BEFORE THE PUBLIC UTILITY COMMISSION
OF OREGON

UG 490

In the Matter of NORTHWEST NATURAL GAS COMPANY, dba NW Natural, Request for a General Rate Revision.	

STAFF OPENING BRIEF

I. Introduction.

This brief addresses the litigated issues in Northwest Natural Gas Company's ("NWN", "NW Natural", or "Company") general rate case. The parties to this docket, NW Natural, the Oregon Citizen's Utility Board ("CUB"), the Alliance of Western Energy Consumers ("AWEC"), Staff, and Coalition of Communities of Color, Climate Solutions, Verde, Columbia Riverkeeper, Oregon Environmental Council, Community Energy Project, and Sierra Club ("Coalition"), have addressed the majority of issues presented by NW Natural's filing through stipulations, leaving eight contested issues. Several of the contested issues stem from a fundamental disagreement between the Company and other parties to this docket about appropriate next steps in the face of the State's ambitious decarbonization goal and likely Greenhouse Gas Emission (GHG) reduction requirements, pressure from many quarters to eliminate natural gas service altogether, and the trend toward more energy efficient homes and appliances that reduces gas consumption.

Most notably, Staff, the Coalition, and CUB recommend eliminating NWN's residential Line Extension Allowance (LEA) that offsets the cost of facilities needed to connect new customers to the system, either through a phasedown consistent with the Commission's order in NW Natural's most recent rate case,[1] or an immediate elimination at the rate effective date of this rate case. The LEA is a subsidy paid for by all customers to defray a new customer's costs to connect to NWN's system and that the new customer repays by paying for service over many years. Staff, the Coalition, and CUB are concerned that in the current environment, the LEA creates risk of stranded investments that would inequitably harm future customers, particularly

[1] *In the Matter of Northwest Natural Gas Company, dba NW Natural, Request for a General Rate Revision*, UG 435, Order No. 22-388 (October 24, 2022).

those that are low-income. This is an opinion shared by other jurisdictions such as California,[2] which has mostly eliminated the LEA for all gas utilities, and Washington,[3] in which Avista Corporation and Puget Sound Energy have agreed to eliminate their LEAs through rate case settlements.

NWN proposes a more costly approach to addressing regulatory risk, at least from the customers' perspective. Rather than mitigating risk of stranded investment by eliminating the LEA, NWN proposes to keep the LEA and nearly triple the fixed basic charge for customers moving into new construction, from $8-$10 to $22.50 to $24.50, in an effort to ensure sufficient revenue to repay the LEA and fixed costs of the system. NWN also urges the Commission to modify the Renewable Natural Gas Automatic Adjustment Mechanism ("RNG AAC") to eliminate any regulatory lag for recovery of new investment in RNG and to limit the sharing contemplated by the mechanism when dollar-for-dollar recovery pushes the Company's earnings above 50 basis points below ROE. In contrast, Staff and other parties are concerned with NWN's apparent reliance on RNG to meet GHG emission reduction requirements given the cost of RNG compared to more cost-effective methods and question the need to modify the AAC to incentivize RNG acquisition even more.

In the argument below, Staff addresses its recommendations related to the appropriate next steps to address challenges faced by NW Natural in the current environment and other contested issues.

II. Contested Issues.

The issues in this docket not addressed in the parties' stipulations are as follows:

[2] See Staff/903, Dlouhy/81, CPUC Decision 22-09-026.

[3] See Staff/903, Dlouhy/99; Coalition/100, Cebulko/20.

a. Whether the Commission should modify NWN's RNG AAC to remove what NWN believes are disincentives to RNG investment?

b. Whether circumstances warrant eliminating the NW Natural's line extension allowance ("LEA") to protect future customers from stranded investments if LEAs go unrecovered?

c. Whether NW Natural should be allowed to increase the fixed basic charge for "new premises" customers joining the system after November 1, 2024, from $8-$10 to $22.50-$24.50 based on the theory such customers will use less gas than customers joining the system before November 1, 2024, and will not pay their share of fixed cost of the system through volumetric rates?

d. Whether the Commission should modify NW Natural's decoupling mechanism to more accurately capture expected load of customers that join the system after 2018.

e. Whether the Commission should adopt CUB's Rate Protection proposal to limit the cumulative effect of November 1 rate changes in advance of the winter heating season?

f. Whether the Commission should reduce NW Natural's rate base to remove certain LEA investment the Coalition and CUB argue should not have been included under the LEA in effect at that time?[4]

g. Whether the Commission should adopt recommendations by Staff and Coalition related to implementation of the Oregon Low-Income Energy Efficiency ("OLIEE") program?

h. Whether the Commission should increase NW Natural's revenue requirement to include expense the Coalition has identified as lobbying expense?

[4] Staff did not take a position on this issue in testimony and does not do so in brief.

III. Argument.

A. The Commission should reject NW Natural's proposed changes to the RNG AAC.

The Commission adopted Schedule 198, NW Natural's RNG AAC, in NWN's most recent general rate case, UG 435.[5] The purpose of the mechanism is to facilitate recovery of qualified investments in renewable natural gas (RNG) pursuant to Senate Bill 98 (2019) (SB 98), which establishes voluntary acquisition targets for RNG.

Schedule 198 calls for an annual rate adjustment every November 1. To the extent NWN seeks to include new RNG investment in rates, it must make a filing no later than February 1, and in any event must file a revised tariff by August 1 of each year to update all charges for the relevant vintage of previously included RNG investment. In addition to annually updating rates, NWN is allowed to defer the variance between actual costs and revenues and those assumed in rates ("Schedule 198 Deferral") and amortize the variance into rates in the November 1 update, subject to an earnings test deadband set at 50 basis points below and 50 basis points above authorized ROE.

