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August 21, 2026

VIA ELECTRONIC FILING

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

Re: AR 676 - Rulemaking to Establish Multi-Year Rate Plan Framework (HB 3179 & SB 688 Implementation)

Northwest Natural Gas Company, dba NW Natural ("NW Natural" or the "Company"), hereby files the Operations and Maintenance Expense Pre-Read Materials in docket AR 676.

Please address any correspondence on this matter to me, with a copy to the following:

eFiling
NW Natural
Rates & Regulatory Affairs
250 SW Taylor Street
Portland, Oregon 97204
Email: eFiling@nwnatural.com
Phone: (503) 610-7330

Sincerely,

NW Natural

/s/ Maddie Pulliam

Maddie Pulliam
Rates & Regulatory Analyst

Enclosure

Operations and Maintenance Expense

Revenue Requirement and "Going-In" Rates

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All else equal, each dollar of Operations and Maintenance ("O&M") expense adds $1 to the revenue requirement used to set going-in rates.

The basic ratemaking concept

The revenue requirement is the amount of annual revenue the utility must be authorized to collect to cover the reasonable costs of providing service and a fair return on invested capital. Under the current cost-of-service model, this calculation establishes the starting, or "going-in," rates for a multi-year rate plan.

O&M expense is one of the direct building blocks of that calculation. O&M expense includes payroll & wages, and the ongoing, non-capital costs required to operate the system, maintain safety and reliability, serve customers, meet regulatory obligations, and support the business. Unlike capital investment, O&M expense is generally expensed in the period incurred and does not earn a return.

This is a revenue-requirement relationship, not necessarily a one-dollar change to any individual customer's bill. After the total revenue requirement is determined, costs are allocated among customer classes and converted into rates using forecast customer counts, usage, and rate design. Revenue-related costs can also affect the final amount collected through rates.

ELEMENTS OF REVENUE REQUIREMENT

Operating & Maintenance	Day-to-day, non-capital costs of providing utility service
Depreciation Expense	Return of capital investment over an asset's useful life
Return on Rate Base	Cost of debt and authorized return on equity
Income Taxes	Federal and state income taxes
Other Taxes	Property, payroll, and other applicable taxes
Gas Costs	Commodity and upstream pipeline costs, recovered through the PGA

REVENUE REQUIREMENT	**Total annual revenue needed to provide service**

Important notes:

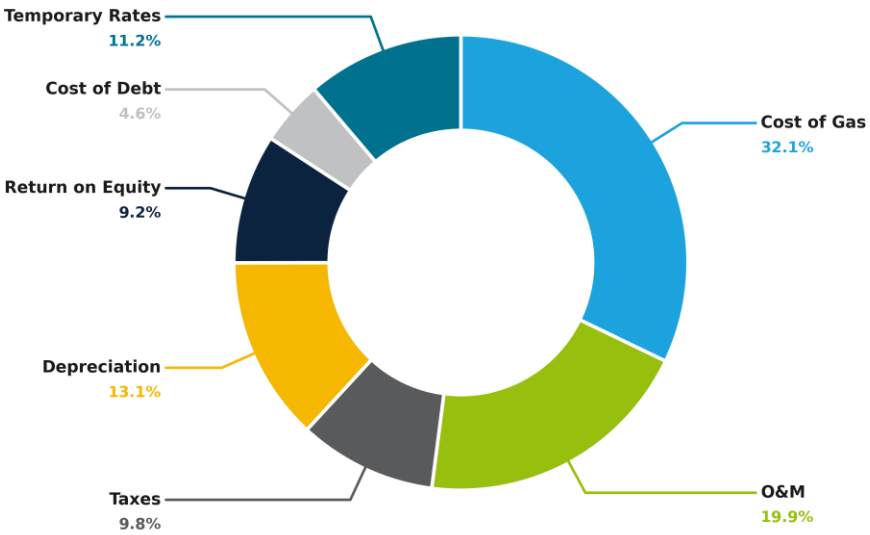
Gas costs are part of total revenue requirement but are ordinarily recovered through the Purchased Gas Adjustment (PGA) rather than base rates.

NW Natural plans to discuss depreciation expense and return on rate base at the Gas Distribution, Transmission and Storage workshops.

NW Natural plans to discuss Taxes and other items at the Gas Other costs workshop.

