

**BEFORE THE PUBLIC UTILITY COMMISSION
OF OREGON**

UM 1722

In the Matter of

PUBLIC UTILITY COMMISSION OF
OREGON,Investigation into Recovery of Safety
Costs by Natural Gas Utilities.

ORDER

DISPOSITION: STIPULATION ADOPTED

I. SUMMARY

In this order we adopt a stipulation addressing cost recovery of local distribution companies' (LDCs) safety investments that includes the parties' guidelines to govern proposals for safety cost recovery mechanisms used between general rate cases, as well as the parties' requirement that the LDCs file annual safety project plans for Staff and stakeholder review.

II. BACKGROUND

We opened this docket in response to a request by Northwest Natural Gas Company, dba NW Natural, to extend its Safety Integrity Program (SIP) Recovery Mechanism.¹ The SIP Recovery Mechanism allowed NW Natural to recover costs related to replacement of bare steel distribution and transmission facilities, as well as other safety investment costs. Commission Staff, Citizens' Utility Board of Oregon (CUB), and Northwest Industrial Gas Users (NWIGU) did not support extending the SIP Recovery Mechanism because

¹ The SIP Recovery Mechanism was Schedule 177 of NW Natural's tariff. It began as the bare steel program and was expanded to include transmission and distribution integrity programs. *In the Matter of NW Natural Application for an Accounting Order*, Docket No. UM 1406, Order No. 09-067 (Mar 1, 2009). The SIP was extended twice—in 2012 as part of a stipulation for NW Natural's rate case. *In the Matter of NW Natural Request for a General Rate Revision*, Docket No. UG 221, Order No. 12-408 (Oct 26, 2012), and again in 2013, *In the Matter of NW Natural System Integrity Program*, Docket No. UM 1406, Order No. 13-179 (May 16, 2013).

they believed the SIP was primarily intended to facilitate bare steel replacement, which has concluded.

We declined to extend the SIP Recovery Mechanism, and, instead opened this investigation to generically examine the recovery of safety costs by natural gas utilities.² NW Natural subsequently withdrew its request to extend the SIP Recovery Mechanism to allow the Commission and the parties to focus on the generic investigation.

NW Natural; Cascade Natural Gas Corporation; Avista Corporation, dba Avista Utilities; Commission Staff; CUB; and NWIGU (collectively, the parties) participated in this proceeding. The LDCs filed three rounds of testimony, Staff and CUB filed two rounds of testimony, and NWIGU filed opening testimony.

Given the general agreement of the parties expressed in testimony, we directed the parties to engage in further discussions to determine whether they could reach agreement on a comprehensive proposal that included: (1) guidelines for the establishment of safety investment recovery mechanisms; (2) detailed requirements of an annual safety plan to be filed by each LDC; and (3) a process for review of the annual safety plans.³

After discussions the parties entered into a stipulation and presented it, along with supporting testimony, in October 2016. The stipulation is attached as Appendix A.

III. DISCUSSION

A. Initial Testimony

To provide the proper context for our review of the parties' stipulation, we begin with a review of issues initially raised by the parties in testimony. The testimony focused on two issues: (1) guidelines for safety investment recovery mechanisms, and (2) a new requirement that the LDCs file regular safety plans with the Commission.

1. Guidelines

The LDCs initially proposed three guidelines they contend are consistent with policies used by the Federal Energy Regulatory Commission (FERC) for the recovery of safety investments made for interstate natural gas pipelines.⁴ These guidelines required that: (1) investments should follow a plan that implements safety laws or policies;

² Order No. 15-093 (Mar 25, 2015) (adopting Staff's recommendation).

³ ALJ Ruling (Apr 15, 2016).

⁴ *Cost Recovery Mechanisms for Modernization of Natural Gas Facilities*, 151 FERC ¶ 61,047 (2015).

(2) investments should either be significant capital costs that are not offset by revenues, or O&M expense that is not included in current rates; and (3) the Commission should consider recovery mechanisms on a case-by-case basis, and subject any mechanism to a prudence review and earnings test.

