benefits, and as RNG acquisitions may become larger,
13 the additional cost that would come with hiring an IE may be more appropriate.

14 **Q. Do you have any concluding thoughts on Staff's general concerns regarding**
15 **NW Natural's procurement process?**

16 A. Yes. As explained above, NW Natural is willing to consider many of Staff's
17 recommendations on a going-forward basis, and the Company believes that this is
18 consistent with Staff's intent. NW Natural, however, does not believe that these
19 recommendations should affect the prudence determination of Dakota City. Many
20 of Staff's recommendations are based on the procurement process for electric

⁵⁶ *In the Matter of Rulemaking Regarding Allowances for Diverse Ownership of Renewable Energy Resources*, Docket AR 600, Order No. 18-324 at 7 (Aug. 30, 2018).

1 utilities, which is established in Chapter 860, Division 89 administrative rules and
2 do not apply to NW Natural.

3 The Company appreciates the time, thought, and effort that went into Staff's
4 recommendations and is interested in further exploring them as it continues to
5 refine and improve its RNG procurement process going forward. As part of the
6 IRP process, NW Natural has already committed to finalizing its internal RNG
7 resource acquisition policy, and the Company will carefully consider Staff's
8 feedback as it does so.

9 **Q. Is NW Natural currently contemplating any modifications to its RNG**
10 **procurement process?**

11 A. Yes. Since the establishment of the CPP, the Company has recognized the
12 importance of casting our net wide to evaluate all options for decarbonizing the
13 gas we deliver to our customers. We have also sought to understand how these
14 different decarbonization options will provide benefits to customers who have their
15 own climate goals and reporting protocols, which may be independent of the
16 Company's CPP compliance obligations. We have begun receiving offers of a
17 variety of decarbonization options, including synthetic methane and large-scale
18 carbon capture. We intend to broaden the suite of decarbonized resources we are
19 considering beyond RNG and evaluate them all through the lens of the likelihood
20 that the promised emissions reductions will occur, and be sustained at certain
21 prices, throughout the life of the project. We also will leverage research with our
22 customers to understand which types of decarbonized resources are of value to

1 agrees that using Schedule 198 is appropriate, but Staff suggests that in the future,
2 it may not recommend a similar approach absent identification of the RNG
3 resource in a Commission-approved IRP.⁶⁰ Finally, Staff asks that the Company
4 provide more information regarding how Dakota City and future RNG projects fit
5 into the Company's CPP strategy.

6 CUB also raises a legal issue in its testimony regarding the interplay of
7 Senate Bill 98 and the CPP, and specifically asks that the Commission make a
8 legal determination that NW Natural should only be permitted to pursue SB 98's
9 voluntary targets to the extent that they fit within a least cost, least risk compliance
10 plan to comply with the CPP.⁶¹ CUB observes that NW Natural had raised related
11 legal issues in the Company's 2022 IRP, which may not be conclusively resolved
12 in that forum; CUB proposes that the Commission take on this legal issue in this
13 docket.⁶²

14 **Q. How do you respond to Staff's comments regarding non-acknowledgement**
15 **of SB 98 procurement in the 2022 IRP?**

16 A. Since Staff's Opening Testimony was filed, the Commission held a public meeting
17 to consider the Company's 2022 IRP on June 6, 2023. During that meeting, the
18 Commission stated that it will not acknowledge the Company's proposed RNG
19 procurements as part of its CPP compliance pathway, but has not yet issued a

⁶⁰ Staff/100, Drennan/15.

⁶¹ CUB/100, Gehrke/6.

⁶² CUB/100, Gehrke/6.

1 written order. When the Company receives the written order, it will carefully
2 evaluate it in determining its RNG procurement strategy going forward.

3 **Q. How do you respond to Staff’s comments regarding possibly recommending**
4 **against using Schedule 198 for future RNG projects if the RNG resource need**
5 **is not included in an acknowledged IRP?**

6 A. NW Natural views this issue differently. The IRP and prudence review proceedings
7 are related but distinct proceedings. The Commission “gives considerable weight
8 to actions that are consistent with an acknowledged IRP, and consistency with the
9 plan is evidence to support favorable rate-making treatment of the action.”⁶³ If a
10 utility seeks rate recovery of a significant investment that has not been included in
11 an IRP, the Commission will hold the utility to the same level of rigorous review
12 required by the IRP to demonstrate the prudence of the project.⁶⁴ Importantly, the
13 Commission has explained that “[a]lthough the IRP process is not a legal
14 prerequisite for a utility to seek recovery of investments in rates, we have
15 repeatedly stated that the IRP process serves as a complement to the rate-making
16 process and reduces the uncertainty of recovery.”⁶⁵ While the IRP process
17 “enhances the quality of information available to the utility and leads to better
18 resource decision-making,” strictly speaking, consideration in an IRP is not a