The RNG AAC ultimately adopted by the Commission in UG 435 is not the mechanism proposed by NWN in that docket. In UG 435, the Commission approved modifications proposed by Staff and CUB to eliminate NWN's proposed deferral of costs of new investment between the investment on-line date and the rate effective date of November 1, and NWN's proposal to set the earnings test benchmark at its authorized ROE. [6]

[5] *In the Matter of Northwest Natural Gas Company, dba NW Natural, Request for a General Rate Revision*, UG 435, Order No. 22-388.

[6] Order No. 22-388, supra, p. 82.

In adopting the modifications proposed by Staff and CUB, the Commission noted its concern that an overly generous AAC may skew the Company's analysis of CPP compliance towards RNG projects that receive full risk-free cost recovery.[7] The Commission also explained it is common practice to not allow for a deferral between the in-service date and rate effective date and did not find reason to change this practice for RNG projects given the Commission's other concerns.[8]

In this docket, the Company proposes to eliminate the two Commission-adopted modifications to NWN's RNG AAC so that NWN may defer costs of investment between the in-service date of the RNG project and the rate effective date,[9] have dollar-for-dollar recovery of the Schedule 198 deferred costs up as long as the Company's earnings do not exceed its authorized ROE.[10] Staff opposes both requests.

In support of its request to defer costs of new RNG investments, the Company argues its acquisition of RNG is like electric utilities' investments under Oregon's Renewable Portfolio Standard (RPS) and thus, NWN's cost recovery mechanism should be like the Renewable Automatic Adjustment Clause (RAC) used by electric utilities to recover costs of compliance with the RPS.[11] The Company notes that the RAC allows utilities to defer costs of new resources and asserts its RNG AAC should do the same.

NWN's reliance on the RAC is misplaced. The RAC was established pursuant to a stipulation between Portland General Electric Company, PacifiCorp, Staff, the Oregon Citizens'

[7] Order No. 22-388, supra, p. 81.
[8] Order No. 22-388, supra, p. 83.
[9] NW Natural/1500, Kravitz – Chittum/15.
[10] NW Natural/1500, Kravitz – Chittum/20.
[11] NW Natural/1500, Kravitz – Chittum/15.

Utility Board, and the Industrial Customers of Northwest Utilities.[12] The Commission typically does not treat orders approving stipulations as "precedent" for future Commission decisions.

Second, there are significant differences between the RPS and the CPP. RNG is only one of various tools the Company may use to reduce greenhouse gas emissions. In contrast, the RPS is a percent of load requirement, requiring Oregon-regulated electric utilities to acquire renewable energy. In theory, the Company could meet its entire GHG emissions reductions obligations while having a non-zero load by reducing its natural gas load through strategic electrification, energy efficiency, non-pipes alternatives, or other means. This is not possible for the RPS if an electric utility's load is non-zero. Staff continues to hold the Commission's concerns voiced in Order No. 22-388 that an overly generous RNG AAC mechanism would incentivize the Company to unfairly favor RNG investments in a way that may be detrimental to customers.

Further, the regulatory environment surrounding renewable electricity when the RAC was approved is much different than the current challenges facing RNG. Whereas renewable electricity projects at the time the RAC was approved were widely commercially available and well known, RNG is still expected to both be costly and risky—a point that the Commission noted in the Company's most recent Integrated Resource Plan IRP in LC 79.[13] Staff believes that allowing NWN to defer investment between the in-service and rate-effective dates is even less appropriate now that the Environmental Quality Commission's rules implementing the Climate Protection Plan (CPP) have been declared invalid and a successor program is only in the rulemaking stage. Until a new set of rules to execute Executive Order 20-04 is created, it is

[12] *In the Matter of Public Utility Commission of Oregon Investigation of Automatic Adjustment Clause Pursuant to SB 838*, UM 1330, Order No. 07-752 (December 19, 2007).

[13] *In the Matter of Northwest Natural Gas Company, dba NW Natural 2022 Integrated Resource Plan*, LC 79, Order No. 23-281, page 12 (August 2, 2023).

unclear how effective RNG will be as a compliance resource. Staff worries that allowing the proposed deferral would remove essentially all performance risk from the Company without a quantifiable benefit for customers.

Finally, NWN's argument the deferral of new investment costs or a flexible filing date for new investment is necessary to create a "balanced mechanism" is without merit.[14] NWN testifies that its RNG mechanism is unbalanced because it is required to update Schedule 198 annually to reflect accumulated depreciation but is not allowed to eliminate regulatory lag for new investment.[15] Staff disagrees. The RNG AAC allows NWN to include voluntary RNG investment in rate base within months of service without filing a general rate case. This benefit balances out benefit to customers from annual updates to RNG revenue requirement. NWN is not entitled to avoid all regulatory lag and a mechanism that does not allow it to do so is not unfair.

The Company's argument in favor of modifying the earnings test benchmark is equally unpersuasive. The Company argues the current benchmark provides a disincentive for projects that offtake more RNG than forecasted. The Company testified that a project that produces more RNG than expected will have a lower per-unit cost but a higher overall revenue requirement due to the biogas contract being tied to the owner's production of biogas.[16] The Company asserts that as a result, the Company may be forced to pay higher than forecasted costs for a project that is performing better than expected. The Company argues limiting dollar-for-dollar recovery with an earnings test benchmark 50 basis points below ROE incents underperformance.

[14] NW Natural/4700, Kravitz-Griffiths/5.
[15] NW Natural/4700, Kravitz-Griffiths/4-5.
[16] NW Natural/1500, Kravitz – Chittum/18.

