BEFORE THE PUBLIC UTILITY COMMISSION

OF OREGON

UG 344

In the Matter of NORTHWEST NATURAL GAS COMPANY, dba NW NATURAL, Request for a General Rate Revision.	ALLIANCE OF WESTERN ENERGY CONSUMERS' BRIEF IN OPPOSITION TO THREE-PARTY STIPULATION

Pursuant to the rulings of Chief Administrative Law Judge Michal Grant o/b/o Administrative Law Judge Allen J. Arlow on September 6, 2018 and September 26, 2018, the Alliance of Western Energy Consumers ("AWEC") submits to the Public Utility Commission of Oregon (the "Commission") this Brief in Opposition to the Three Party Stipulation ("Contested Stipulation") filed by Northwest Natural Gas Company ("NW Natural"), Staff of the Public Utility Commission of Oregon ("Staff") and the Citizens' Utility Board ("CUB"). This Brief summarizes the more detailed Testimony in Objection to Three-Party Stipulation of Bradley G. Mullins on behalf of AWEC.[1]

I. INTRODUCTION

On December 29, 2017, NW Natural filed a request for a general rate increase and revised tariff sheets to become effective November 1, 2018. NW Natural requested a revision to customer rates that would increase the Company's annual Oregon jurisdictional revenues by $52.4 million.[2] On March 20, 2018, the Company filed supplemental direct testimony regarding

[1] AWEC/600/Mullins/1-24.

[2] *See In the Matter of Nw. Natural Gas Co. Application for General Rate Revision*, Docket No. UG 344, NW Natural Executive Summary (Dec. 29, 2017) at 1:6-8.

updates to the test year and revenue requirement that accounted for, among other things, some of the impacts of the 2017 federal Tax Cuts and Jobs Act ("TCJA") to the Test Year. The impact of these revisions was to reduce NW Natural's requested revenue requirement to $37.8 million.[3]

After several rounds of testimony and a series of settlement conferences, on August 6, 2018, NW Natural, Staff, CUB and AWEC submitted a stipulation agreement (the "Stipulation") to the Commission resolving all but three issues in this proceeding.[4] AWEC urges the Commission to adopt the Stipulation.

Then, on September 7, 2018, NW Natural, Staff and CUB entered into the Contested Stipulation, making a number of new radical ratemaking proposals which were never addressed in the evidentiary phase of this docket, including proposals on how to deal with (1) the treatment of NW Natural's pension balancing account ("PBA") and how to address pension costs going forward; and (2) the impact of the TCJA on NW Natural's interim deferred tax benefits from January 1, 2018 through October 31, 2018 ("Interim Period deferral") and excess deferred federal income tax ("EDFIT"). The sharing of revenues produced from the optimization of certain NW Natural assets and storage operations and the proper approach to reporting NW Natural's optimization revenues remained unresolved.

SUMMARY OF AWEC'S POSITIONS AND ARGUMENTS

Pension Balancing Account

In Docket UM 1475, NW Natural established a PBA to address a deficiency in recovery of pension expenses that it was collecting. At that time, NW Natural forecast that pension expenses and revenues would eventually balance out, and that further contributions from

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[3] NW Natural/1200, McVay/5:15-17.

[4] *In the Matter of Nw. Natural Gas Co. Application for General Rate Revision*, Docket No. UG 344, Stipulation (Aug. 6, 2018).

ratepayers would be unnecessary.[5] This trend, however, never materialized and all parties agree that the PBA is not sustainable.[6] The Contested Stipulation contains a proposal to begin amortizing in rates $94,600,000 in pension expense that has been recorded in the PBA, which has not been shown to be completely a ratepayer obligation. While AWEC agrees with the proposal to terminate or freeze the PBA and adopt a ratemaking methodology based on SFAS 87 for future pension costs, AWEC urges the Commission to open an investigation into the proper treatment and ratepayer/shareholder responsibilities for the balances in the account. Additionally, AWEC opposes NW Natural's proposal to use amounts due to ratepayers from the TCJA to pay down the PBA over a 10-year period. The tax benefits should be refunded to ratepayers without unreasonable delay and considered separately from the PBA because they are distinct issues that should be addressed separately on their own merits.