Staff, CUB, and NWIGU agreed that any safety investment recovery mechanism should include an earnings test and periodic review, but did not support the LDCs' other proposed criteria. They disagreed with the LDCs' assertion that the guidelines were consistent with FERC policy. Staff explained that FERC's policy statement contemplates one-time capital investments with costs that are specifically identified at the time the mechanism is proposed and estimated with an upper limit. Staff asserted that, by contrast, the LDCs proposed to recover a broader set of costs, such as ordinary capital costs incurred in regular distribution system maintenance, or a bundled set of small project costs.

CUB and Staff offered an alternative list of criteria. CUB believed that a mechanism should be limited to discrete, clearly identifiable capital investment programs (no O&M) that take place over several years. CUB also believed a mechanism should be proposed as part of a general rate case filing, so that parties may fully evaluate the proposal while also examining base rates. Staff proposed similar elements, with the addition of a cost recovery cap, a proposal for periodic review of the mechanism, and a depreciation review test. The depreciation review test would allow cost recovery only if the company's total annual capital investment in all outside plant exceeds the annual amount of depreciation expense for the company's Oregon rate base in that year.⁵

In response, the LDCs disagreed with Staff and CUB that recoverable costs should be limited to capital costs, because a future safety program may consist primarily of O&M expenses that are difficult to forecast in rates. The LDCs also disagreed with Staff's depreciation test, stating that depreciation expense allows a utility to recover its return of past investment and should not be applied to future investments. The LDCs also noted many areas of agreement with the parties, including that the utility must set forth the specific, significant investments that will be recovered, that the mechanism include an earnings test, and that the mechanism be periodically reviewed.

⁵ Staff/300, Johnson/4. See also Staff/300, Johnson/6 for a table setting out the parties' recommended guidelines.

2. *Safety Plans*

All parties agreed that the LDCs should file annual or bi-annual safety plans for review by the Commission. CUB proposed a safety plan process that would either be part of an LDC's integrated resource plan (IRP) or a separate safety docket, and that filing of a safety plan should precede approval of any safety cost recovery mechanism. CUB explained that the safety plan would identify all of an LDC's safety projects, the safety standards the LDC is trying to meet, the measures proposed, and the proposed accounting treatment. CUB also outlined suggestions for the contents and process of a safety cost recovery mechanism application.

The LDCs believed that a safety plan should be filed prior to, or contemporaneously with, an initial request for a safety cost recovery mechanism. Thereafter, the safety plan would be filed annually, separately from the IRP but following a similar format, although on a more compressed timeline. The LDCs believed that if an LDC has not been granted a safety cost recovery mechanism, it should not be required to file a safety plan, and any safety investments will be evaluated in a general rate case.

B. Stipulation

In their stipulation, the parties agree to a set of guidelines to govern safety cost recovery mechanisms, or SCRM, which LDCs may propose to recover safety investment costs outside of a general rate proceeding. The parties also agree that LDCs should file annual Safety Project Plans (SPPs) for Staff and stakeholder review.

1. *Guidelines for SCRM*

The parties ask us to adopt six guidelines, summarized here and described in full in the attached stipulation:

1. A safety cost recovery mechanism may be established in a general rate case or within three years of a general rate case. This helps ensure an LDC's overall rates are appropriate at the time the safety cost recovery mechanism is approved.
2. A safety cost recovery mechanism will be limited to discrete, identified, safety-related capital investments. An LDC may request authorization to add qualified projects, subject to party comment. The parties explain that this allows parties to fully evaluate an LDC's proposal, while also giving the LDCs flexibility to modify the mechanism.