As Staff discussed in testimony, the Company has acknowledged that its two current RNG projects have *lower* overall costs if they produce more natural gas than forecasted.[17] Accordingly, the Company's concern the earnings test could penalize the Company for overly successful RNG projects is unsubstantiated. An earnings benchmark of 50 bps below ROE sends appropriate signals regarding investment in RNG. Staff does not think the current circumstances warrant changes to make RNG investment more attractive.

B. The Commission should eliminate NW Natural's Line Extension Allowance.

1. The Commission modified NWN's LEA in 2022 to address risk of unrecovered investment.

Line extension allowances (LEA) are discounts or offsets provided to new customers for the cost of plant needed to connect the customer to the utility's system. These amounts are included in a Company's revenue requirement and spread to existing customers based on the assumption the LEA can benefit both new customers and existing customers. New customers are benefited by decreasing the cost to join the system, and existing customers are benefitted by the addition of another customer that will be able to contribute to the recovery of the system's existing costs over time. The LEA is also beneficial to the Company as it is allowed to earn a return on the capital investment from all customers and provides a material incentive for new customers to sign up for service.[18]

In Docket No. UG 435, the Commission addressed NWN's Line Extension Allowance (Schedule X) that had been in place since 2012. The Commission concluded NWN's LEA failed to account for future GHG emission reduction costs each new customer will bring to the system,

[17] Staff/3200, Dlouy/12-13 .
[18] CUB/400, Garrett/6-8.

left some rate base unrecovered after 30 years of continuous service, and was based on unrealistic assumptions regarding customer longevity:

> Finally, we find that the current methodology, which assumes customers remain on the system for 30 years with a predictable throughput, is likely too optimistic of an assumption given the changes to the industry that are identified by the parties. We share CUB's concerns around the 30-year timeframe of the current LEA calculation, and about that fact that other components within the calculation assume an even longer life for associated plant.
>
> In essence the current methodology would assume a "business as usual" approach well into the future, while the record in these proceedings shows the future is more likely to be an extremely dynamic and different environment for natural gas distribution, including evolving customer preferences and state and local mandates regarding restrictions on service. Most of these changes point toward a trend where at least some existing and future customers are likely to respond to the changes by modifying equipment or taking other purposeful measures to change their fuel consumption. Or in some cases, their continued usage may be directly impacted by a policy initiative. We find the company's arguments to the contrary not persuasive, given the robust record in these proceedings about the policy changes taking place in the natural gas distribution business. These changes, including the CPP and activities of municipalities or other jurisdictions in potentially enacting limitations on natural gas, point to a reasonable possibility that the company will encounter a trend of decreasing gas usage, potentially driven by economic signals toward fuel switching.[19]

Based on the conclusions above, the Commission ordered the Company to abandon its previous LEA calculation and use a Revenue /Margin Multiplier to determine the LEA for new residential customers.[20] Under this approach, the amount granted for a line extension equals a multiple of the annual expected non-fuel base distribution margin revenues.[21] The Commission directed the Company to calculate residential LEAs using a 5x margin approach with a cap of $2300 for the period starting November 1, 2022, which would be lowered to a 4x margin on November 1, 2023, and to a 3x margin on November 1, 2024.[22] The Commission's decision

[19] Order No. 22-388, supra.
[20] NW Natural/1900, Therrien/8.
[21] NW Natural/1900, Therrien/6.
[22] NW Natural/1900, Therrien/8.

resulted in a downward adjustment to residential LEAs in 2022 from the previous level of $2,875.

Finally, the Commission specified that if the Company sought to modify its LEA from the approach described above, the Commission expected the Company's best reasonable estimates of present and future CPP compliance costs, how each new customer addition changes the costs of CPP compliance for other customers, and how the proposed LEA incorporates and recognizes the costs of CPP compliance; supported assumptions about the expected time new customers will remain on the system; a demonstration of the expected year-by-year economic impact on existing customers from the addition of new customers under the proposed LEA, such that the "breakeven" year is shown, along with the costs and benefits expected in other years; and a demonstration of when rate-based investments for customer additions covered by the LEA are depreciated and removed.[23]

2. NW Natural has not supported its proposed modifications to its LEA calculation.

In this case, the Company seeks to modify the previously ordered LEA calculation, asking the Commission to approve a four-tiered residential allowance that is lowest for customers predicted to use the most gas and increases as expected usage decreases.[24] NWN's proposal has gone through several iterations, starting with a proposal for LEAs ranging from $1,800 for the highest usage tier to $3,600 for the lowest usage, and changing in value in supplemental testimony and then reply testimony. In its surrebuttal testimony, NWN proposes the following,

[23] Order No. 22-388.
[24] NW Natural/2000, Kravitz – Therrien/23.

with revisions based on some modifications to its modeling inputs and the stipulated proposed revenue requirement increase.[25]

NW Natural Revised LEA Proposal (Surrebuttal Testimony)				
Usage Tiers (therms)	0-250	251-450	451-650	651+
LEA	$2,950	$2,300	$1,650	$500

NW Natural supports its proposed LEAs with analysis based on Discounted Cash Flow (DCF) modeling that NW Natural asserts shows no stranded LEA investment assuming the new customer remains on the system for 25 Years.

Staff opposes the Company's proposed revisions to its LEA. The Company's modeling, even as revised, relies on unrealistic assumptions about future costs and revenues and therefore fails to support NWN's proposed changes. Further, putting aside Staff's critique of NWN's analysis, the risk associated with a continued LEA is too significant to overlook. A likely outcome of decarbonization is a decrease in natural gas use. Even if natural gas use falls across the Company's system, line extension investments and other fixed costs will still be in base rates and contribute to revenue requirement.[26] And, even if these assets are not technically stranded assets, it is possible that customers induced to join the natural gas system by favorable LEAs will be on the hook to pay for these assets in the future even if their usage declines.