⁶³ *In the Matter of PacifiCorp d/b/a Pac. Power Request for a Gen. Rate Revision*, Docket No. UE 246, Order No. 12-493 at 33 (Dec. 20, 2012).

⁶⁴ Order No. 12-493 at 33.

⁶⁵ Order No. 12-493 at 33.

1 prerequisite for a prudence review—nor would it bear on the availability of a
2 prudence review.⁶⁶

3 We also note that Schedule 198 was only approved late last year and that
4 Dakota City is the first project to use that mechanism. As such, we believe it is
5 premature to make any structural changes to the mechanism at this time.

6 **Q. How do you respond to Staff’s request for additional information about how**
7 **the Dakota City project and future RNG projects fit into the Company’s CPP**
8 **strategy?**

9 A. NW Natural decided to pursue the Dakota City RNG project before the CPP rules
10 were adopted. As such, these RNG acquisitions were not made with a view
11 towards CPP compliance. As explained in my Direct Testimony, however, the
12 Company took steps to ensure that these RNG acquisitions would count towards
13 the Company’s CPP obligation.⁶⁷ Obtaining this clarification ensured that all the
14 RNG acquisitions made within this timeframe, including the Dakota City RNG
15 project, fit into both the Company’s CPP strategy and meeting SB 98 sales targets.

16 Regarding future RNG projects, NW Natural is still determining how these
17 acquisitions will fit into the Company’s CPP strategy in light of the Commission’s
18 recent decision in our IRP, as mentioned above. As of the date of this testimony,
19 the Company has not received a written IRP order and, therefore, is unable to
20 comment further at this time.

⁶⁶ Order No. 12-493 at 33, n.55.

⁶⁷ NW Natural/100, Chittum/6.

1 **Q. How do you respond to CUB’s recommendation to resolve the legal issue in**
2 **this proceeding?**

3 A. To the extent this remains a disputed issue in the case, NW Natural will address it
4 further in legal briefing. NW Natural continues to believe that SB 98 authorizes it
5 to procure RNG up to the sales targets in ORS 757.396 and it follows that this RNG
6 should be used to comply with the CPP. However, the interaction between SB 98
7 and the CPP is not squarely before the Commission in this docket because the
8 decision to pursue the Dakota City RNG project predates the CPP.

9 **VI. AFFILIATED INTEREST FILING**

10 **Q. Staff noted that as of when Staff filed Opening Testimony on May 25, 2023,**
11 **the Company had not yet made its affiliated interest filing for Dakota City.**
12 **Has the Company since made that filing?**

13 A. Yes. The Company’s request for approval of an affiliated interest transaction was
14 filed with the Commission on June 5, 2023, and docketed as UI 490.

15 **Q. Staff commented that certain protections that were included in the**
16 **settlement for the Lexington affiliated interest agreement may be appropriate**
17 **to apply to Dakota City. Does the Company agree?**

18 A. Potentially yes. In Lexington, these conditions were developed for the affiliated
19 interest agreement. If similar conditions were adopted for Dakota City, the
20 Company believes that they should also apply to the affiliate interest agreement
21 as they are focused on that transaction. Like Lexington, the Company is willing to
22 discuss the conditions that should apply to the affiliated interest agreement and it
23 is hopeful that the parties can resolve this issue in that docket (UI 490).

- 1 Q. Does this conclude your Reply Testimony?
- 2 A. Yes.

BEFORE THE
PUBLIC UTILITY COMMISSION OF OREGON

UG 462

NW Natural
Exhibits of Anna K. Chittum

DAKOTA CITY RNG PROJECT
EXHIBIT 301

HIGHLY CONFIDENTIAL

June 26, 2023

EXHIBIT 301 – Data Requests

ANNA CHITTUM

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Rates & Regulatory Affairs
UG 462

Renewable Gas Adjustment Mechanism - Dakota City
Data Request Response

Request No.: UG 462 OPUC DR 10

Please provide the analysis that led to the revised output projections for the Dakota City project as discussed in NW Natural/100 Chittum/22, lines 6-17, including all workpapers.

