

**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.)
_____)

**LIBERTY REPORT OPENING TESTIMONY
OF EDWARD A. FINKLEA
ON BEHALF OF
ALLIANCE OF WESTERN ENERGY CONSUMERS**

May 4, 2018

1 **Q. PLEASE STATE YOUR NAME AND BUSINESS ADDRESS.**

2 A. Edward A. Finklea. My business address is 545 Grandview Drive, Ashland, Oregon
3 97520. I am the Director of Natural Gas for the Alliance of Western Energy Consumers.

4 **Q. HAVE YOU PREVIOUSLY FILED TESTIMONY IN THIS PROCEEDING?**

5 A. Yes. I previously filed Opening Testimony marked as AWEC/300. My qualifications were
6 provided in Exhibit AWEC/301 as part of that earlier testimony.

7 **Q. ON WHOSE BEHALF ARE YOU TESTIFYING IN THIS PROCEEDING?**

8 A. I am testifying on behalf of the Alliance of Western Energy Consumers (“AWEC”).^{1/}
9 AWEC members include diverse industrial and commercial interests that purchase sales
10 and transportation services from Northwest Natural Gas Company, dba NW Natural (“NW
11 Natural” or the “Company”).

12 **Q. WHAT IS THE PURPOSE OF YOUR TESTIMONY?**

13 A. The purpose of my testimony is to:

14 (a) discuss Order No. 15-066, issued in Docket UM 1654, where the Public Utility
15 Commission of Oregon (“Commission”) directed the parties to form a steering committee
16 and to hire an independent consultant to conduct a cost study for the revenue sharing
17 associated with NW Natural’s Mist Storage Services (“Storage Services”) and resource
18 optimization activities (“Optimization Activities”);

19 (b) discuss the cost study and report from The Liberty Consulting Group (“Liberty”), the
20 independent consultant chosen by the steering committee, which reviewed and made

¹ On March 31, 2018, Northwest Industrial Gas Users (“NWIGU”) merged into the Industrial Customers of Northwest Utilities (“ICNU”), and on April 1, 2018 ICNU changed its name to Alliance of Western Energy Consumers (“AWEC”). The advocacy and work previously performed by NWIGU now occurs as part of AWEC.

1 recommendations on the revenue sharing percentages of the Storage Services and
2 Optimization Activities; and

3 (c) respond to the Supplemental Direct Testimony on Randolph S. Friedman where he
4 discusses NW Natural's recommendation for the Storage Services and Optimization
5 Activities.

6 **Q. WHY WAS THERE AN INVESTIGATION INTO NW NATURAL'S INTERSTATE**
7 **STORAGE AND OPTIMIZATION REVENUE SHARING?**

8 A. Questions about NW Natural's revenue sharing for its Storage Services and Optimization
9 Activities began in Docket UG 221, NW Natural's last general rate case proceeding. In
10 that docket, the parties agreed to open a separate proceeding to investigate the sharing
11 arrangements described in NW Natural's Schedules 185 and 186. Based on that
12 agreement, the Commission initiated Docket UM 1654, opening an investigation to
13 assess whether the sharing arrangement for Storage Services and Optimization Activities
14 should be revised.

15 **Q. DID THE COMMISSOIN REVISE THE REVENUE SHARING AS PART OF**
16 **THAT SEPARATE PROCEEDING?**

17 A. No. After multiple hearings and briefings in that docket, the Commission maintained the
18 current revenue sharing. That arrangement was intended to be a temporary maintenance
19 of the status quo to allow further analysis by a third party to better inform the issues in
20 that proceeding. This was an approach that AWEC – at the time acting as the Northwest
21 Industrial Gas Users (“NWIGU”) – supported. NWIGU's Post Hearing Brief in UM
22 1654 expressly urged the Commission to require the third party analysis as a sort of audit,
23 “to identify the various components of NW Natural's system that drive the costs and

1 revenues associated with Interstate Storage Services, and to definitively identify all
2 shared facilities and resources” that “would in turn inform whether the split in revenue
3 between ratepayers and shareholders is equitable.”²/

4 **Q. WHY DID AWEC TAKE THAT POSITION IN THE EARLIER DOCKET?**

5 A. Based on a review of the history of the sharing mechanisms, AWEC determined that
6 there was no technical support for those mechanisms, which were developed before the
7 full value of NW Natural’s services were known. In light of the amount of time that had
8 passed since the sharing started and the level of information that it now known, AWEC
9 believed that it would be imprudent to continue the sharing mechanisms without a more
10 formal analysis.