As these costs accumulate and compliance costs with a possible successor program to the CPP rise, one would expect that customers who have the means to switch away from natural gas will choose to do so for economic reasons or other personal preferences. In effect, this may

[25] NWN/4400, Kravitz/7.

result in only customers with the least ability to leave the natural gas system stuck paying for system costs that they may not have had a part in.

Rather than modifying NWN's LEA, Staff recommends the Commission eliminate it completely starting with the rate effective date of this general rate case, November 1, 2024. Alternatively, Staff recommends the Commission build on its decision in UG 435 and continue phasing out residential line extensions with a residential LEAs equal to 2x margin beginning on November 1, 2025, then 1x margin on November 1, 2026, and $0 starting November 1, 2027.

a. NWN's DCF Analysis does not support its proposed LEAs.

As noted above, the Commission specified that if NW Natural proposed to modify the LEA methodology ordered in UG 435, NWN must base its proposal on reasonable assumptions regarding present and future CPP compliance costs and how addition of new customers impacts recovery of those costs, the expected longevity of new customers, and when rate-based investments for customer additions are fully depreciated; and a demonstration of the expected year-by-year economic impact on existing customers from the addition of new customers under the proposed LEA, such that the "breakeven" year (i.e., the year when the customer provides a net benefit to the system) is shown.

In response to the Commission's directive the Company employed a DCF model to calculate its proposed LEAs. To capture the elements ordered by the Commission in UG 435, the Company assumed:

- New customers will pay back the LEA over an uninterrupted 25-year term rather than the 30-year term rejected by the Commission in UG 435.[27]

[27] NW Natural/1900, Therrien/19.

- Incremental expenses related to the CPP based on costs to comply with Washington's CCA in the early years and an estimated marginal cost for RNG in the later years;
- A credit to account for new customers' contribution to CPP compliance costs;
- A credit for new customers' contribution to new, non-growth capital and the decline in rates that occurs due to asset depreciation; and
- Revenue from the Company's proposed increases to the fixed charge, including the New Premises Customer Charge, that would go into effect on November 1, 2024, if approved.[28]

As explained in the testimony of Staff, the Coalition, and CUB, the modeling assumptions used by the Company to support its proposed LEAs are unreasonable, which negates the probative value of the analysis. Staff discusses the assumptions used by the Company and its own analysis with substituted assumptions below.

First, the Company's use of a 25-year payback period for the LEA is unreasonably long in the current environment and creates too great of risk of stranded assets. For the purpose of testing the Company's analysis, Staff assumed a 15-year payback period, which is a conservative time period and likely longer than what should be used when calculating the actual LEA.

Second, NWN's modeling relied on unreasonably low estimates of compliance costs for GHG emission reduction requirements. For the earlier years, the Company assumed the dollar value of the decarbonization obligation falls from the Climate Protection Plan CCA price of $123 per metric ton of CO2 to only $63 per metric ton of CO2.[29] The value selected by NW Natural was based on the price of a compliance instrument for the Washington Climate Commitment Act, which was the most expensive carbon credit that the Company was aware of in the US as of

[28] NW Natural/1900, Therrien/19.
[29] NW Natural/2000, Kravitz – Therrien/18.

the publication of the Company's supplemental testimony filed on February 23, 2024. For the later years, the Company's NPV model assumed the CPP compliance cost is based on RNG acquisition being the marginal resource and initially modeled this as a fixed $22 per MMBtu, but in subsequent testimony modified this value to $25 per MMBtu.

To limit potential areas of dispute, Staff did not alter the compliance cost NWN used in the earlier years for purposes of Staff's own analysis. However, Staff did modify the compliance cost for the later years. The low cost NWN assumed for the later years is similar to costs projected by the Company in its most recent IRP (LC 79), with which Staff took issue. The Commission raised multiple concerns about both the Company's RNG acquisition strategy and its modeling of RNG in LC 79,[30] and Staff expressed concerns in comments throughout the docket that the Company's modeling of RNG costs did not align with other RNG cost forecasts.[31]

For purposes of its own DCF analysis, Staff assumed a compliance cost of $30/mmbtu in place of NWN's assumed $22/mmbtu and $25/mmbtu. Staff arrived at this value by considering the costs presented in Table 3 of Staff's Final Comments in LC 79.[32] These included historic EPA D3 Cost ranges from a minimum of $22.46/MMBtu to a maximum of $40.95/MMBtu and S&P estimates of RNG that range from $20/MMBtu to $35/MMBtu.

Third, NWN's DCF modeling uses an overly optimistic CPP revenue multiplier for revenue new customers are expected to contribute to future CPP reduction requirement, assuming that a new customer contributes more revenue to the Company's CPP compliance as the Company's CPP emissions cap decreases. By doing so, the Company inherently assumes

[30] Order No 23-281, p. 12.
[31] Staff/905, Dlouhy/8.
[32] Id.

that the GHG emissions compliance obligations will be passed directly back to the new customer without any consideration of rate spread, rate design, or shareholder burden of decarbonization costs. Staff believes NWN's CPP revenues line item was a gross overestimation of revenues brought in by a new residential customer and resulted in an optimal LEA estimate higher than what would be obtained if a more realistic assumption was used. Notwithstanding, Staff did not alter the Company's assumption regarding the CPP revenue multiplier for its own analysis, again to limit potential points of contention.

