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.	)
	)

PHASE II REBUTTAL TESTIMONY OF

BRADLEY G. MULLINS

ON BEHALF OF THE ALLIANCE OF WESTERN ENERGY CONSUMERS

DECEMBER 12, 2018

Redacted Version

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I. INTRODUCTION

Q. ARE YOU THE SAME WITNESS THAT PROVIDED TESTIMONY FOR AWEC IN PHASE I OF THIS DOCKET?

A. Yes. I previously filed testimony in this matter on behalf of the Alliance of Western Energy Consumers ("AWEC").

Q. WHAT IS THE PURPOSE OF YOUR PHASE II REBUTTAL TESTIMONY?

A. As required by Order No. 18-419 issued by the Public Utility Commission of Oregon ("Commission"),[1] Administrative Law Judge ("ALJ") Arlow issued a Prehearing Conference Memorandum[2] on November 13, 2018 to open Phase II of this docket to resolve two outstanding issues: (1) the regulatory treatment associated with terminating the Pension Balancing Account ("PBA"); and, (2) the proper ratemaking treatment of tax reform savings NW Natural recognized over the period January 1, 2018 and October, 31, 2019 ("Interim Period"). Northwest Natural Gas Company ("NW Natural") filed Phase II Opening Testimony of witnesses Wilson[3] and Borgerson[4] on November 21, 2018. NW Natural also filed Phase II Supplemental Testimony of witness Wilson[5] on November 29, 2018.

In my testimony, I discuss my review and conclusions with respect to the two issues outstanding in this docket, and respond to NW Natural's Phase II Opening Testimony and Phase II Supplemental Testimony.

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1 *In the Matter of Northwest Natural Gas Company*, *dba NW Natural, Request for a General Rate Revision* Docket UG-344, Order No. 18-419 (Oct. 26, 2018) ("Order No. 18-419").

2 Docket UG-344, Prehearing Conference Memorandum (Nov. 13, 2018).

3 NW Natural/2800.

4 NW Natural/2900.

5 NW Natural/3000.

Q. PLEASE SUMMARIZE YOUR RESPONSE WITH RESPECT TO THE PENSION BALANCING ACCOUNT.

A. As AWEC noted in Phase I of this Docket, the stipulation filed in *In re Northwest Natural Gas Company, dba NW Natural, Application to Defer Pension Costs*, docket UM 1475 (the "UM 1475 Stipulation") does not provide NW Natural with the right to amortize any amount in rates in connection with the PBA.[6] Before amortizing any excess pension expenses—the amount by which actual pension expenses exceed the amount included in rates—the UM 1475 Stipulation required the PBA to reverse and become negative. Because all parties to the UM 1475 Stipulation were mistaken about what would happen to the PBA, and because it did not reverse or become negative (and never would), the Commission froze and terminated the PBA in Phase I of this docket.[7] In addition, the general principle historically applied in Oregon is that excess pension expenses are not recoverable through deferrals.[8] Indeed, this principle governed how the PBA operated for many years, up until the UM 1475 Stipulation, requiring NW Natural to refund the overcollections, but not recover excess pension expenses. Accordingly, neither the UM 1475 Stipulation, nor Oregon regulatory policy, supports amortization of $79,861,289 of excess pension expenses that exists in the current circumstances, without further determination by this Commission.

For the reasons set forth in this testimony, it is not reasonable to simply assume, as NW Natural has, that ratepayers should be responsible for all the excess pension expense amounts that NW Natural has recorded in its financial statements in connection with the PBA. Before

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6 AWEC/600; Mullins/4:3-6.

7 *In the Matter of Northwest Natural Gas Company, Request for a General Rate Revision*, Docket UG 344, Order 18-419 (Oct. 26, 2016).

8 *In the Matter of Portland General Electric Company, Application for Deferral Accounting of Excess Pension Costs and Carrying Costs on Cash Contributions*, Docket UM 1623, Order 16-257 (Aug. 7, 2016)

any potential ratepayer responsibility should exist, I recommend that the Commission consider the reasons the PBA did not reverse as intended. My review focuses on a few key questions that I believe are pertinent before considering any, or the degree of, ratepayer responsibilities resulting from the failure of the run-away regulatory account.