Tax Cuts and Jobs Act

On December 22, 2017, the United States Congress enacted a federal income tax reform, known as the TCJA. Among other things, the TCJA lowers the U.S. federal corporate income tax rate from 35 percent to 21 percent, effective January 1, 2018.[7] The two TCJA related items addressed in the Contested Stipulation are the Interim Period deferral and EDFIT. AWEC recommends that the best estimate of both of these amounts be considered in the rates that go into effect on November 1, 2018.

Mr. Mullins calculated that $13,890,000 is the amount due to customers in connection to the Interim Period, which over 2 years, equates to an annual amortization of $7,735,000.[8] Mr. Mullins detailed this calculation on Pages 1-3 of Exhibit AWEC 602. Notwithstanding, Mr.

[5] NW Natural's Opening Brief at 18:13-15.
[6] NW Natural's Opening Brief at 19:7-13.
[7] AWEC/200, Mullins/6:3-5.
[8] AWEC/600/Mullins/12.

Mullins recommends that the provisional amortization be set at $5,000,000, which is a value less than both AWEC's calculation and the calculation provided by NW Natural.[9] This way customers would begin to see the benefits associated with the Interim Period tax savings, and the Commission would still be free to adopt either approach, without requiring a corresponding reduction in the second year.[10]

Further, AWEC continues to have concerns with the methodological assumptions used to calculate EDFIT. Notwithstanding, AWEC is in general agreement with the EDFIT balances and amortization amounts that have been identified in the Contested Stipulation. However, the $6,700,000 of unprotected EDFIT funds NW Natural proposes to earmark for the PBA balance should be refunded to transportation customers, in the same way that the $14,640,000 of unprotected EDFIT due to sales customers is being refunded to sales customers.[11] Treating these two items differently is discriminatory towards transportation customers, who would not receive the same treatment as sales customers with respect to EDFIT.

II. ARGUMENT

A. The Contested Stipulation's Treatment of the Pension Balancing Account and Tax Reform Is Not Fair, Just or Reasonable.

The Contested Stipulation, if approved, would allow NW Natural to apply the customer owned tax refund amounts to offset a regulatory account balance, where there is no evidence that customers are responsible for 100 percent of those PBA amounts. This is in no way an acceptable settlement term to AWEC or in the public interest. Ratepayers deserve to get the refunds associated with the TCJA reform in a timely and reasonable manner and not have them

[9] AWEC/600/Mullins/12-13.
[10] *Id.*
[11] *Id.* at 17.

earmarked for a regulatory account balance that has not yet been shown to be a ratepayer obligation. The PBA and TCJA refunds are two are separate issues that AWEC recommends the Commission decide and consider on their own merits.

B. The Commission Should Terminate or Freeze the Pension Balancing Account.

It is undisputed that the PBA has failed to operate as expected when the Commission approved the stipulation in UM 1475.[12] AWEC recommends that the Commission terminate or freeze the pension balancing account, transition going forward to a ratemaking methodology based on SFAS 87 pension expense and open an investigation to determine how to deal with the balances in the PBA.

In Docket UM 1475, NW Natural filed an application for deferral of FAS 87 pension expense to fund NW Natural's pension plans.[13] At the time, NW Natural was concerned that its FAS 87 expense was greater than the $3.8 million it was collecting in rates.[14] NW Natural forecasted that this deficiency would continue for three more years, followed by a period of four years in which expenses and revenues would balance out, and then a period where expenses would be less than $3.8 million.[15] After settlement discussions, NW Natural entered into a stipulation with NWIGU, CUB and Staff establishing a pension balancing account rather than a deferral.[16] NW Natural agreed to establish this balancing account, with the expectation the balancing account would net to zero in approximately twelve to thirteen years.[17]

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[12] *In the Matter of Nw. Natural Gas Co. Application to Defer Pension Costs*, Docket No. UM 1475, Order No. 11-051 (Feb. 10, 2011).
[13] *In the Matter of NW. Natural Gas Co. Application to Defer Pension Costs*, Docket No. UM 1475, Application to Defer Pension Costs (Mar. 15, 2010).
[14] *In the Matter of NW. Natural Gas Co. Application to Defer Pension Costs*, Docket No. UM 1475, Joint Brief in Support of Stipulation (Dec. 13, 2010) at 1.
[15] CUB/100, Jenks-Gehrke/34:13-18.
[16] *In the Matter of NW. Natural Gas Co. Application to Defer Pension Costs*, Docket No. UM 1475, Order No. 11-051 (Feb. 10, 2011) at 2-3.
[17] *Id.* at 3.