3. A safety cost recovery mechanism will have a cost recovery cap, which the Commission may adjust as needed. This encourages the LDC to manage costs.
4. A safety cost recovery mechanism will be subject to an annual earnings test that will allow recovery only when recovery does not cause the LDC to exceed its authorized return on equity. The earnings test protects customers.
5. A safety cost recovery mechanism will recover costs only to the extent the LDC's total annual capital investments in all plant exceeds the annual amount of depreciation for the LDC's Oregon rate base.
6. The duration of the safety cost recovery mechanism will be specified at the time it is established, and may be modified by the Commission as needed. The limited duration links the recovery mechanism to the duration of the project.

The parties add that the stipulation does not preclude an LDC from seeking deferred accounting and cost recovery of O&M or capital costs associated with safety projects at any time. If an LDC is authorized to use a safety cost recovery mechanism, it will file an annual report providing the status of the safety costs included in the mechanism, comparing actual costs to projected costs, and relevant earnings test information.

2. *Safety Project Plans*

The stipulation also requires each LDC to file an annual Safety Project Plan for our review. The parties explain that the filing of a safety plan is intended to increase transparency into safety investments. The safety plan information will be particularly helpful to parties reviewing safety investments in the more expedited safety cost recovery mechanism process.

The parties explain that a safety plan will provide parties with a yearly snapshot of the LDC's expected safety investments and activities, allowing parties to evaluate the costs and benefits. The safety plan will include a twelve month planning period, a description of safety initiatives for the planning period, a description of the risks addressed with the safety projects, a description of the analysis supporting the safety projects, with cost-

benefit analysis of projects and alternatives considered, and explanation of any change from the previous plan.⁶

As for process, the parties propose that each LDC file a safety plan before the end of September annually with the Commission. Under the parties' proposed process, we will establish a period for comments, Staff will file a public meeting memorandum, and we will review the plan at a public meeting. The parties emphasize that the safety plan is not a ratemaking filing and inclusion of a project in a safety plan is not a prerequisite for recovery of costs in a general rate case. The parties also clarify in the stipulation that the safety plan process does not change the standard for a prudence review in a general rate case, with respect to either the costs of the project or the determination to proceed with the project.

C. Commission Resolution

We adopt the parties' stipulation with two clarifications. First, the depreciation test included in the stipulation has no precedent in our ratemaking history, and we have no means to evaluate its impact on future recovery of safety investment costs. Consequently, we interpret the test as a non-binding guideline to consider in our safety cost recovery mechanism review. We also agree with the utilities that traditional ratemaking treatment of depreciation expense allows a utility to recover its return of past investment; therefore it is not generally appropriate to apply that depreciation expense to offset future investments. For this reason, we adopt the depreciation test here as a stipulated customer-protection mechanism, but not as precedent for any future ratemaking issues.

Second, we view the safety plan as an informational report only. We agree with the parties that narrative descriptions of anticipated safety projects will help the parties and the Commission to better understand upcoming LDC safety projects, but we will not be taking any Commission action on these informal plans.

With these clarifications, we agree with the parties that the safety cost recovery guidelines and the safety plan process described in the stipulation constitute a fair and reasonable resolution of the issues in this proceeding. The guidelines provided in the stipulation establish a framework for our review of future safety cost recovery mechanism proposals. The LDCs' safety plan filing will facilitate communication

⁶ The safety plan will identify actions based on the more technical analysis provided to Staff through the Distribution Integrity Management Program (DIMP) or Transmission Integrity Management Program (TIMP). Stipulation at 5.

between the parties and the Commission, and inform us of upcoming safety requirements. For these reasons, we adopt the stipulation.

IV. ORDER

IT IS ORDERED that the stipulation between Northwest Natural, dba NW Natural; Avista Corporation, dba Avista Utilities; Cascade Natural Gas Corporation; Staff of the Public Utility Commission of Oregon; the Citizens' Utility Board of Oregon; and the Northwest Industrial Gas Users, attached as Appendix A, is adopted.


Made, entered, and effective MAR 06 2017.