1. Why did the PBA not reverse and become negative, as required by the UM 1475 Stipulation?
2. When did NW Natural recognize that the balancing account would not reverse and would not become negative?
3. Did NW Natural contribute to the PBA in a manner consistent with the UM 1475 Stipulation?
4. Should NW Natural be compensated for the time value of money in connection with excess pension expenses?

Based on my analysis and answer to these questions, NW Natural's actions and inactions contributed to the failure of the PBA, such as making inadequate contributions and de-risking the plan assets. In addition, despite having the burden of proof, NW Natural has provided no evidence to demonstrate that the failure of the PBA was due to factors outside of its control, a problem exacerbated by the fact that the documentation necessary to make such a determination was destroyed in connection with NW Natural's document retention policy. Accordingly, I have concluded that it is not fair, just or reasonable to allow NW Natural to amortize all of the funds in the PBA, and some form of sharing between customers and shareholders should be required.

Even if the UM 1475 Stipulation did allow for amortization in these circumstances, some form of sharing between shareholders and ratepayers is necessary to account for NW Natural's role in the PBA's failure. In the following testimony, I will discuss principled adjustments that should be considered by this Commission.

Q. WHAT ARE YOUR PRINCIPAL CONCLUSIONS REGARDING THE INTERIM PERIOD TAX SAVINGS CALCULATION?

A. While AWEC is concerned with using the *with* and *without* method proposed by NW Natural, AWEC is willing to accept NW Natural's calculation, provided that it is adjusted to properly reflect Excess Deferred Federal Income Tax ("EDFIT") amortization. Specifically, AWEC recommends: (1) that protected EDFIT amortization of $2,719,166[9] be considered in the Interim Period deferral calculation; and (2) that unprotected EDFIT amortization of $6,700,000 be include in the Interim Period deferral calculation.[10] After including these amortization amounts, the total Interim Period deferral AWEC supports is $16,207,166. AWEC recommends the Commission amortize this amount over a two-year period and be returned to customers on an equal percent of margin basis. AWEC's proposed treatment for the Interim Period deferral, including protected and unprotected EDFIT amortization, is identical to the treatment that the Commission recently approved for Portland General Electric Company ("PGE").[11]

II. EARLY TERMINATION OF PENSION BALANCING ACCOUNT

a. NW Natural's Amortization Proposal

Q. PLEASE SUMMARIZE NW NATURAL'S PROPOSAL WITH RESPECT TO THE PENSION BALANCING ACCOUNT.

A. NW Natural proposes to amortize *at least* $79,861,289 in connection with the early termination of the PBA.[12] The reason I say "*at least*" is that, for financial purposes, NW Natural continues

9 *See* NW Natural-Staff-CUB/201. Calculated by prorating $3,263,000 protected EDFIT amortization over 10 months.

10 *Id.*

11 *See In the Matter of Portland General Electric Company*, Application for Authorization to Defer Benefits Associated with the US Tax Reconciliation Act, Docket UM 1920, Order 18-459 (Dec. 5, 2018).

12 NW Natural/3001

to accrue interest on the balance, and thus, apparently has some expectation of amortizing an even larger amount that includes the additional interest despite Order No. 18-419.

Q. WHAT DOES THE $79,861,289 AMOUNT REPRESENT AND HOW WAS IT CALCULATED?

A. It was not until NW Natural filed its Phase II Testimony that it provided the calculation of the PBA balance as an exhibit. NW Natural argues, in part, that the UM 1475 Stipulation provided "dollar for dollar recovery by NW Natural of all amounts booked to the PBA, without a prudence review, and without an earnings review until the full amount in the account had been reduced to zero."[13]

Q. DO YOU AGREE THAT THE ABOVE REFERENCED QUOTE PROVIDES NW NATURAL THE AUTHORITY TO RECOVER THE ENTIRE BALANCE OF THE PBA IN RATES?

A. No. That is not how I interpret the UM 1475 Stipulation because the UM 1475 Stipulation also provides that NW Natural is not entitled to recover any amounts of the PBA from customers under the current circumstances.

Further, the PBA does not represent any amounts that have been approved by the Commission annually, like the Commission would typically do for a power cost deferral. The PBA balances appear to correspond only to the amounts NW Natural has accrued <u>on its books</u> with respect to the PBA. In addition, the balances are extraordinarily large, as far as deferrals go; about three to four times larger than the overall revenue requirement increase NW Natural received in Phase I of this docket. That magnitude warrants scrutiny of these amounts before assigning responsibility to ratepayers.