Response:

Throughout the construction period of Dakota City, we communicated with Tyson management and sought updates on raw gas production from facility staff. The reductions in 2020 and 2021 gas production had been noted by Tyson as related to

[BEGIN HIGHLY CONFIDENTIAL] [REDACTED]

[REDACTED]

[REDACTED] [END HIGHLY CONFIDENTIAL]

UG 462 OPUC DR 10
Attachment 1
Filed Separately in Native Electronic Format

Highly Confidential
Subject to Modified Protective Order 23-70

**UG 462 OPUC DR 10
Attachment 2**

**Highly Confidential
Subject to Modified Protective Order 23-70**



Rates & Regulatory Affairs

UG 462

Renewable Gas Adjustment Mechanism - Dakota City

Data Request Response

Request No.: UG 462 OPUC DR 15

Please provide board presentations where the Dakota City project was discussed, as well as supporting materials.

Response:

Please see Confidential UG 462 OPUC DR 15 Attachments 1-6. NW Natural has only included Dakota City materials from these board presentations and is not providing any materials that are covered by attorney/client privilege and attorney work product doctrine.

**UG 462 OPUC DR 15
Attachment 1**

**Confidential
Subject to General Protective Order**



Rates & Regulatory Affairs

UG 462

Renewable Gas Adjustment Mechanism - Dakota City

Data Request Response

Request No.: UG 462 OPUC DR 23

In response to OPUC DR 11 NW Natural states, "The proposals at or below the average pricing moved on to the next step in the process. At that point, we considered a "short list" of 17 proposals as detailed in Confidential UG 462 OPUC DR 11 Attachment 1.

- a. Please provide the underlying file for Confidential UG 462 OPUC DR 11 Attachment 1, in native format, complete with formulae intact for the confidential attachment.
- b. Please provide an explanation for any projects above the average price that were included on the short list.
- c. Please provide an explanation for any projects lower than the average price that were excluded from the short list.
- d. Did the Company develop cost-of-service models for all of the short list projects? Please explain why not if the response is no.

[Start Confidential] e. Please explain the adder for unbundled projects. [End Confidential]

Response:

- a. See Confidential UG 462 OPUC DR 23 Attachment 1. Please note that Confidential UG 462 OPUC DR 11 Attachment 1 includes all proposals and has incorrect data in the Below or Above Average column. Confidential UG 462 DR 23 Attachment 1 reflects the correct values.
- b. A total of six projects were included on the short list that had an average bundled price that was higher than the average. See Confidential UG 462 DR 23 Attachment 2.
- c. Not applicable.
- d. NW Natural prepared incremental cost models for all of the short-listed RFP proposals. These were de facto incremental cost models, because they integrated the total costs customers would be paying for the RNG resource using the inputs provided by RFP respondents. The incremental cost model is a cost-of-service model for offtake projects or, in the case of the development projects, the respondents provided offtake prices on a per-mmbtu basis and that was used in lieu of any detailed cost-of-service model, because we had no complete information on the capital and operating costs of the projects.

e. **[START CONFIDENTIAL]** [REDACTED]
[REDACTED]
[REDACTED]
[REDACTED]
[REDACTED] . **[END CONFIDENTIAL]**

UG 462 OPUC DR 23
Attachment 1
Filed Separately in Native Electronic Format

Confidential
Subject to General Protective Order

**UG 462 OPUC DR 23
Attachment 2**

**Confidential
Subject to General Protective Order**

 **NW Natural®**
Rates & Regulatory Affairs
UG 462

Renewable Gas Adjustment Mechanism - Dakota City
Data Request Response

Request No.: UG 462 OPUC DR 39

Please explain why the Company excluded the following project from the short list when it was below the average costs as presented in DR 34? See also the Company's response to DR 23c which asked the Company to "Please provide an explanation for any projects lower than the average price that were excluded from the short list." **[BEGIN CONFIDENTIAL]**

[REDACTED]

[End Confidential]

Response:

Upon initial evaluation, the proposal from **[BEGIN CONFIDENTIAL]** [REDACTED] **[END CONFIDENTIAL]** that was more than the average calculated for all proposals. **[BEGIN CONFIDENTIAL]** [REDACTED] [REDACTED] **[END CONFIDENTIAL]** Confidential UG 462 OPUC DR 34 Attachment 1 reflects the **[BEGIN CONFIDENTIAL]** [REDACTED] **[END CONFIDENTIAL]**. We did not, however, update the Short List to 'Yes' because the Short List reflects a specific point in time – the time after the initial evaluation of all offers. We did eventually calculate the incremental cost for this resource and determined that it was too expensive compared to other options and the **[BEGIN CONFIDENTIAL]** [REDACTED] **[END CONFIDENTIAL]** was also rejected.