Lisa D. Hardie
Chair



John Savage
Commissioner



Stephen M. Bloom
Commissioner

A party may request rehearing or reconsideration of this order under ORS 756.561. A request for rehearing or reconsideration must be filed with the Commission within 60 days of the date of service of this order. The request must comply with the requirements in OAR 860-001-0720. A copy of the request must also be served on each party to the proceedings as provided in OAR 860-001-0180(2). A party may appeal this order by filing a petition for review with the Court of Appeals in compliance with ORS 183.480 through 183.484.

**BEFORE THE PUBLIC UTILITY COMMISSION
OF OREGON**

UM 1722

In the Matters of

PUBLIC UTILITY COMMISSION OF
OREGON

Investigation into Recovery of Safety
Costs by Natural Gas Utilities (UM 1722)

STIPULATION

This Stipulation resolves all issues among all parties to this docket related to the Public Utility Commission of Oregon's ("Commission") investigation into recovery of safety costs by natural gas utilities.

PARTIES

1. The parties to this Stipulation are NW Natural, Avista Corporation ("Avista"), Cascade Natural Gas Corporation ("Cascade"), Commission Staff ("Staff"), Northwest Industrial Gas Users ("NWIGU"), and the Citizens' Utility Board of Oregon ("CUB") (collectively, "Parties").

BACKGROUND

2. Since 2001, NW Natural has utilized a cost recovery mechanism under which it may defer and recover on an annual basis the costs it incurs associated with its System Integrity Program ("SIP"), which implements federal legislation and regulations requiring natural gas pipeline operators to make critical improvements to enhance system

safety and reliability. The SIP cost recovery mechanism was scheduled to expire on October 31, 2014, unless extended by the Commission

3. On October 14, 2014, NW Natural filed Advice No. 14-23 requesting that the Commission continue the SIP cost recovery mechanism. The filing was docketed as UG 286.

4. On March 25, 2015, the Commission issued Order No. 15-093, which suspended NW Natural's Advice No. 14-23 for investigation and opened a generic investigation to examine the recovery of safety costs by local distribution companies (LDC). The generic investigation was docketed as UM 1722 and was consolidated with UG 286. NW Natural, Cascade, Avista, NWIGU, and CUB intervened.

5. On April 15, 2015, Administrative Law Judge Shani Pines held a prehearing conference at which the Parties agreed to hold a workshop on May 20, 2015.

6. Following the May 20, 2015 workshop, Administrative Law Judge Sarah Rowe held a second prehearing conference on September 30, 2015.

7. On October 9, 2015, ALJ Rowe issued a procedural schedule in the docket.

8. Staff and CUB served discovery requests on NW Natural, Avista, and Cascade. The Parties conducted a thorough investigation into the recovery of safety costs by natural gas utilities.

9. On December 1, 2015, NW Natural, Avista, and Cascade filed Joint Testimony that proposed guidelines for safety investment recovery mechanisms. NW Natural also filed testimony on its own behalf supporting its request to extend the SIP cost recovery mechanism.

10. On February 8, 2016, Staff, CUB and NWIGU each filed testimony responding to the Joint Testimony and NW Natural's Testimony.

11. On March 4, 2016, NW Natural withdrew its Advice No. 14-23, which had requested that the Commission extend its SIP cost recovery mechanism. As a result of the withdrawal, the Commission closed docket UG 286 on March 28, 2016.

12. On March 9, 2016, all Parties filed reply testimony.

13. On April 13, 2016, NW Natural, Avista, and Cascade filed Supplemental Reply Testimony to address a new issue raised by Staff and CUB in their Reply Testimony. Specifically, the Joint Utilities were supportive of Staff and CUB's new proposal that natural gas utilities file annual safety plans, subject to certain conditions and modifications.

14. On April 15, 2016, ALJ Rowe issued a ruling vacating the procedural schedule in this docket and instructing the Parties to undertake further settlement discussions.

15. Thereafter, the Parties held several settlement conferences. At the settlement conference held on June 23, 2016, the Parties agreed to resolve all the issues in this docket.