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13 NW Natural/2800, Mullins at 4:14-17.

The PBA balances NW Natural calculates span a wide range in time going back eight years to the beginning of 2011 and include a staggering $20,936,625 in interest, a number NW Natural continues to inflate for financial purposes.[14]

Q. IS IT APPROPRIATE FOR NW NATURAL TO CONTINUE TO ACCRUE INTEREST FOLLOWING THE COMMISSION'S OCTOBER 26, 2018 ORDER IN THIS DOCKET?

A. No. In Order No. 18-419 resolving the issues in Phase I of this docket, the Commission stated: "To mitigate the growth of the problem during this time, we direct NW Natural to freeze the pension balancing account, and authorize the company to set its FAS 87 expense to be included in rates at $8.1 million annually."[15]

Accordingly, NW Natural has transitioned to FAS 87 going forward, but apparently concludes that it may nevertheless continue to accrue interest on the PBA pending a final order in Phase II of this docket. This is not how I read the Commission's Order, and thus, I find NW Natural's financial presentation to be problematic. In fact, it is not reasonable to assume that any interest may be recoverable through the PBA since the UM 1475 Stipulation did not allow for any amortization in these circumstances.[16]

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14 NW Natural/3001 Wilson/1.

15 Docket UG 344, Order 18-419 (Oct. 26, 2018).

16 *In the Matter of Northwest Natural Gas Company, Approving Deferral of Certain Expenses for Revenues Pursuant to ORS 757.259*, Docket UM 1475, Stipulation at 4 (Nov. 4, 2010) (agreeing that "[t]he Company may not submit a request to amortize the balancing account balance prior to the termination date of the balancing account.").

b. NW Natural's Financial Accounting

Q. WHAT AMOUNTS HAS NW NATURAL RECORDED FOR FINANCIAL PURPOSES WITH RESPECT TO THE PBA?

A. For financial purposes, NW Natural had recorded a $72,291,000 regulatory asset as of September 30, 2018 in connection with the PBA that it assumes is the responsibility of ratepayers.[17] I have been unable to reconcile the PBA financial balance with the balances that were presented in NW Natural's Supplemental Phase II Testimony.

Q. WHAT ARE THE FINANCIAL STANDARDS FOR RECORDING A REGULATORY ASSET?

A. Accounting Standards Codification ("ASC") 980-340-25-1 outlines two criteria that must be met to recognize a regulatory asset. First, it must be probable that future revenues in an amount equal to the capitalized cost will be recoverable in rates. For accounting purposes "probable" is usefully defined as a likelihood in excess of 50%. Second, the future revenue must allow for recovery of previously incurred costs, rather than providing for an expected level of similar future costs.

Q. DID THE PENSION BALANCING ACCOUNT MEET THESE CRITERIA?

A. Since the PBA was designed to reverse naturally, it did not necessarily meet the second criteria for recognition. The PBA was designed such that any excess pension expenses would be applied as an offset to future levels of SFAS 87 expenses. The PBA was not designed to allow NW Natural to increase rates in the future; the PBA balance was designed to offset reductions in future expense.

In addition, the PBA also did not necessarily meet the first criteria for recognition because it was obvious within the first accounting period of the PBA that it was not "probable"

[17] NW Natural, *Form 10-Q* at 13 (Sep 30, 2018)

that the PBA would naturally reverse, and thus, be eligible for amortization in customers rates. At a minimum, annual impairment testing should have been conducted to remeasure the PBA asset, yet that did not occur.

Q. IS NW NATURAL REQUIRED TO PERIODICALLY TEST REGULATORY ASSETS SUCH AS THE PENSION BALANCING ACCOUNT FOR IMPAIRMENT?

A. Yes. ASC 980-340-35-1 requires a regulated entity, such as NW Natural, to periodically test the regulatory asset for impairment, and apply a valuation allowance, if necessary.