In regards to DR 23C, although this proposal was not flagged as 'Short List' in the initial evaluation due to its failure to qualify on the initial proposal, we did perform the secondary step of calculating the incremental cost **[BEGIN CONFIDENTIAL]** [REDACTED] **[END CONFIDENTIAL]** was not considered to be excluded from the short list.

BEFORE THE
PUBLIC UTILITY COMMISSION OF OREGON

UG 462

NW Natural

**Reply Testimony of Lora M. Bourdo and
Kyle T. Walker**

**DAKOTA CITY REVENUE REQUIREMENTS
EXHIBIT 400**

CONFIDENTIAL

June 26, 2023

EXHIBIT 400 – REPLY TESTIMONY– DAKOTA CITY REVENUE REQUIREMENTS

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1 I. INTRODUCTION AND SUMMARY

2 Q. Are you the same Lora Bourdo and Kyle Walker who filed Direct Testimony in this
3 proceeding on behalf of Northwest Natural Gas Company (“NW Natural” or the
4 “Company”)?

5 A. Yes, we presented NW Natural/200, Bourdo-Walker.

6 Q. What is the purpose of your Reply Testimony in this proceeding?

7 A. The purpose of our Reply Testimony is to respond to testimony filed on May 25, 2023 by
8 the Alliance of Western Energy Consumers (“AWEC”) related to the Dakota City RNG
9 project, which the Company seeks recovery of in this proceeding. Specifically, we will
10 respond to issues presented in the testimony of AWEC witness Bradley Mullins
11 (AWEC/100) concerning rate spread and the structure of investment tax credits. The
12 Reply Testimony of Anna Chittum (NW Natural/300) addresses the other issues raised by
13 AWEC, as well as the issues raised in testimony filed by the Public Utility Commission of
14 Oregon Staff and the Oregon Citizens’ Utility Board.

15 II. RATE SPREAD

16 Q. Please summarize the rate spread you proposed in your Direct Testimony.

17 A. We proposed to allocate Dakota City RNG project’s revenue requirement to all non-
18 storage customers on an equal cent per therm basis. NW Natural proposed this allocation
19 methodology because all non-storage customers benefit from the project. Specifically, the
20 project helps meet ORS 757.396 RNG sales targets and lowers the Company’s covered
21 emissions under the Climate Protection Program (“CPP”). The Commission has
22 previously adopted the same methodology for the Lexington RNG project in Order No. 23-
23 046. See Direct Testimony of Lora Bourdo and Kyle Walker, NW Natural/200 at 8-9.

24 Q. Did AWEC propose a different rate spread?

1 A. Yes. AWEC proposed to allocate costs to rate schedules based on what it considers to
2 be the actual CPP compliance obligations generated by each rate schedule.¹ In other
3 words, AWEC's rate spread is calculated based on the difference between actual
4 throughput and a value that AWEC calculated as a CPP cap by rate schedule. AWEC
5 argues that its proposal is consistent with how the CPP compliance obligations are
6 calculated.²

7 **Q. How are NW Natural's CPP compliance obligations calculated?**

8 A. The CPP does not impose an emissions cap by rate schedule. Instead the CPP requires
9 NW Natural to obtain a CPP compliance instrument or a community climate investment
10 credit for each metric ton of CO₂e of its total compliance obligation.³ Per OAR 340-271-
11 9000, NW Natural receives CPP compliance instruments as a lump sum, not on a per rate
12 schedule basis. Community Climate Investments are also not distributed on a per rate
13 schedule basis and instead may be purchased by entities covered under the CPP.⁴ In
14 short, each therm of conventional natural gas consumed has the same CPP cost
15 regardless of rate schedule.

16 **Q. Does NW Natural agree with AWEC's rate spread proposal?**

17 A. No. NW Natural continues to believe that the Dakota City project benefits all non-storage
18 customers and should be allocated on an equal cent per therm basis across all rate
19 schedules because it is: 1) consistent with the cost causation, 2) promotes stable and
20 consistent rates, and 3) is simpler to apply.