11 **Q. WHAT DID THE COMMISSION ORDER AT THE CONCLUSION OF THE**
12 **PROCEEDING?**

13 A. In Order 15-066, the Commission ordered NW Natural and the other parties to form a
14 steering committee to interview and to hire an independent consultant to perform a cost
15 study for the Storage Services and Optimization Activities.

16 **Q. DID THE PARTIES SELECT AN INDEPENDENT CONSULTANT TO**
17 **PERFORM A COST STUDY?**

18 A. Yes. After reviewing multiple proposals, the steering committee selected Liberty to
19 perform the analysis.

20 **Q. WERE THE PARTIES INVOLVED WITH THE LIBERTY ANALYSIS?**

21 A. Yes. Liberty allowed the stakeholders to participate in the process, provide comments on
22 the scope of the review, and review and provide comments on the final report and

² Docket UM 1654, NWIGU’s Post Hearing Brief at pp 4-5.

1 analysis.

2 **Q. WHAT DID LIBERTY RECOMMEND IN ITS FINAL ANALYSIS?**

3 A. Liberty concluded that the current revenue sharing for Storage Services is reasonable but
4 that the revenue sharing for Optimization Activities should be more favorable to
5 customers.

6 **Q. WHAT IS THE CURRENT REVENUE SHARING FOR NW NATURAL'S
7 STORAGE SERVICES?**

8 A. The current revenue sharing for NW Natural's Storage Services is set at 20 percent for
9 customers and 80 percent for NW Natural.

10 **Q. WHAT IS THE CURRENT REVENUE SHARING FOR NW NATURAL'S
11 OPTIMIZATION ACTIVITIES?**

12 A. The revenue sharing for Optimization Activities is set at 67 percent for customers and 33
13 percent for NW Natural for resources included in customer rates, and 20 percent for
14 customers and 80 percent for customers on resources not included in customer rates.

15 **Q. WHAT DOES NW NATURAL RECOMMEND FOR THE STORAGE SERVICES
16 AND OPTIMIZATION ACTIVITIES?**

17 A. According the testimony of NW Witness Mr. Friedman, NW Natural believes that the
18 Commission should maintain the existing revenue sharing arrangements for both Storage
19 Services and Optimization Activities.

20 **Q. DO YOU AGREE WITH NW NATURAL REGARDING THE APPROPRIATE
21 LEVEL OF REVENUE SHARING FOR STORAGE SERVICES?**

22 A. Yes, I agree with NW Natural that the Commission should maintain the current revenue
23 sharing for the Storage Services. The Liberty Report convincingly shows that the flow of
24 benefits from Storage Services has been relatively balanced between customers and the

1 Company under the existing sharing mechanisms. Moreover, Liberty's analysis shows
2 that changing the sharing percentages does not result in a meaningful shift of any benefits
3 in light of the dollar amounts that are at issue. As a result, it appears that the current
4 revenue sharing for Storage Services is the best option.

5 **Q. DO YOU AGREE WITH NW NATURAL ABOUT THE APPROPRIATE LEVEL**
6 **OF REVENUE SHARING FOR THE OPTIMIZATION ACTIVITIES?**

7 A. No, I do not agree with NW Natural's recommendation for the revenue sharing associated
8 with Optimization Activities. NW Natural disagrees with Liberty's analysis and argues
9 that the current revenue sharing for Optimization Activities be maintained.

10 **Q. WHAT IS YOUR RECOMMENDATION FOR THE REVENUE SHARING FOR**
11 **OPTIMIZATION ACTIVITIES?**

12 A. I recommend that the revenue sharing for Optimization Activities be increased in favor of
13 customers. Specifically, I am recommending that the current 67/33 split for resources in
14 customer rates be changed to an 85/15 split so that customers receive 85 percent of those
15 revenues. Further, I am recommending that the current 20/80 split for resources not in
16 customer rates be flipped to an 80/20 split so that customers receive 80 percent of those
17 revenues. I believe this change is supported by the analysis and recommendation
18 contained in the Liberty report.