Q. DID NW NATURAL OR ITS AUDITORS EVER CONDUCT SUCH IMPAIRMENT TESTS?

A. No. In response to AWEC Data Request 70, NW Natural admits that it never conducted or considered a valuation allowance for accounting purposes.

c. UM 1475 Stipulation Requirements

Q. WHAT DOES THE UM 1475 STIPULATION ACTUALLY SAY ABOUT AMORTIZING THE PENSION BALANCING ACCOUNT IN RATES?

A. Both the UM 1475 Stipulation, and supporting testimony, were clear that amortization of the PBA could only commence when the account reversed and became negative. The Stipulation memorialized this expectation as follows:

> "Whereas, the Company has estimated that its pension expense will continue to exceed the amounts recovered in rates for the next three years, but that this trend will reverse over the following years and that expenses and revenues will balance out over the next approximately four years."[18]

Thus, the PBA was expected to accrue a positive balance (excess pension expenses) over the period 2011 through 2013. Beginning in 2014, the PBA was expected to accrue negative

[18] *In the Matter of Northwest Natural Gas Company*, dba NW Natural Application to Defer Pension Costs, UM 1475, Stipulation, Page 2 (Nov. 4, 2010).

amounts (i.e. over collection). By 2018, the impact of these off-setting accruals were supposed to balance out and the PBA balances were supposed to become negative.

Thus, over a seven-year period, the pension was supposed to be fully funded and the PBA would naturally reverse, allowing for reversal of the deferred funds. In support of the UM 1475 Stipulation, the following testimony was cited:

> The Company expects that [redacted]

The entire Stipulation agreement was premised on this understanding.

Q. DID NW NATURAL MAKE THE CONTRIBUTIONS REQUIRED BY THE PBA AND UM 1475?

A. [redacted]

Q. HOW WAS THIS REQUIREMENT TO BE ENFORCED IN THE STIPULATION?

A. The requirement that the PBA reverse was contained in Paragraph 4 in the UM 1475 Stipulation, which provides:

> "The balancing account will terminate upon the effective date of the tariffs filed in connection with the first NW Natural general rate case submitted to the Commission after the balance of the FAS 87 pension expense balancing account becomes negative. The Company may not submit a request to amortize the balancing account balance prior to the termination date of the balancing account."[19]

Thus, amortization was not to commence prior to the termination date and the termination date did not occur until after the PBA became negative, and the pension was fully funded. This requirement of the UM 1475 Stipulation is clear: if the balances did not reverse naturally, as

[19] *Id.*

represented in the preamble section, NW Natural was not entitled to automatically amortize any excess pension expenses in rates.

Q. HOW DID THE PENSION BALANCING ACCOUNT OPERATE PRIOR TO THE STIPULATION?

A. Prior to the UM 1475 Stipulation, the PBA had operated for many years under a construct where NW Natural was required to issue a refund to customers if it over-collected pension expenses, but was not entitled to collect excess pension expenses in years when actual pension expenses exceeded the amount incorporated in rates. The UM 1475 Stipulation continued the same treatment, with the exception that excess pension expenses would be recoverable, but only through the natural reversal process identified in the UM 1475 Stipulation.

Q. DID NW NATURAL COMMIT TO FULLY FUND THE PENSION WHEN IT ENTERED INTO THE UM 1475 STIPULATION?

A. When entering into the UM 1475 Stipulation, NW Natural represented that its pension plan would be fully funded within a matter of six or seven years. To actually achieve that outcome, NW Natural had the onus, pursuant to the UM 1475 Stipulation, to contribute to the plan in a manner that would result in fully funding the pension plan within that period. If the burden of the necessary contributions were too high, then it was NW Natural's burden to seek relief, as the accrued balances were not recoverable if the PBA did not reverse.

Q. SHOULD RATEPAYERS BE RESPONSIBLE FOR ALL OF THE RESIDUAL BALANCES ASSOCIATED WITH THE PENSION BALANCING ACCOUNT?

A. Before summarily concluding that ratepayers should bear responsibility for all amounts in connection with the PBA, it is necessary to understand the reasons the PBA did not reverse in the manner represented by NW Natural in the UM 1475 docket. It would not be appropriate, for instance, to provide NW Natural with extraordinary rate relief in connection with its actual FAS 87 pension expense if NW Natural did not behave in a manner that was consistent with the intent of the UM 1475 Stipulation. If the causes were extraordinary, on the other hand, then the analysis might be different. To analyze NW Natural's request, it is necessary to provide some brief background on deferred accounting and pension expenses accounting, as both are relevant in considering that request.

d. Regulatory Framework

Q. WHAT IS THE PROPER REGULATORY FRAMEWORK FOR CONSIDERING AMORTIZATION OF THE PENSION BALANCING ACCOUNT?

A. The PBA is somewhat of an amalgam for ratemaking purposes. In UG 152, the PBA was originally established as a deferral, pursuant to the Appendix to the UG 152 Partial Stipulation Regarding Revenue Requirement as follows:

> "Deferred accounting will be implemented to provide customer credits in the event that actual pension expenses are less than those included in the filed case. Agreement that the Parties will consider implementation of deferred accounting if pension costs increase above the stipulated amount in future years."