¹ AWEC/100, Mullins/12.

² AWEC/100, Mullins/12.

³ OAR 340-271-0450.

⁴ OAR 340-271-0020(7); OAR 340-271-0820.

1 **Q. What is cost causation?**

2 A. Cost causation is the general ratemaking principle that the customer that causes the costs
3 to be incurred should pay for them.

4 **Q. Is AWEC's proposal consistent with the cost causation principle of ratemaking?**

5 A. No, we don't believe that it is. However, as stated above, each therm of conventional
6 natural gas consumed generates the same emissions as another and, therefore, should
7 bear the same CPP compliance costs. These CPP compliance costs include the
8 acquisition of RNG to lower emissions covered under the CPP. Under AWEC's proposal,
9 the CPP costs of each therm would vary depending on the rate schedule. For example, if
10 a customer was consuming conventional natural gas under a rate schedule that was
11 already below AWEC's proposed emissions cap for that schedule, then it would not incur
12 any CPP costs. A customer, however, consuming natural gas under a rate schedule that
13 was above the proposed cap for that schedule would incur higher CPP costs. We continue
14 to believe that such an approach is inconsistent with cost causation. Under both
15 circumstances, the customer consumes conventional natural gas, which causes NW
16 Natural to incur CPP compliance costs and, therefore, both should pay CPP costs based
17 on terms of conventional natural gas consumed.

18 **Q. Do you continue to believe that your proposal is consistent with cost causation?**

19 A. Yes. We continue to believe that the approach proposed in our Direct Testimony, which
20 allocates costs on an equal cent per therm basis, is consistent with cost causation. As
21 stated above, neither NW Natural's CPP compliance obligation nor the compliance
22 instruments it receives are based on rate schedules.

23 **Q. AWEC also comments that CPP compliance is determined not only by total**
24 **throughput, but also by declining caps, and asserts that its proposal is a better**

1 **method to reflect cost-causation and ensure that CPP-related costs are assigned to**
2 **the rate schedules driving the costs.⁵ Please respond.**

3 A. Because each therm of conventional natural gas has the same amount of emissions that
4 count against a cap that is determined in aggregate (not by rate schedule), we continue
5 to believe that our proposal better reflects cost causation than AWEC's. We do not believe
6 that these costs should differ by rate schedule because, as stated above, each therm of
7 conventional natural gas has the same costs under the CPP. For that reason, our proposal
8 more appropriately reflects the cost-causer, cost-payer principle.

9 **Q. In addition to cost causation, you stated that your proposal promotes stable and**
10 **consistent rates. Why are stable and consistent rates important?**

11 A. Stable and consistent rates help customers better predict and manage their energy costs.
12 While rate increases may be necessary for a number of reasons, they should be spread
13 to customers in a manner that—to the extent practicable—seeks to minimize sharp and
14 sudden rate increases while also considering cost causation (as discussed above) and
15 any other relevant factors.

16 **Q. Relative to your proposal in Direct Testimony, does AWEC's proposal promote**
17 **stable and consistent rates?**

18 A. No. AWEC's proposed rate spread would lead to rates that are not as stable or as
19 consistent as what we originally proposed in Direct Testimony. Our proposal reflects
20 normalized throughput, which is what NW Natural traditionally uses to set rates because
21 it results in rates set on an average basis (in the middle over a range of outcomes),
22 reducing year-to-year variations.

⁵ AWEC/100, Mullins/13.

1 Unlike our proposal, AWEC uses actual throughput. Using actual throughput to
2 calculate rates would increase volatility to customer bills as external factors are
3 unpredictable and can skew throughput volumes higher and lower. This would likely
4 create larger revenue shortfalls or surpluses as compared to using normalized volumes.
5 While these differences are accounted for in the Schedule 198 deferral, using actual
6 throughput as billing determinants will likely generate a large deferral and could
7 exacerbate rate impacts to customers, as compared to using normalized volumes for
8 billing determinants. As such, AWEC's proposal does not promote stable and consistent
9 rates to the same degree as our proposal in Direct Testimony.