Fourth, the Company assumed an exceptionally high amount of new non-growth capital expenditures – an *annual* incremental increase of $187 to $205 million. Increases in non-growth-related capital investment increase the value of new customers to the system. However, as explained in Staff and Coalition testimony, the Company's assumptions regarding the future need for non-growth-related capital spending are unsupported[33] and in any event, appear to include some growth-related investment.

Staff's DCF modeling relied on a more reasonable assumption regarding non-growth-related spending that removed incorrectly included growth-related investment and a less optimistic forecast of non-growth-related investment. Reducing the projected amounts of non-growth-related capital investment reduced the amount of plant that a new customer helps pay for, which in effect reduced the appropriate LEA produced by Staff's modeling.

Fifth, the Company's model assumed that new residences are permanently occupied and paying rates. However, Staff assumed for purposes of its modeling that there would be periods when residences are unoccupied, i.e., when occupants move, and not contributing to covering the Company's revenue requirement.

[33] Coaliton/100, Cebulko/34; Coalition/400, Cebulko/15; Staff/900, Dlouhy.

Finally, the Company's calculation of LEAs is dependent on forecasted revenue from NWN's proposed New Premises Customer Charge. This new charge is discriminatory, unsupported by the record, and should be rejected. For purposes of its own DCF analysis, Staff lowered the basic charge for a new premises customers in new construction to the amounts proposed by NWN in this rate case for existing customers, which are $10 and $8.

The table below contains a summary of the calculated LEAs for each of NWN's proposed usage tiers using Staff's modifications to the Company's LEA DCF model. Staff's analysis using the NWN's DCF, but with more reasonable values for some but not all of the inputs, shows a line extension *disallowance* is justified at every usage tier. If the reduction in revenue requirement associated with the parties' stipulations were incorporated into Staff's analysis, or more reasonable estimates substituted for the Company inputs that Staff left untouched, Staff's estimates would likely be more negative than those presented below.

Model Results at Proposed Consumption Levels (Therms)				
UPC (Therms)	250	450	650	1,000
LEA	-$144	-$1,284	-$2,424	-$4,419
Times Margin	-0.4	-2.4	-3.4	-4.3

Based on its analysis, Staff recommends the Commission take one of two actions. Staff's primary recommendation is to discontinue the Company's residential LEAs. Staff believes this to be in the best interest of customers at the time given the regulatory uncertainty surrounding the successor program to the CPP and the results of Staff's model indicating that a line extension disallowance would be in customers' best interest even with generous assumptions.

As an alternative and more conservative recommendation, Staff proposes the Commission maintain its current policy that identified a phase down to the residential LEAs. Such a phase down could be to a level equivalent to the 2x margin beginning on November 1, 2025, and then

1x margin on November 1, 2026, and then entirely eliminate residential LEAs by November 1, 2027.

C. The Commission should adopt Staff proposed changes to NW Natural's decoupling mechanism.

NWN has had a Distribution Margin Normalization (DMN) mechanism ("decoupling mechanism) since 2002. In 2002, the Commission authorized the decoupling mechanism to facilitate NWN's recovery of fixed costs when customers on average do not consume as much gas, or consume more, than assumed in the utility's rate case load forecast. The decoupling mechanism tracks a portion of the under- or over-collection of revenues in a deferred account and allows NWN to recover or refund the variance by annually adjusting the per-therm rate the Company charges for gas.

In Docket UG 435, Staff noted that further refinement to the decoupling mechanism may be appropriate to account for lower average usage levels by customers in modern versus older homes. Staff observed that assuming all new customers will use on average the same amount of gas as existing customers could lead to an overestimation of customer baseline usage and artificially inflate the amount of lost revenue that is deferred and collected under the mechanism. To address Staff's issue, NWN and parties to UG 435 stipulated that NW Natural would provide in its next rate case filing information regarding use per customer and the number of new customers forecasted.[34]

The information provided in this docket shows that customers joining NWN's system after 2018, on average, use less gas than customers that joined prior to 2018, on average. Based on this information, NWN proposes to bifurcate the residential decoupling calculation between

[34] Order No. 22-388, p. 24.

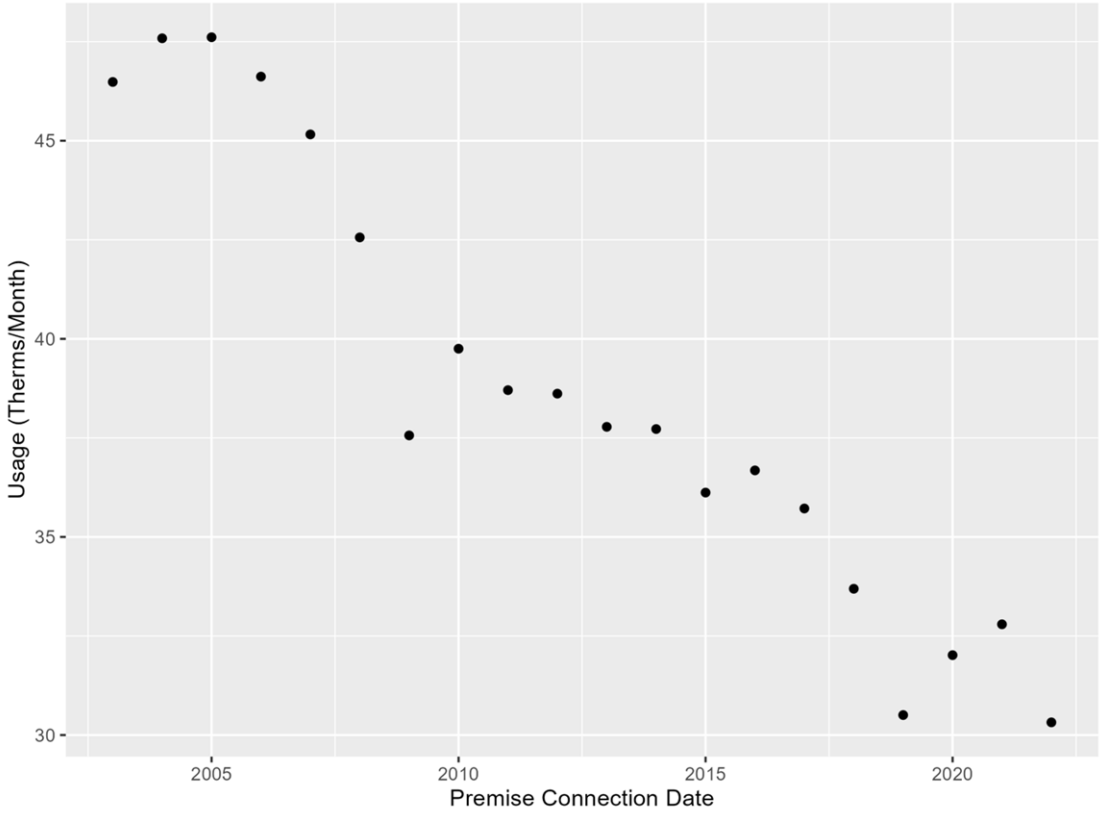
established customers and new customers that join the system after each rate case, starting with customers that join after the effective date of this rate case. NWN also proposes the bifurcation of baseline usage should account for each customer set's (new vs. existing) usage during normalized and actual heating days.