16. This Stipulation, presented on behalf of the Parties to this docket, resolves all issues in this docket.

AGREEMENT

17. Guidelines for Recovery of Safety Costs. The Parties agree that the Commission should adopt the following guidelines to apply to natural gas utilities' requests for an annual mechanism to track safety related costs into rates ("Safety Cost Recovery Mechanism" or "SCRM"):

i. An SCRM may be established in a general rate case ("GRC") or within three years of a final order in a GRC.

ii. An SCRM will be limited to discrete safety related capital investments or other costs that are capitalized and that are identified at the time the SCRM is established. An LDC may request authorization from the Commission to modify an SCRM to include additional discrete safety related capital investments that otherwise meet these guidelines, and other parties are free to support or oppose such a request.

iii. An SCRM shall have a cost recovery cap, which will be set at the time the SCRM is established. The cost recovery cap may be adjusted up or down by the Commission to reflect new safety related projects that may be included in the SCRM in later years, or the removal or modification of safety related projects included in the SCRM.

iv. SCRMs will be subject to an annual earnings test that will allow utility investments to be tracked into rates only where the recovery does not cause the utility to exceed its authorized Return on Equity.

v. An SCRM will only recover eligible costs on an annual basis to the extent the LDC's total annual capital investments in all plant exceeds the annual amount of depreciation for the LDC's Oregon rate base.

vi. The duration of the SCRM will be specified at the time the SCRM is established. The duration may be modified if new safety-related projects are added to the SCRM in later years by the Commission.

18. Deferred Accounting. This Stipulation does not prohibit an LDC from seeking deferred accounting and cost recovery of O&M or capital costs associated with safety related projects at any time.

19. SCRM Annual Reports. If an LDC is authorized by the Commission to utilize an SCRM, the LDC will file an annual report with the Commission providing the status of the safety projects included in the SCRM, including comparisons of projected costs to actual costs, and relevant earnings test information.

20. LDC Annual Safety Plans. The LDCs will file annual system safety plans (SPP) with the Commission. The purpose of the SPP is to:

i. Explain the expected level of capital investment and O&M expense required to mitigate issues identified by risk analysis or to meet newly implemented federal code.

ii. Demonstrate to ratepayers and the public the LDCs' commitment to and prioritization of safety planning.

iii. Explain technical reports provided to the Commission's Safety Staff in a manner easily understood by the public, and other regulatory stakeholders.

iv. Identify when major regulatory changes drive new safety planning priorities and/or changes to existing safety plans.

21. The SPP is not intended to:

i. Replicate the analysis used for Distribution Integrity Management Program (DIMP) or Transmission Integrity Management Program (TIMP), but the SPP should identify and explain when actions are based on this analysis.

ii. Provide in-depth descriptions of models and algorithms used to evaluate risks.

iii. Replicate filings already provided to the Commission's Safety Staff.

22. The elements of the SPP will include:

i. A twelve-month planning period;

ii. Identification and narrative description of the LDC's significant safety initiatives and projects for the planning period;

iii. Identification and narrative description of the perceived risks addressed with the planned safety initiatives and projects;

iv. Narrative description of the analysis and methodology underlying the decisions to proceed with safety initiatives and projects;

v. Narrative description of the cost-benefit analysis underlying safety initiatives and projects, including alternatives considered; and

vi. Explanation of any significant changes in safety plans from the prior year SPP.

23. The procedural process for the SPP will be as follows:

- i. On or before September 31 annually, each LDC will file an SPP, for the upcoming calendar year, with the Commission.
- ii. The Commission will establish a period for interested parties to file comments regarding the SPP with the Commission.
- iii. Staff will file a public meeting memorandum.
- iv. The SPP will be reviewed at a public meeting.
- v. The parties will periodically review the requirements for the content and scope of the SPP to ensure it fulfills the purposes of the plan outlined in paragraph 20.

24. The parties agree that the inclusion of a safety-related project in the SPP is not a prerequisite to recovery of the costs associated with that project in a GRC. Further, the SPP process does not change the standard for a prudence review in a GRC, with respect to either the costs of the project or the determination to proceed with the project.