Rather than leveling off after three years as predicted, the balancing account has continued to grow and is currently unmanageable. When NW Natural requested the balancing account, it was facing a pension expense of three to four million dollars greater than was accounted for in its rates.[18] In contrast, the Contested Stipulation is requesting that $94,600,000 be amortized into customer rates for a 10 year period to pay off the balances in the account, which does not include the more than $8 million that will be recovered from ratepayers annually to pay current and future pension amounts. Transitioning to a SFAS expense methodology will represent a significant increase for ratepayers compared to the amounts the parties stipulated to in Docket UM 1475, but AWEC does not oppose doing so.[19] The Contested Stipulation provides for an $8.1 million increase to NW Natural's revenue requirement to recover test year FAS 87 pension expense going forward.[20]

However, the Commission should open a new proceeding to address how to deal with the $94,600,000 PBA balance, and what amount should be recovered from customers and what amount should be recovered from shareholders. SFAS 87 pension expenses are based on historical contributions, interest rates and other actuarial assumptions.[21] Therefore, to consider the responsibly for these balances, it is necessary to perform an analysis for each year to analyze the prudence of historical pension contribution levels, interest rate assumptions, and other actuarial assumptions, which give rise to the year-to-year balances.[22] If, for example, the higher than expected expenses were caused by an imprudent pattern of contributions, then it would not be appropriate for NW Natural to recover those amounts. Further, if the interest rate

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[18] UM 1475 NW Natural/200, Feltz/15.
[19] AWEC/500, Mullins/4:6-7.
[20] Second Partial Stipulation, p. 5.
[21] AWEC/500, Mullins/4:15-16.
[22] AWEC/500, Mullins/4:16-19; *See* ORS 757.259(5) (providing that "the Commission's determination on the amount of deferrals allowable in the rates of the utility is subject to a finding by the Commission that the amount was prudently incurred by the utility").

assumptions have declined based on actions taken by NW Natural to reduce the risk of its pension portfolio, that may be an indication of imprudence.[23]

Finally, the stipulation in UM 1475 provides that if NW Natural's earnings exceed the company's authorized rate of return on equity, NW Natural must remove that amount from the pension expense booked to the SFAS 87 pension expense balancing account.[24] To effectuate this provision, the stipulation requires that NW Natural present an earnings test. No earnings test has been provided.

If the Commission agrees that the PBA has not functioned as intended and should be frozen or terminated, AWEC recommends that the Commission open an investigation regarding the ratemaking treatment of the remaining balance in the account. There is simply insufficient information in this docket to properly assess the extent to which ratepayers should be responsible for the remaining balances in the PBA.

C. AWEC Opposes the Contested Stipulation's Proposal to Apply TCJA Refunds to The Pension Balancing Account.

The Contested Stipulation asks that the Commission authorize the amortization of TCJA refunds to pay down the PBA.[25] AWEC disagrees with this approach. Amortization of TCJA refunds and the treatment of the PBA are distinct issues that must be addressed on their own merits. The PBA failed mid-way through its intended life and the recovery of pension costs should be transitioned going forward to a ratemaking method based on SFAS 87. But, as noted above, it is premature to assume that all the balances in the PBA are recoverable from ratepayers. Accordingly, it would be improper to apply TCJA refunds to the PBA balance before the

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[23] AWEC/500, Mullins/5:3-5.
[24] *In the Matter of NW. Natural Gas Co. Application to Defer Pension Costs*, Docket No. UM 1475, Stipulation (Nov. 4, 2010).
[25] NW Natural Opening Brief/22:15-17.

Commission determines, in a separate proceeding, how much of the PBA balance should be recovered from ratepayers—including application of an earnings test and consideration of actuarial assumptions.[26]

D. The Full Amount of Benefits Associated with the Federal Tax Cuts and Jobs Act Should be Returned to Customers

On December 22, 2017, the United States Congress enacted a major federal income tax reform, also known as the Tax Cuts and Jobs Act. Among other things, the TCJA lowers the U.S. federal corporate income tax rate from 35 percent to 21 percent, effective as of January 1, 2018.[27] There are two TCJA related issues addressed in the Contested Settlement—the Interim Period deferral and the EDFIT. AWEC urges the Commission to address amortization of the Interim Period Deferral and return of the EDFIT amounts separately from consideration of the PBA.