The UM 1475 Stipulation changed that treatment, and allowed deferred accounting for excess pension expenses, but only to the extent the account naturally reversed. While the mechanism is called "balancing account," it is appropriately viewed as a deferral under ORS 757.259, amounts includable in rate schedules. Thus, the deferral statutes and rules are the appropriate regulatory framework for determining whether amounts may be amortized in connection with the PBA.

In support for considering the PBA under the deferral rules, I observe that the account is clearly not an automatic adjustment clause. Nor is the PBA an unrecovered investment regulatory asset, such as the Trojan Nuclear Power Plant or Deer Creek Mine.

Q. WHAT ARE THE STATUTORY REQUIREMENTS FOR AMORTIZING A DEFERRAL?

A. Under ORS 757.259, issuance of a deferral by the Commission is no guarantee that deferred amounts are recoverable from ratepayers through amortization. Oregon follows a two-step process that requires Commission approval at both the deferral and amortization stage. The general requirements for amortization described in ORS 757.259(5), are as follows:

> [Amortization] shall be allowed in rates only to the extent authorized by the commission in a proceeding under ORS 757.210 (Hearing to establish new schedules) to change rates and upon review of the utility's earnings at the time of application to amortize the deferral. The commission may require that amortization of deferred amounts be subject to refund. The commission's final 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.

Q. WHAT ARE THE ADMINISTRATIVE REQUIREMENTS FOR AMORTIZATION?

A. The Commission's rules also contain a number of requirements that must be met to begin amortizing an approved deferral. For example, OAR 860-027-0300(2) provides that deferrals are limited to a 12-month period of time:

> "Expiration: Any authorization to use a deferred account expires 12 months from the date the deferral is authorized to begin. If a deferral under ORS 757.259 or 759.200 is reauthorized, the reauthorization expires 12 months from the date the reauthorization becomes effective."

While I have not researched the precise genesis of this requirement, I believe the 12-month limitation was designed to prevent problems that occur with multi-year deferrals, which have the potential to produce significant balances without any visibility by the Commission.

This 12-month limitation, along with the requirement for an earnings test, is further detailed in OAR 860-027-0300(9):

> "Amortization: Amortization in rates of a deferred amount is allowed only as authorized by the Commission. The Commission may authorize amortization of such amounts only for utility expenses or revenues for

> which the Commission previously has authorized deferred accounting. Upon request for amortization of a deferred account, the energy or large telecommunications utility must provide the Commission with its financial results for a 12-month period or for multiple 12-month periods to allow the Commission to perform an earnings review. The period selected for the earnings review will encompass all or part of the period during which the deferral took place or must be reasonably representative of the deferral period."

Q. DID NW NATURAL SATISFY THE COMMISSION RULES FOR AMORTIZING THE PENSION BALANCING ACCOUNT?

A. No. First, NW Natural has not "provided the Commission with its financial results for a 12-month period or for multiple 12-month periods to allow the Commission to perform an earnings review." Interestingly, NW Natural acknowledges the need to conduct an earnings test.[20] Notwithstanding, NW Natural argues that there is "no reason" an earnings test should be performed now.[21] I disagree. I view the earnings test to be a requirement of the law and that it is NW Natural's burden to satisfy the test.

Second, NW Natural does not appear to have ever sought annual reauthorization of the PBA deferred account. This might be due to the fact that the account was expected to naturally reverse, without the need to amortize any additional amounts into rates. Because the PBA did not naturally reverse as intended, the lack of a reauthorization procedure is problematic. If NW Natural had followed the reauthorization procedure above, it is possible that the problems with the PBA would have been observable sooner, even in the first year following the UM 1475 Stipulation.

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20 NW Natural/2800, Wilson 12:9-13:2
21 NW Natural/2800, Wilson/21:15-22:2,

Q. HAS THE COMMISSION HISTORICALLY ALLOWED UTILITIES TO RECOVER EXCESS PENSION EXPENSES THROUGH DEFERRED ACCOUNTING?

A. No. Due to the inter-temporal natural of pension expenses, application of deferred accounting for pension expenses can be particularly problematic.