19 **Q. WHAT DID LIBERTY CONCLUDE ABOUT THE OPTIMIZATION ACTIVITIES**
20 **PERFORMED BY NW NATURAL?**

21 A. The Liberty Report concluded that customers should receive more of the revenue for a
22 couple of different reasons. For one, Liberty concluded that Optimization Activities are
23 not a risky enterprise for NW Natural. Liberty also concluded that these activities are not

1 particularly complex for NW Natural and that the Company's efforts are in line with
2 normal utility practices.

3 **Q. WHY IS THIS NOT A RISKY OR COMPLEX OPERATION FOR NW NATURAL?**

4 A. As the testimony of Mr. Friedman confirms, the Optimization Activities capture extra value
5 from the Mist storage facilities without putting the actual facilities or gas at risk. For
6 example, in the "backdraft" example Mr. Friedman provides, gas is traded only after peak
7 winter conditions have passed and it is certain that the gas will not be needed for core
8 customers. While the gas never leaves the facility, it is essentially traded to take advantage
9 of price spreads that occur over time. If for some reason favorable price spreads never
10 materialize, NW Natural simply relies on the surplus physical gas to backstop any trade.
11 Given the likelihood that price spreads will exist, and NW Natural's decision to engage in
12 trades only when it knows gas is available as a backstop, there appears to be no downside
13 to these trades. The only uncertainty is the size of the price spread. NW Natural adds to
14 the certainty through its use of a third-party asset manager to manage the Optimization
15 Activities. The asset manager has deep expertise and a good track record in this area and,
16 therefore, NW Natural's role is limited. The Liberty Report also points out that FERC has
17 standardized asset management to a considerable degree, facilitating asset management.
18 As a result, it is clear to me that these kinds of activities are standard utility practices and
19 do not foist much risk on the Company.

20 **Q. WHY DO YOU RECOMMEND THE PARTICULAR SHARING SPLIT YOU DO?**

21 A. AWEC's goal in UM 1654 and now this proceeding is to find a principled basis for
22 determining the appropriate split in revenue sharing. For example, NW Natural cautioned
23 the parties in that docket that if a cost analysis were performed, customers would receive

1 an allocation that is “significantly less” than their current sharing percentage.³ AWEC was
2 willing to accept that outcome because it makes more sense to base the sharing on actual
3 benefits and risks of the various interests than solely on an agreed-to number derived before
4 much was known about how these activities would pan out. While NW Natural’s warning
5 statement was made in the specific context of Storage Services, the Liberty Report showed
6 that statement to be unfounded. Just as the Company is suggesting the Commission should
7 rely on the thoughtful analysis in the Liberty Report for Storage Services, the Commission
8 should also rely on Liberty’s analysis for Optimization Activities.

9 The specific split I am recommending tracks with the conclusions in the Liberty Report.
10 First, my recommendation maintains the distinction between revenues derived from
11 facilities currently in customer rates and those that are not in customer rates, and it provides
12 a higher sharing percentage to the Company for the latter compared to the former since it
13 is relying less on customers’ prior investments for those revenues. Second, my
14 recommendation decreases the overall sharing to the Company to acknowledge (1) that
15 these activities have become standardized, (2) that they involve very little risk to the
16 Company’s investors, and (3) that the level of sharing is outside the norm compared to
17 other jurisdictions.

18 **Q. DO YOU BELIEVE THAT REVISING THE SHARING MECHANISM WILL**
19 **REDUCE NW NATURAL’S INCENTIVE TO MAXIMIZE REVENUES?**

20 A. No. The Liberty Report addressed this issue and concluded that even if NW Natural
21 receives a lower share of the revenue, it should still have a significant incentive to
22 maximize performance without incurring undue risk.

³ Docket UM 1654, NW Natural Gas Company’s Post Hearing Brief at p.19.

1 **Q. HOW SHOULD THE NW NATURAL REVENUE BE TREATED FROM THESE**
2 **OPERATIONS?**

3 A. As the parties argued in UM 1654, revenue derived from Optimization Activities should
4 be reported on NW Natural's annual results of operations ("ROO") because the income
5 derived from Schedules 185 and 186 is derived or made possible from customer-funded
6 assets.

7 **Q. DOES THIS CONCLUDE YOUR OPENING TESTIMONY?**

8 A. Yes, it does.