1. Amortization of the Interim Period Deferral Should Commence on November 1, 2018

Beginning on January 1, 2018, NW Natural's regulated utility income tax expense reflects the lower deferral income tax rate instituted by the TJCA.[28] NW Natural's current rates established in its last rate case reflect the higher pre-TJCA federal income tax rate amount and will remain in effect until NW Natural's rates are reset in this proceeding on November 1, 2018. As a result, NW Natural will collect from customers income tax expenses in excess of its actual tax liability from January 1, 2018 to November 1, 2018.[29]

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[26] AWEC/500, Mullins/6:16-19.
[27] AWEC/200, Mullins/6:3-5.
[28] *In the Matter of Nw. Natural Gas Co. Application for General Rate Revision*, Docket No. UG 344, Stipulation (Aug. 6, 2018) at 1.
[29] AWEC/602.

AWEC recommends that the Commission begin amortization of the Interim Period deferral on November 1, 2018. Mr. Mullins has concluded that the establishment of a deferral equal to $13,890,000, amortized over two years would be justified.[30] Notwithstanding, he recommended that the provisional amortization be set at $5,000,000, which is a value that is less than both his calculation and the calculation provided by NW Natural.[31] This way customers would begin see the benefits associated with the Interim Period tax savings, and the Commission would still be free to adopt either approach, without requiring a corresponding reduction in the second year.

2. AWEC Supports the Protected Excess Deferred Federal Income Tax Values Contained in the Contested Stipulation, But Not the Treatment of These Amounts.

Deferred income tax liabilities are amounts recorded on a utility's balance sheet that represent cash income taxes that will be paid by the utility in the future. Utility deferred income taxes usually arise when depreciation expense for plant investments are accelerated for income tax purposes into earlier periods.[32] Oregon utilities collect from customers both "current and deferred income taxes" of the utility.[33] Therefore, rates recover income taxes associated with the test year forecasted income of the utility, without regard to whether those income taxes are deferred or current.[34] Because the corporate income tax rate decreased, NW Natural will pay the decreased income tax rate on income taxes associated with test years for which customers paid the pre-TJCA rate.

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[30] AWEC/600, Mullins/12.
[31] *Id.* at 12-13.
[32] NW Natural, Opening Brief/30:10-12.
[33] ORS 757.269(1).
[34] NW Natural, Opening Brief/31:1-3.

For plant-related EDFIT, Mr. Mullins calculated $3,421,941, using the Alternative Method.[35] The Contested Stipulation provides for $3,263,000 of plant-related EDFIT amortization, which is within a range of reasonableness.[36] While the amount appears reasonable, AWEC requests that these amounts be refunded to ratepayers and not applied to the PBA balances.

3. The Contested Stipulation Treats Transportation Customers Unfairly

The $6,700,000 of unprotected EDFIT funds the Contested Stipulation proposes to earmark for the PBA balances should be refunded to transportation customers, in the same way that the $14,640,000 of unprotected EDFIT due to sales customers is being refunded to sales customers.[37] Treating these two items differently is discriminatory towards transportation customers, who would not receive the same treatment as sales customers with respect to EDFIT. Further, AWEC would accept a five-year amortization, which is the same period used for the refunds due to sales customers. Mr. Mullins recommended in his Opening Testimony to use a four-year amortization for these items, but five years is also reasonable.

III. Conclusion

For the reasons set forth above, AWEC respectfully requests that the Commission: (a) reject the Contested Stipulation; (b) terminate or freeze the pension balancing account, open a new docket to address how to deal with the balances and transition to ratemaking method based on SFAS 87 for future pension costs; and (c) decline to apply the Interim Period TJCA benefit and EDFIT amount to the PBA balances, and instead refund these monies to ratepayers under the amortization methodologies proposed by AWEC.

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[35] AWEC/600; Mullins/17.
[36] *Id.*
[37] *Id.* at 17-18

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Respectfully submitted,

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