This was evident in Docket UM 1623, where the Commission denied the request of PGE to defer excess pension expenses over the period 2012 through 2015.[22]

Q. WHAT DID THE COMMISSION FIND IN UM 1623?

A. The Commission found that pension expenses are not good candidates for deferrals because "actual FAS 87 expense naturally fluctuates above and below the forecasted expense, and that under-collections in one period tend to be offset by over-collections in other periods."[23]

The Commission found that "the higher-than-expected FAS 87 expense during the deferral period constitutes a stochastic risk, meaning; it was a natural variation and requires a finding of "substantial" harm to justify deferred accounting."[24] Since PGE made no such showing in UM 1623, the application was denied.

Q. DID THE COMMISSION MAKE A SIMILAR DECISION IN THE GENERIC PENSION INVESTIGATION IN UM 1633?

A. Yes. There the Commission found that SFAS 87 "has been used successfully for almost 30 years as part of this Commission's overall ratemaking formula to appropriately balance the interests of the utilities and customers and establish overall rates that were just and reasonable."[25]

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22 *In the Matter of Portland General Electric Company, Application for Deferral Accounting of Excess Pension Costs and Carrying Costs on Cash Contributions*, Docket UM 1623, Order 16-257 (Aug. 7, 2016)

23 *Id.*

24 *Id.*

25 *In the Matter of Public Utility Commission of Oregon, Investigation into Treatment of Pension Costs in Utility Rates*, Docket UM 1633, Order 15-226 (Aug 5, 2015) at 10.

Q. DOES THIS DOCKET REINFORCE THE COMMISSION'S DECISION IN UM 1633?

A. Yes. This docket reinforces the notion that balancing accounts for pension expense are not workable regulatory mechanisms and that the traditional use of SFAS 87 expense is the preferred way for dealing with the recovery of pension expenses.

e. <u>Pension Expense Calculation</u>

Q. PLEASE PROVIDE SOME ACCOUNTING BACKGROUND ON PENSION EXPENSES.

A. Two general accounting issues arise when dealing with pension expenses. First, it is necessary to determine the liability, or *pension obligation*, that must be recorded on the utility's balance sheet. Second, it is necessary to determine pension expense that must be accrued for the period.

Q. HOW IS THE PENSION OBLIGATION DETERMINED?

A. For financial accounting purposes, the *projected benefit obligation* is used to establish the employer's pension obligation. Using the projected benefit obligation calculation, the pension obligation amount represents the present value of vested and non-vested benefits accrued using an estimate of future salary levels. In contrast, use of an *accumulated benefit obligation* bases the benefit calculation on current salary levels.

Prior to the issuance of FASB Statement No. 87, accounting for pension plans followed a non-capitalization approach, where pension expenses were primarily tied to contribution levels. In 1985, the issuance of FASB Statement No. 87 changed that view and moved towards a full-capitalization approach, where the employer records liability for pension benefits that it has promised to pay for employee services already performed. FASB Statement No. 87 was a compromise between a capitalization and non-capitalization approach because it required employers to use the projected benefit obligation for purposes of determining the current pension expense, but used the *accumulated benefit obligation* for purposes of determining the liability amount, often referred to as the *minimum liability*.

Q. HOW ARE PENSION EXPENSES DETERMINED?

A. Accounting for pension expenses is complicated, which is why actuaries are typically hired to perform the calculation. At its simplest form, however, the goal of pension accounting is to isolate how different events occurring during the financial period impacted the change in projected benefit obligation. The expense is usually attributed to the following categories:

> **Current Service Costs –** The expense caused by the increase in the projected benefit obligation due to employee services rendered in the current period.
>
> **Unrecognized Prior Service Costs –** The amount of the change in the projected benefit obligation attributable to prior periods employee services due to plan amendments. These amounts are typically amortized over the remaining service-years of affected employees.
>
> **Interest on the Liability –** Because the benefit obligation is recorded on a discounted basis, periodic interest will accrue with respect to the change in the projected benefit obligation.
>
> **Actual Return on Plan Assets –** The interest and dividends that accumulate with the fund, as well as increases and decreases in the market value of the fund assets. This category also includes the impact of differences between contributions and benefits paid.
>
> **Other Gains or Losses –** Difference between actual return and the expected return on plan assets and amortization of the unrecognized gains or losses from prior periods. These amounts are typically only amortized when exceeding 10 percent of fund assets, called a “corridor”.