NWN has proposed a modification to the decoupling mechanism to address this issue and Staff agrees with NWN that an adjustment is appropriate. However, Staff disagrees with NW Natural's proposal to use November 1, 2024, as the bifurcation date and its proposal to continuously update this bifurcation with each rate case. Instead, Staff believes January 1, 2018, is a more appropriate bifurcation date on a more permanent basis and that baseline usage for new customers connecting to NWN's system prior to that date should be calculated separately from the usage for customers connecting to NWN's system after that date.

Staff proposes 2018 as the bifurcation year primarily because the downward usage trend of the past 20 years seems to have stabilized around 2018 and houses built during and after 2018 are subject to the updated residential building codes set in 2017. Together, these facts make 2018 a logical year to demarcate between existing and new customers.[35] Staff's proposed demarcation is supported by the average monthly usage for premises connected from 2003-2022, which shows usage of customers that connected to the system between 2018-2022 has remained fairly constant.[36]

[35] Staff/1900, Stevens/20-24.
[36] Figure 13 was created using data obtained in Staff DR 390.

Average Monthly Usage by Premises Connection Year



Staff's recommendation to make a "permanent" distinction between customers joining the system before and after January 1, 2018, is based largely on Staff's observations related to customer attrition. NWN's decoupling mechanism accounts for differences both in usage per customer and customer count compared to the load forecast. If the baseline for "existing" customers includes all customers connected at the time of the rate case, then the system-wide baseline usage and heating coefficient will be the weighted averages of older and newer customers. However, customers who leave the system are likely not customers who have only connected to the system recently. As such, the usage distribution of customers leaving the system is likely shifted to right of the usage distribution for the entire system. This would then lead to a mechanism that compares customers remaining on the

system to a baseline usage that is skewed upward. Having a more permanent bifurcation in the decoupling mechanism between "existing" and "new" customers would help mitigate the impact of this phenomenon. However, this does not mean that the usage baselines for customers joining before January 1, 2018, and those joining after must remain constant for all time. Instead, the baseline could be moved at some future time if data shows a different demarcation is appropriate.

Further, Staff supports the Company's proposal to separately calculate heating coefficients separately for "new" and "existing" customers (those joining after January 1, 2018, and those joining before). Staff recognizes this recommendation runs counter to Staff's proposal in UG 435.[37] However upon further review, Staff has altered its recommendation. This change is meant to reflect the fact that new customers to the system will likely both have lower baseline usage and less reaction to weather fluctuations.

In surrebuttal testimony, the Company complains that Staff's modification to the bifurcation date for purposes of establishing the baseline usage for existing versus new customers results in a $3 million reduction to revenue requirement. The Company's meaning is unclear as the calculation of the usage baselines should not impact the revenue requirement increase expected to take place November 1, for either this general rate case or the Purchased Gas Adjustment (PGA). Staff has reviewed the Company's workpapers submitted with its surrebuttal testimony and has not been able to identify the source of any revenue requirement discrepancy. Mathematically speaking, Staff's proposal should not affect the Company's revenue requirement in this rate case.

[37] Staff/1300, Scala/27.

If the Company means Staff's proposed change would reduce the Company's revenue requirement by $3 million in a future rate case because the Company would defer a smaller differential between costs assumed in rates and actual costs, that is the point of Staff's adjustment. Staff is concerned the Company's use of a single value for baseline customer usage artificially inflates the estimate of revenue the Company will collect under rates, and therefore, artificially inflates the amount of actual costs deferred under the decoupling mechanism. Modifying the decoupling mechanism to more accurately capture the expected average usage of new customers should result in a smaller deferral and consequently, a smaller increase to NWN's rates in a future PGA.

Finally, Staff anticipates the Company will continue to argue Staff's recommendations related to the decoupling mechanism and the New Premises Customer Charge are inconsistent. The Company is wrong, and its arguments reflect the Company's refusal to recognize the significant and likely negative financial impact its proposed increase to the basic charge would have on customers.