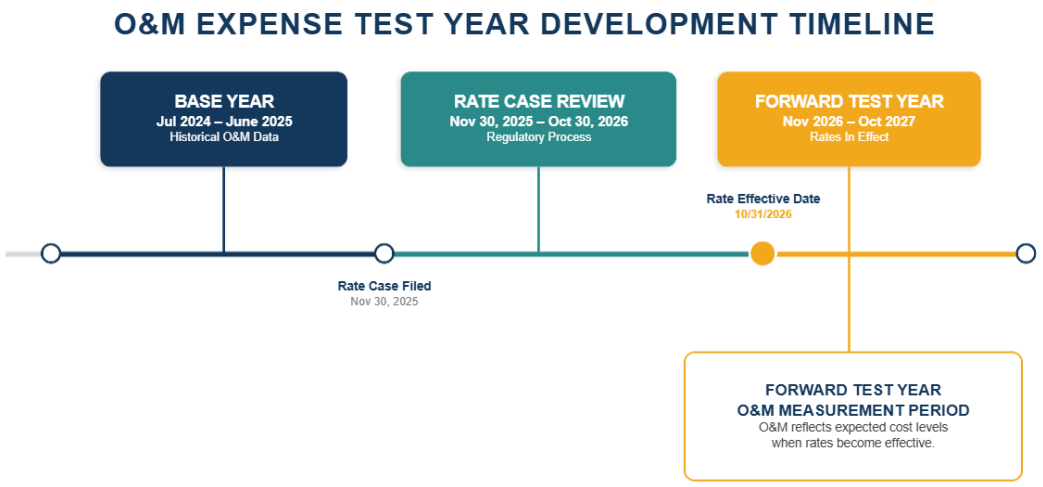
O&M as a Percentage of Total Bill

Below is a high-level illustrative break out of O&M as a portion of bills. Note: Temporary rates include deferrals and other adjustments that are typically outside of a revenue requirement determination



"Test Year" O&M Expense

Forward Test Year for O&M Expense. To set rates, utilities establish a level of O&M expense that reflects the conditions expected to exist while the new rates are in effect. The example below assumes a rate case filed in November 2025. Beginning with a historical base year (e.g., July 2024 – June 2025), actual O&M expense is normalized to remove non-recurring items and adjusted for known and measurable changes, producing a forecast of the costs the utility expects to incur once rates take effect. Because this forward test year is anchored to the rate effective date of October 31, 2026, the resulting O&M expense level captures a forward-looking snapshot of the cost of providing service during the period customers will actually pay for those services — rather than the cost of an earlier historical period.



O&M expense categories

Payroll (NBU/BU)
Employee labor costs for non-bargaining-unit (NBU) and bargaining-unit (BU) employees, including wages, salaries, overtime, and other labor-related costs needed to operate the utility.

Administrative and General (A&G)
A&G support costs, including regulatory, finance, planning, accounting, legal, human resources, employee benefits, insurance, safety, facilities, business governance, public relations and other business functions.

Information Technology (IT)
Technology and cybersecurity costs, including software subscriptions, cloud services, hardware and software maintenance, vendor support, system operations, and IT services that support utility operations and business functions.

Customer Service
Customer-facing and account-support costs, including billing and collections, payment processing, call-center support, customer communications, customer programs, and account administration.

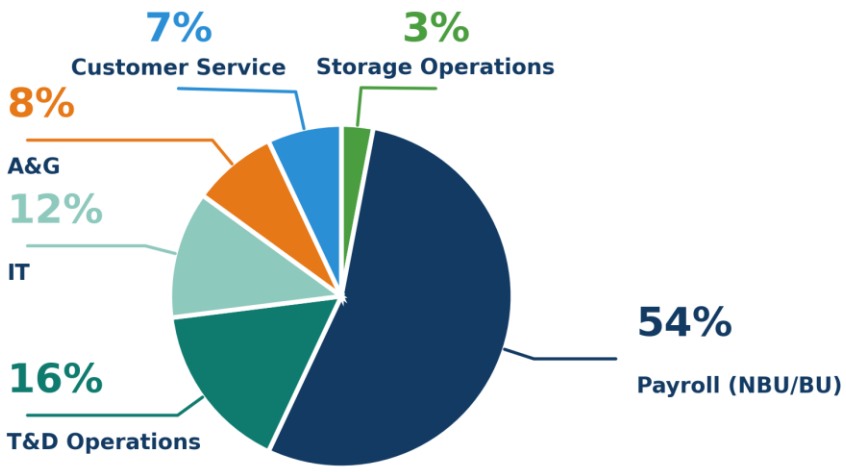
Transmission and Distribution (T&D) Operations

Costs to operate and maintain a safe gas utility system, including receiving stations, pipelines, service lines, meters, and regulators, and services such as locating underground facilities, leak surveys, integrity inspections, repairs, maintenance, engineering support, and routine field work.

Storage Operations

Costs to operate and maintain the underground gas storage system, liquefied natural gas (LNG) facilities, and related services needed to safely store, process, and deliver natural gas.