10 **Q. AWEC argues that your proposed billing determinants are out-of-date.⁶ How do you**
11 **respond?**

12 A. NW Natural used the normalized throughput for the Test Year (November 1, 2022 to
13 October 31, 2023) in its last general rate case (UG 435) as the billing determinants to
14 calculate our proposed rates for the Dakota City RNG project. Using these billing
15 determinants is reasonable because we are currently in the Test Year. AWEC states that
16 our actual throughput has increased materially since filing UG 435, but this only reflects
17 the Company choice to use normalized throughput and not actual throughput that is
18 skewed by weather. To date, the Test Year has been colder than normal. After accounting
19 for weather, throughput is actually lower than forecasted because customer additions are
20 lower than what we estimated in the Test Year for UG 435. It's important to note, however,
21 that the cost of service, and billing determinants, will be updated annually per Schedule
22 198.

⁶ AWEC/100, Mullins/13.

1 **Q. You stated that your rate spread proposal is simpler than AWEC's. Why is**
2 **simplicity important?**

3 A. Simplicity is important because it reduces the administrative burden associated with
4 setting rates and it is easier for customers to understand how rates are calculated.

5 **Q. Please explain why your proposal is simpler than AWEC's.**

6 A. To mitigate for using actual throughput, AWEC proposes using a true-up mechanism that
7 would be based on the difference in the previous year's actual usage and the current
8 year's usage by schedule.⁷ It would then be amortized based on the current year usage,
9 which could be dramatically different from the previous year's actual usage. It is also
10 possible that a rate schedule that generates the deferral would not pay for it in the true-
11 up, and it would be amortized to a different schedule. This type of true-up, based on
12 differences in actual usage, is complex and not necessary under our proposal, which is
13 based on normalized usage, where the true-up is spread to all customers based on normal
14 usage on an equal cent per therm basis.

15 **Q. AWEC argues that large volume sales and transportation customers are already**
16 **paying more than their relative cost of service and that in future general rate cases**
17 **CPP costs should be considered in conjunction with the overall rate spread.⁸ Do**
18 **you agree?**

19 A. While AWEC's recommendation is outside the scope of this proceeding, the Company
20 acknowledges that large volume sales and transportation customers are paying more than
21 their relative cost of service and that this issue must be considered in future general rate
22 cases in conjunction with other relevant ratemaking principles. To date, however, NW

⁷ AWEC/100, Mullins/13.

⁸ AWEC/100, Mullins/13-14.

1 Natural has not considered pass-through costs, such as CPP costs, in establishing the
2 cost of service for each customer group.

3 **III. INVESTMENT TAX CREDITS**

4 **Q. Please summarize the concerns that AWEC has articulated regarding the**
5 **anticipated investment tax credit from the Dakota City investment.**

6 A. AWEC expressed a number of concerns regarding the anticipated investment tax credit
7 (“ITC”) and how it is included in ratemaking. These concerns can be summarized into
8 two broad themes:

- 9 a) Normalization - The benefit of the ITC should not be normalized in rates because
10 customers will not receive the full benefit of the ITC or any time value of money, and
11 b) Allocation - Customers should receive the benefit of 100 percent of the ITC
12 generated from the Dakota City project regardless of how much, if any, ITC is
13 allocated to the third-party developer under the terms of the limited liability company
14 operating agreement or operation of tax law.⁹

15 **Q. Can you expand on the concerns that AWEC has articulated regarding**
16 **normalizing the ITC benefit in rates for customers?**

- 17 A. Yes, AWEC included the following notes regarding normalization in their testimony:
18 a) Using normalization in ratemaking for the ITC is unfair because customers will not
19 receive “the full benefit” of the ITC (AWEC/100, Mullins at 7). NW Natural receives
20 the ITC benefit upfront, but customers “will not receive any time value of money”
21 (AWEC/100, Mullins at 8).

⁹ AWEC/100, Mullins/7-10.

1 b) It's "unclear whether the Dakota Project will be subject to normalization
2 requirements" (AWEC/100 Mullins at 8).

- 3 ○ NW Natural should structure the transaction to avoid normalization
4 requirements. One approach could be selling the credit, but that would result
5 in a discounted sale value (e.g., 90-92 percent of face value). "There is no
6 clear requirement that proceeds from a sale of ITCs be normalized."
- 7 ○ If necessary, NW Natural should "seek a private letter ruling" from the IRS
8 requesting guidance.