As Coalition witness Mr. Cebulko testified, the near-term impacts to the decoupling mechanism from distinguishing between new and existing customers are *de minimis*. For the Test Year, NWN forecasts New Premises Single Family and Multi Family Customer revenue of $2.3 million, and existing Single-Family and Multi-Family revenue to of $471.4 million. Mr. Cebulko explains that this translates to a forecast of New Premises customer revenue that is 0.488 percent of total residential revenue. Staff's proposed change to the decoupling mechanism will result in a modest incremental change to the amount lost revenue deferred and recovered by NWN. The impact to new and existing customers from the hanged deferral amount is minimal as the modest change is spread to all residential customers.

In contrast, the Company's proposed New Premises Customer Charge is not a modest change and does not have a minimal impact. The increased charge is limited to a group of customers with consumption that is similar to approximately a third of NWN's other residential customers that are not affected by the charge. NWN has provided no basis for the distinction between new customers connecting to the system after November 1 and before, other than the fact November 1 is the rate effective date of the current rate case.

D. The Commission should reject NWN's proposed New Premises Customer Charge.

NWN proposes to increase the single-family and multi-family fixed charge for customers moving into "new premises" ("New Premises Customer Charge") to $24.50 and $22.50, respectively.[38] For purposes of this proposal new premises customers are those with new connections to NWN's system after November 1, 2024. For other single-family and multi-family residential customers, the proposed fixed charges are $10 and $8, respectively. NWN argues the New Premises Customer Charges are appropriate because on average, new residential customers use approximately 210 therms less than existing residential customer base (660 therms per year). NWN asserts the New Premises Customer Charges will ensure that new customers as a group contribute their appropriate share to cost of service.

Staff, CUB, and the Coalition oppose NWN's New Premises Customer Charge, each voicing similar concerns. CUB witness John Garrett observes that under NWN's proposal, a new premises customer would expect to pay approximately 24.3 to 37 percent more than an existing customer for using the same amount of gas, which over the course of a year, would be equivalent to adding two winter-month bills relative to existing customers.[39] Mr. Garrett explains that

[38] NW Natural/4400, Kravitz/10.
[39] CUB/200, Garrett/8.

saddling customers that joining NWN's system after November 1, 2024, with this increased fixed charge is unfair because these customers can be expected to have usage higher than nearly a third of customers (approximately 180,000) that joined the system prior to November 1, 2024. Mr. Garrett testifies that CUB is concerned that charging new premises customers 37 percent more than approximately 180,000 customers with the same or lower usage is discriminatory "and creates intra-class equity concerns.[40]

The Coalition brings up similar concerns about a higher charge hurting lower income and energy burdened customers.[41] The Coalition also asserts that the New Premises Customer Charge proposal rejects the regulatory tenet of gradualism, decreases incentives for energy efficiency, disproportionally affects lower-income households, is duplicative with the Company's decoupling proposal, and sends conflicting signals to homebuilders and renters who purchase energy efficient appliances.[42]

Staff agrees with the concerns voiced by CUB and the Coalition that the proposed charges are arbitrary and discriminatory and finds the Company's arguments in support are unpersuasive. First, NWN's assertion that new premises customers are generally higher income and would not be harmed by the significant increase to the fixed charge fails to acknowledge the significance of the rate change or the potential diversity of customers joining the Company's system after November 1, 2024. The New Premises Customer Charge would result in an increase in bills of 24.3 percent to 37.0 percent more annually, as compared to existing customers with the same usage.[43] This significant increase in cost will undoubtedly impose a significant burden on some new premises customers. Furthermore, NWN fails to address the

[40] Id.
[41] Coalition/100,Cebulko/53.
[42] Coalition/100, Cebulko/48-49.
[43] NW Natural/3900, Wyman/47-48.

very significant concern that the New Premises Customer Charges disincentivize energy efficiency.

As pointed out in the opening testimony of Staff, CUB, and the Coalition, one effect of the New Premises Customer Charges is to juice the Company's Line Extension Allowance (LEA) Discounted Cashflow (DCF) model.[44,45,46] The *only* way that Staff found a non-negative or trivially small LEA could be justified by the Company's DCF model is through the inclusion of an exceptionally high fixed charge for newly added customers.[47] As previously stated, Staff believes that this is discriminatory and deceptive to these customers.

The LEA flows to builders, not necessarily to the customer. While some or many homeowners may see a more direct benefit from the LEA, landlords or apartment owners may be able to pocket the generous LEA without passing any of the savings onto their tenants. These tenants would then be faced with an exceptionally high and discriminatory customer charge while potentially not receiving any of the benefit from the LEA. Staff has testified that this bait-and-switch may hide the true costs of the LEA in the New Premises Customer Charge. However, in the case of a renter, the New Premises Customer Charge would extract benefits from renters and shift them to landlords or builders. Staff finds this to be an entirely inequitable transfer of costs that raises serious cost causation and equity concerns.

Further, the Company's proposed change would have far-reaching impacts on the balance of fixed vs. volumetric cost recovery going forward. According to the Company's estimates of average bills at their proposed rates, roughly 10 percent of revenues would be recovered through the fixed charge for existing premises customers. For new premises customers, this amount

[44] Staff/900, Dlouhy/44.
[45] CUB/900, Garrett/104.
[46] Coalition/100, Culko/24.
[47] Staff/900, Dlouhy/44.

would be nearly 40 percent. It is impossible to ignore the dramatic change in cost recovery and business risk faced by the Company due to this change.

Staff acknowledges that in the immediate future the number of customers living in existing premises would vastly outweigh the number of new premises customers, leading to a relatively small impact on the Company's overall cost recovery and risk profile. However, the City of Portland, for example, has been in a declared housing state of emergency since 2015. This has led to zoning and permitting reform allowing for more dense infill development.[48] As infill development increases in NWN's service territory, more customers will be subject to the New Premises Customer Charge, further altering NWN's cost recovery profile. While the Company claims this is not the reasoning for their proposal, this aspect of the New Premises Customer Charge cannot be ignored.