Illustrative O&M Cost Categories

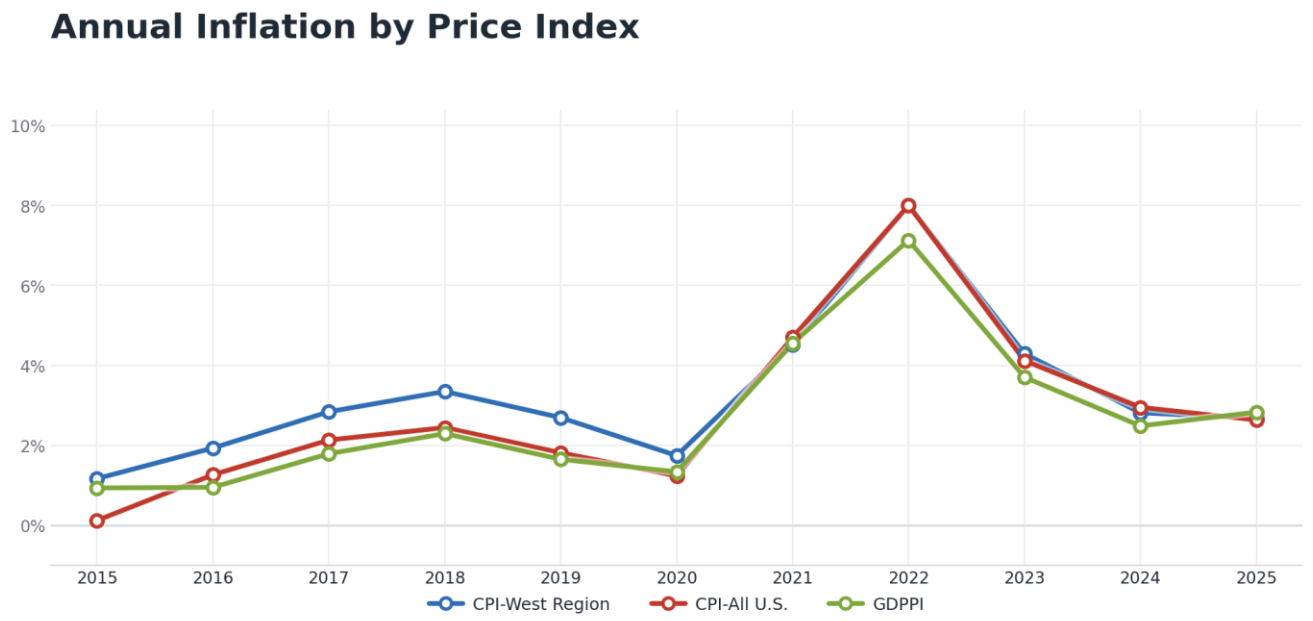


O&M Expense Cost Drivers and Adjustment-Factor Considerations

Inflation is a reasonable starting point for O&M expense categories that generally move with the overall economy. It is not always a good fit for every cost. Some O&M expense changes are driven by known contracts, required work, inspection cycles, customer behavior, market pricing, or accounting treatment. Those costs may move above or below inflation and may be uneven from year to year.

> **The objective is to match each material O&M expense category with the most appropriate, supportable method: standard escalation, a known and measurable contract, a specific forecast, or another targeted adjustment.**

As additional context, here is a breakout of how various inflation related indexes have changed over a 10-year period.



- **Consumer Price Index (CPI-All)** is a measure of inflation that tracks how the prices of a representative "basket" of goods and services purchased by consumers change over time. (Source: BLS)
- **Western CPI** (**CPI-West Region**) is a regional version of the Consumer Price Index that measures inflation specifically in the western United States rather than across the entire country. (Source: BLS)
- **GDPPI (Gross Domestic Product Price Index)** is a broad measure of inflation that tracks price changes across all goods and services produced in the U.S. economy. Unlike CPI, which measures what consumers buy, GDPPI measures price changes for the entire economy. (Source: BEA)

Examples of O&M expenses that may not follow standard inflation

Cost driver	Why inflation may not fit	Potential support
Union Wages	Collective-bargaining agreements are negotiated, arms-length contracts with our union. The wages have outpaced inflationary indices.	**Known agreements and focused forecasts**
Safety and Integrity Inspections	Required inspections and risk-based work determine the timing and scope of required activity. Well-casing re-inspections also shift required work from capital to O&M expense, which changes at non-inflationary levels. The cost of each inspection generally track with inflation but the amount of inspections does not.	**Known cost + operational schedule**