9 **Q. Can you explain the role of normalization in the regulatory ratemaking process,
10 especially in relation to income tax items and investment tax credits?**

11 A. Normalization plays a crucial role throughout the ratemaking process. The approach
12 ensures that utility rates are established based on consistent, recurrent costs and
13 revenues, fostering equity and stability in utility pricing. Normalization is applied to a
14 variety of income tax and non-income tax elements, even in cases where such treatment
15 is not mandated by law or rule, in order to uphold these principles of fairness and
16 economic stability.

17 When it comes to normalizing investment tax credits, the benefits and detriments
18 of such incentives are distributed to customers over the functional lifespan of the
19 corresponding property. This process ensures that the advantages are received by the
20 customers benefiting from the investment throughout its operational years.

21 Consequently, it is not just the customers who happen to be present when the
22 investment is initially made that benefit, but rather a broader range of customers over
23 time.

1 **Q. Please expand on what the detriments of the ITC are that you noted in the**
2 **response above.**

3 A. The ITC is a dollar-for-dollar tax credit against the federal income tax liability of the
4 taxpayer who receives the credit. The credit is calculated as a percentage of the
5 qualifying capital investment. A \$10 million dollar capital investment that qualifies for a
6 credit of 25 percent would generate an ITC of \$2.5 million. When an ITC is generated,
7 the detriment is that a portion of the income tax basis in the underlying capital
8 investment, equal to 50 percent of the credit amount, is foregone. Continuing this
9 example, if an ITC of \$2.5 million is generated, income tax basis equal to \$1.25 million is
10 foregone (\$2.5 million X 50 percent). If the federal income tax rate is 21 percent, this
11 foregone tax basis will result in lost income tax depreciation worth \$262,500 (\$1.25
12 million X 21 percent).

13 **Q. Will customers receive the full benefit of the ITC in rates if the ITC is normalized?**

14 A. Yes. Continuing with the example in the answer immediately above, if NW Natural
15 received an ITC of \$2.5 million, and included the benefit of that ITC and the detriment of
16 the foregone tax depreciation in rates over the 30-year useful life of the underlying
17 property, NW Natural would receive a net cash benefit of \$2,237,500. Customers would
18 receive a rate reduction of \$2,832,279 over 30 years. The time value of money return
19 received by customers over the 30-year period is 1.7 percent. See Exhibit 401 for details
20 of this example.

21 **Q. Is the anticipated ITC from the Dakota City investment subject to normalization by**
22 **law?**

23 A. **[BEGIN CONFIDENTIAL]** [REDACTED]
[REDACTED] **[END**

25 **CONFIDENTIAL]** Normalization is required for “public utility property.” Internal Revenue

1 Code section 168(i)(10) defines public utility property as “property used predominantly in
2 the trade or business of the furnishing or sale of [gas through a local distribution system]
3 if the rates for such furnishing or sale, as the case may be, have been established or
4 approved by a state or political subdivision thereof.” Treasury Regulation 1.46-
5 3(g)(ii)(2)(iii), clarifies that “rates are ‘regulated’ if they are established or approved on a
6 rate-of-return basis.” [BEGIN CONFIDENTIAL] [REDACTED]

[REDACTED]

[REDACTED]

[REDACTED] [END CONFIDENTIAL]

10 **Q. Does NW Natural think it is necessary to seek a private letter ruling from the IRS**
11 **as AWEC suggested?**

12 **A.** No. Seeking a private letter ruling in this case is unnecessary and unwarranted. First, it
13 is an expensive and lengthy exercise. It would likely cost upwards of \$120 thousand,
14 including filing fees, legal fees, and intervening party time, to prepare and file the ruling
15 request. If the ruling request was accepted by the IRS, it would likely take at least 90
16 days to receive a response after filing, assuming there are no follow up information
17 requests from the IRS which may further delay the process. In addition, [BEGIN

18 **CONFIDENTIAL]** [REDACTED]

[REDACTED]

[REDACTED]

[END CONFIDENTIAL]

22 **Q. If there is agreement among the parties that it is unlikely that [BEGIN**
23 **CONFIDENTIAL]** [REDACTED] **[END CONFIDENTIAL] is required, is there a**
24 **way to reduce or eliminate the risk of a [BEGIN CONFIDENTIAL]** [REDACTED]
[REDACTED] **END CONFIDENTIAL]?**

█ A. Yes. [BEGIN CONFIDENTIAL] █
█
█
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█
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█

10 [END CONFIDENTIAL]

11 Q. Did AWEC recommend another approach to incorporating the net benefit of the
12 anticipated ITC if it was not normalized?