25. Standard Provisions. The Parties agree to submit this Stipulation to the Commission and request that the Commission approve the Stipulation as presented.

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

27. If this Stipulation is challenged, the Parties agree that they will continue to support the Commission's adoption of the terms of this Stipulation. The Parties agree to cooperate in cross-examination and put on such a case as they deem appropriate to respond fully to the issues presented, which may include raising issues that are incorporated in the settlements embodied in this Stipulation.

28. The Parties have negotiated this Stipulation as an integrated document. If the Commission rejects all or any material part of this Stipulation, or adds any material

condition to any final order that is not consistent with this Stipulation, each Party reserves its right, pursuant to OAR 860-001-0350(9), to present evidence and argument on the record in support of the Stipulation or to withdraw from the Stipulation. Parties shall be entitled to seek rehearing or reconsideration pursuant to OAR 860-001-0720 in any manner that is consistent with the agreement embodied in this Stipulation.

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

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

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

SIGNATURE PAGE TO FOLLOW

ORDER NO. 17 084

NW NATURAL

By: 

Printed Name: ZACHARY KRAUTZ

Date: 8-4-16

STAFF

By: _____

Printed Name: _____

Date: _____

CITIZENS' UTILITY BOARD OF
OREGON

By: _____

Date: _____

NORTHWEST INDUSTRIAL GAS
USERS

By: _____

Date: _____

AVISTA CORPORATION

By: _____

Date: _____

CASCADE NATURAL GAS COMPANY

By: _____

Date: _____

ORDER NO. 17 084

NW NATURAL

By: _____

Printed Name: _____

Date: _____

STAFF

By: Mike Weinrich for Stephanie Andrews

Printed Name: Mike Weinrich

Date: 9/23/16

CITIZENS' UTILITY BOARD OF
OREGON

By: _____

Date: _____

NORTHWEST INDUSTRIAL GAS
USERS

By: _____

Date: _____

AVISTA CORPORATION

By: _____

Date: _____

CASCADE NATURAL GAS COMPANY

By: _____

Date: _____

NW NATURAL

STAFF

By: _____

By: _____

Printed Name: _____

Printed Name: _____

Date: _____

Date: _____

CITIZENS' UTILITY BOARD OF
OREGON

NORTHWEST INDUSTRIAL GAS
USERS

By: 

By: _____

Date: 8/2/16

Date: _____

AVISTA CORPORATION

CASCADE NATURAL GAS COMPANY

By: _____

By: _____

Date: _____

Date: _____

ORDER NO. 17 084

NW NATURAL

STAFF

By: _____

By: _____

Printed Name: _____

Printed Name: _____


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Date: _____

CITIZENS' UTILITY BOARD OF
OREGON

NORTHWEST INDUSTRIAL GAS
USERS

By: _____

By:  _____

Date: _____

Date: 8/2/2016 _____

AVISTA CORPORATION

CASCADE NATURAL GAS COMPANY

By: _____

By: _____

Date: _____

Date: _____

ORDER NO. 17 084

NW NATURAL

STAFF

By: _____

By: _____

Printed Name: _____

Printed Name: _____

Date: _____

Date: _____

CITIZENS' UTILITY BOARD OF
OREGON

NORTHWEST INDUSTRIAL GAS
USERS

By: _____

By: _____

Date: _____

Date: _____

AVISTA CORPORATION

CASCADE NATURAL GAS COMPANY

By: [Signature]

By: _____

Date: 8/2/16

Date: _____

ORDER NO. **17 084**

NW NATURAL

STAFF

By: _____

By: _____

Printed Name: _____

Printed Name: _____

Date: _____

Date: _____

CITIZENS' UTILITY BOARD OF
OREGON

NORTHWEST INDUSTRIAL GAS
USERS

By: _____

By: _____

Date: _____

Date: _____

AVISTA CORPORATION

CASCADE NATURAL GAS COMPANY

By: _____

By: Michael Pa

Date: _____

Date: 8/4/16