Contracted field services	Locating (Call 8-1-1) and survey costs are the contracted field services required to identify, mark, inspect, and verify underground utility facilities. These costs are driven by both contract pricing and the volume of locate requests and inspection work, which is why they often move differently than general inflation. The current contract provides for 3% annual rate increases through 2026.	**Known and measurable contract**
Customer-service transactions	Payment-processing expenses change with payment method, transaction volume, and contracted fees. Customers' use of credit cards increases costs above inflationary levels.	**Volume forecast plus contracted unit cost**
Insurance	Premiums and available coverage respond to utility insurance-market conditions and claims trends, which can change sharply between policy years. We use insurance brokers to bid out for this coverage to ensure competitive rates, but they have not tracked with inflation.	**Current quote or policy-year forecast**
Technology and cloud services	Subscriptions, cybersecurity needs, vendor pricing, and system replacements can create step changes. Cloud solutions also shift some costs from capital investment to ongoing O&M expenses.	**Contract and implementation forecast**

Why the distinction matters

- **Accuracy.** A broad escalation factor can overstate some costs and understate others. Category-specific support improves the forecast.
- **Transparency.** Contracts, work plans, volumes, and regulatory requirements provide a clear basis for review.
- **Operational reality.** Required work may change in timing, scope, or accounting treatment even when economy-wide inflation is stable.
- **Balanced treatment.** Costs that adjust below inflation should be reflected just as costs that change above inflation are reflected.
- **Rate Smoothing.** If non-inflationary O&M expenses are not accurately captured during the multi-year rate plan (MRP), unrecovered costs will accumulate and regulatory lag will grow. That accumulated gap may then require a considerable increase in going-in rates at the start of the next MRP. Accurate treatment during the plan period can moderate that reset and produce a smoother rate path over time.

Customer Programs and Annual Cost Recovery

Customer programs include the **low-income discount program, arrearage management program, demand response programs, and transportation-customer energy-efficiency programs**. These programs are driven by policy to advance shared objectives, including energy affordability, customer assistance, demand response, and energy efficiency.

The costs of administering and delivering these programs would otherwise be treated as O&M expenses because they are ongoing, non-capital costs incurred to provide customer services and carry out approved program requirements. Examples include program administration, customer enrollment and support, vendor services, outreach, incentives, measurement and reporting, and related regulatory compliance activities.

Today, these program costs are deferred on our balance sheet and amortized annually based on the amounts actually spent. This approach provides one-for-one recovery of prudently incurred program costs and aligns recovery with actual program activity.

Annual one-for-one recovery is important because program costs can be volatile from year to year based on customer participation.

Policy rationale: Annual one-for-one recovery removes the potential for utilities to over- or under-recover their expenses and promotes shared goal of expansion of these programs.

O&M Expense Deferrals for Start-Up Costs

A different type of deferral may be appropriate for O&M expenses associated with the start-up of a new program or major undertaking. For example, a large IT transition may involve implementation, training, vendor, or other transition costs that cannot be capitalized and therefore must be recorded as expense when incurred.

These costs can be significant and uneven, but they are not representative of the ongoing O&M expense level needed to operate the program after implementation. The Company has deferred these O&M expenses and amortized them over a defined period to mitigate the immediate rate impact to customers.

Necessary Business Expenses and the Built-In Recovery Gap

A utility must incur certain expenses to operate prudently, safely, and effectively, just as other well-managed businesses do. These costs do not become optional simply because Oregon ratemaking practices may limit or exclude their recovery from customers.

Competitive employee compensation Market-based pay and benefits are necessary to recruit and retain the employees who operate the system, serve customers, maintain technology, and meet safety and regulatory obligations.	**Competitive executive compensation** Qualified leadership is required to manage a complex, highly regulated utility and remain accountable for operational, financial, safety, and compliance performance.
Directors and Officers (D&O) insurance D&O insurance is a standard corporate risk-management expense that protects the utility and its leadership against covered governance and management claims.	**Corporate communications** Businesses must communicate with customers, recruit employees, provide information, and maintain an effective public presence.

Oregon rates do not start from full expense recovery

Oregon ratemaking may exclude or limit recovery of portions of these expenses even when the utility continues to incur them because they are necessary for ongoing operations.

The result is a built-in recovery gap: the Company's authorized revenue requirement begins below the total cost the Company must incur to operate the business. **The utility must absorb the excluded or reduced portion through efficiencies elsewhere or accept less-than-authorized earnings.**

Connection to a stretch factor

A stretch factor assumes that the utility can achieve additional efficiency savings beyond the expense changes otherwise reflected in the rate plan. That assumption should be evaluated in light of the built-in recovery gap already embedded in Oregon rates.

- **The first reduction occurs in the revenue requirement.** Certain necessary business costs are excluded or only partially recovered even before rates are set.
- **A stretch factor creates a second reduction.** It lowers the annual O&M expense adjustment on the assumption that still more savings can be achieved during the rate-plan period.
- **The effects are cumulative.** The stretch factor is therefore not applied to a revenue requirement that provides full recovery of all expenses incurred to operate the business. Rather, it is layered on top of costs the Company is already required to absorb.