13 A. No. While AWEC clearly indicated their position that normalizing the net ITC benefit
14 should be avoided, it did not suggest any alternative mechanisms for incorporating the
15 net benefit in customer rates.

16 Q. Does NW Natural have any recommendations on incorporating the net ITC benefit
17 [BEGIN CONFIDENTIAL] █ [END CONFIDENTIAL]

18 A. Yes. [BEGIN CONFIDENTIAL] █
█
█
█
█
█
24 █
█

[REDACTED]

[REDACTED]

[REDACTED]

[REDACTED] [END CONFIDENTIAL]

5 Q. Can you expand on the concerns that AWEC has articulated regarding the
6 allocation of the ITC between NW Natural and the third-party developer?

7 A. Yes, AWEC included the following notes regarding the ITC allocation in their testimony:

8 • “NW Natural modeled 100% of the Dakota Project’s ITCs as being allocated to
9 ratepayers” (AWEC/100 Mullins at 9). [BEGIN CONFIDENTIAL] [REDACTED]

[REDACTED]

[REDACTED]

[REDACTED] (AWEC/100 Mullins at 9) [END

13 CONFIDENTIAL]

14 • NW Natural should structure the Dakota City investment so that 100 percent of the credit
15 is allocated to NW Natural (AWEC/100 Mullins at 9). “Further, I recommend that
16 ratepayers be protected and held harmless if any ITCs are allocated to the BioCross
17 partners” (AWEC/100 Mullins at 10).

18 Q. Does NW Natural anticipate that 100 percent of the anticipated ITC credit will be
19 allocated to NW Natural and be available to incorporate into customer rates?

20 A. [BEGIN CONFIDENTIAL] [REDACTED] [END CONFIDENTIAL] The Dakota City Renewable
21 Energy LLC operating agreement uses a target capital account approach to allocate
22 profits and losses among its members. This approach ensures that after the allocation,
23 each member’s capital account is as close as possible to the amount they would receive

1 if the LLC were to liquidate. In addition, no member is allowed to have a negative capital
2 account.

3 According to Treasury Regulation section 1.46-3, a member's share of the investment
4 tax credit and the qualified property basis adjustment should be determined in
5 accordance with how the partnership allocates its general profits, while also considering
6 special allocations.

7 [BEGIN CONFIDENTIAL]

[REDACTED]

[REDACTED]

[REDACTED]

[REDACTED]

[REDACTED]

[REDACTED]

[REDACTED]

[REDACTED]

[REDACTED]

[REDACTED] [END CONFIDENTIAL]

16 **Q. Should customers receive the benefit of 100 percent of the anticipated ITC**
17 **generated from the Dakota City project regardless of how much of the credit is**
18 **allocated to NW Natural?**

19 **A.** No. When the Dakota City project was entered into, the ITC credit for biogas property
20 was not yet law and was not part of the original decision. It is a fortuitous outcome that
21 the federal Inflation Reduction Act, which became law in August of 2022, recognized the
22 importance of promoting biogas and incorporated an appropriate tax incentive to
23 encourage this type of investment in energy infrastructure. NW Natural has incorporated
24 the expected economic benefits of the anticipated incentive into customer rates in order
25 to reflect the economics of ratemaking.

[BEGIN CONFIDENTIAL]

[REDACTED]

[END CONFIDENTIAL] If this did occur, customer

9 rates would be directly benefited by the lower costs and increased volumes. As a result,
10 customers would receive a double benefit from the operational outcome as well as ITCs
11 that are not economically allocated.

12 **Q. Can NW Natural restructure the Dakota City investment, as AWEC suggests, to**
13 **ensure that NW Natural receives 100 percent of the anticipated ITC?**

14 A. As noted in the answer above, [BEGIN CONFIDENTIAL]

[REDACTED]

[END CONFIDENTIAL]

21
22 **Q. Does this conclude your Reply Testimony?**

23 A. Yes.

BEFORE THE
PUBLIC UTILITY COMMISSION OF OREGON

UG 462

NW Natural

Exhibit of of Lora M. Bourdo and Kyle T. Walker

DAKOTA CITY RNG PROJECT EXHIBIT 401

June 26, 2023

UG 462
Exhibit 401
ITC Normalization Example

Filed Separately in Native Electronic Format