E. The Commission should adopt CUB's Rate Protection Proposal.

CUB recommends the Commission adopt a rate impact mitigation mechanism that would cap any November 1 increase to the residential class at the lower of 10 percent, or 7 percent plus the Consumer Price Index. Staff supports CUB's proposal. Michelle Scala, the Commission Energy Justice Program Manager testified, "it is a known fact that environmental justice communities are disproportionately burdened by the energy system in general. This includes health disparities associated with pollution proximity, energy insecurity, energy poverty, and energy democracy. What this means is that as certain components of the system change, such as costs recovered in rates, disproportionate burdens are worsened as the impacts of the changes are augmented for these communities."[49]

[48] See https://www.opb.org/article/2022/03/30/portland-extends-housing-state-of-emergency-for-three-years/.
[49] Staff/300, Scala/22.

Although there are programs in place to provide financial assistance to energy burdened customers, these programs are not used by all eligible customers. Staff agrees with CUB that it is appropriate for the Commission to protect customers by capping any rate increase for NWN customers going into the winter heating season at a reasonable level.

F. The Commission should reject NWN's request to recover costs the Coalition has identified as lobbying expense.

1. Allowing NWN to recover additional expense for Government Affairs is not warranted.

As discussed in the Joint Testimony in Support of the Second Stipulation executed by NW Natural, Staff, CUB, the Coalition, and AWEC, agreed to separately address NWN's recovery of Government Affairs expense challenged by the Coalition. The parties agreed the $95 million revenue requirement increase does not include $1,725,922 of Government Affairs costs included in NWN's original revenue requirement request and that NWN's recovery of this amount must be separately decided by the Commission.

Staff urges the Commission to reject NWN's request for this additional revenue requirement increase. The agreed-to revenue requirement increase of $95 million is within the range of reasonableness required by Commission precedent, state statute, and the federal and state constitutions and increasing this agreed-to rate increase to include additional expense is not warranted in the current economic environment. Furthermore, Staff supports the Coalition's extensive analysis showing why exclusion of Government Affairs costs is appropriate as a policy matter.

2. The Commission should adopt Staff's recommendation related to recording time spent on lobbying activities.

In testimony, Staff proposed that NW Natural be required to record time spent lobbying before a judicial, executive, or administrative body (e.g., Department of Environmental Quality, Department of Energy, Treasury, school boards, housing authorities, sewer and water districts, and zoning board) whether elected or appointed, to ensure such costs are charged "below the line" rather than to ratepayers. As the Commission concluded in Docket No. UG 435, "communications intended purely to ensure that public officials are receiving routine information about the company and the gas system do not qualify as lobbying expenses," and thus would not be captured by Staff's recommendation. Further, as clarified by Staff in discovery, the proposed requirement to record time spent lobbying does not apply to regulatory activities.

NWN objects to the proposed requirement, arguing it is too broad and vague. Staff believes NW Natural employees are sophisticated enough to identify when communications to the bodies listed above are lobbying as opposed to merely informational or part of regulatory proceedings and advocacy, and that the need for transparency around lobbying expense justifies the inclusion recommended by Staff.

G. Staff's recommendation regarding NW Natural's outreach for the OLIEE program should be adopted.

In testimony, Staff acknowledged NW Natural's commitment to expand spending on the Oregon Low-Income Energy Efficiency (OLIEE) program and recent removal of project caps for projects to meet its qualifications. However, Staff encouraged the Company to continue to increase enrollment numbers in the OLIEE program with additional targeted design and outreach, to close the gap Staff observed between NW Natural's OLIEE projections and actual completions.[50] In rebuttal testimony, Staff reiterated its recommendation the Company continue to provide robust and adequate energy efficiency offerings through the OILEE program and

[50] Staff/3500, Lockwood/26-29.

urged the Company to increase enrollment numbers with additional targeted design and outreach to close the gap Staff observed between NW Natural's OLIEE projections and actual completions. In response, the Company notes that it appreciates Staff's recommendations and shares Staff's goals, but points out that "customer engagement, project estimates, and project completions within the OLIEE program are largely determined by the CAP Agencies . . . [a]nd since CAP Agencies set their own annual projections, the Company does not have full control over how well projections align with actual completions."[51]

Again, Staff appreciates NW Natural's commitment to expand spending on the OLIEE program and recognizes NW Natural does not have complete control over the CAP Agencies that administer the OLIEE program. However, the point of Staff's recommendation, which Staff believes NW Natural understands and agrees with, is that the utility must be proactive, both with direct outreach to customers and CAP Agencies, to help ensure successful and robust implementation of the OLIEE program. The Company testifies that it is optimistic that project completions will continue to increase under the OLIEE program and Staff hopes and expects that improved program execution is facilitated by the Company's direct and targeted involvement.

Conclusion

For the reasons stated above, Staff recommends the Commission reject NW Natural's proposed New Premises Customer Charges, modifications to the LEA, RNG AAC, and decoupling mechanism, and its request to increase revenue requirement for additional Government Affairs costs. Staff also recommends the Commission eliminate NW Natural's LEA, adopt Staff's proposed modifications to NW Natural's decoupling mechanism and the Company's time exception reporting requirements related to lobbying activities, Staff's

[51] NW Natural/4500, Tanaka/4.

recommendation for concentrated outreach related to implementation of the OLIEE program, and CUB's proposal for rate impact mitigation for residential customers.

DATED this 15th day of August 2024.

Respectfully submitted,

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