f. <u>Evaluation of Docket UM 1475 Assumptions</u>

Q. WHY DID THE PENSION BALANCING ACCOUNT NOT REVERSE AS INTENDED IN THE UM 1475 STIPULATION?

A. I understand that NW Natural has the burden of proof with respect to its PBA amortization proposal. Notwithstanding, few records exist to determine the reasons the PBA did not reverse as intended in UM 1475. Basically, the only information available are the hardcoded forecasts numbers of SFAS 87 that were presented in UM 1475 testimony.[26] These forecasts do not detail the individual categories of SFAS 87 expense, as I have outlined above. Accordingly, it is not known which categories of SFAS 87 led to extreme variances between the actual expense and the UM 1475 forecast.

Q. DID YOU REQUEST THE DETAIL SURROUNDING THE UM 1475 SFAS 87 EXPENSE FORECAST?

A. Yes. In AWEC Data Request 74, AWEC requested NW Natural to "provide copies of all workpapers associated with NW Natural's September 20, 2010 Direct Testimony filing in Docket UM 1475." NW Natural responded "NW Natural did not submit work papers in association with this filing and has not retained any such documentation in compliance with our records retention policy."

Q. WHAT DATA DID NW NATURAL PROVIDE?

A. In response to CUB Data Requests 72, NW Natural provided confidential versions of the testimony in UM 1475, including PDF copies of the associated exhibits. I have attached a copy of the confidential portions of the UM 1475 filings in Confidential Exhibit AWEC/702.

In addition, in response to AWEC Data Request 73, NW Natural provided responses to several data requests from UM 1475, although the degree to which the information in those data requests were used to support the Stipulation is unknown. Notwithstanding, in UM 1475 Staff Data Request 03, NW Natural provided a forecast of SFAS 87 expenses, that was different than the one presented in UM 1475 Testimony. I have attached that slightly different forecast in Confidential Exhibit AWEC/703.

[26] *See* UM 1475, NWN/206.

Q. WHEN DID IT BECOME EVIDENT THAT THE PENSION BALANCING ACCOUNT WAS NOT OPERATING AS INTENDED?

A. It should have been plainly obvious in 2011 (the first year the PBA was in operation following the UM 1475 Stipulation) that the PBA was not operating as anticipated. Below is a comparison between actual SFAS 87 expenses, and SFAS 87 expenses assumed in UM 1475.

CONFIDENTIAL TABLE 1

Comparison of Actual SFAS 87 to UM 1475 Forecast

[redacted]

[redacted] That variance was significant enough that it should have raised a red flag. [redacted]

Even if the 2011 variance was not enough to cause concern, the following years certainly should have. [redacted]

[redacted] Given such significant variances, it was not reasonable for NW Natural to conclude that it was probable that the account would reverse in rates.

Q. WHAT CAUSED ACTUAL SFAS 87 EXPENSE TO EXCEED THE UM 1475 FORECAST BY SUCH A DEGREE?

A. NW Natural cannot demonstrate why actual SFAS 87 expenses exceeded the UM 1475 forecast by such significant variances. In fact, in response to AWEC Data Request 74, NW Natural admitted that it destroyed the information consistent with its document retention policy. Since NW Natural has the burden of proof, it calls into question the efficacy of this policy, particularly when considering complex multi-year deferrals such as the PBA.

Q. HOW WERE THE ABOVE FORECASTS USED IN THE UM 1475 STIPULATION?

A. It is not known which, if any, of the available forecasts were used to inform the UM 1475 Stipulation requirement for the balance to reverse before amortization could commence. Notwithstanding, both forecasts followed a consistent pattern that resulted in the pension being fully funded by 2017.

Q. WHAT INFORMATION CAN BE GAINED FROM THE ACTUARIAL REPORTS?

A. Based on my review of the actuarial reports, which were provided in response to AWEC Data Request 65, some inferences can be made about the reasoning that the PBA did not reverse. From those documents it is possible to compare some of the SFAS 87 forecasting assumptions, such as interest rates or contribution levels, to actual SFAS 87 expense. Although, it is not known how those assumptions impacted the forecast since the forecast numbers were hardcoded, and NW Natural destroyed the supporting documentation. When comparing against these forecasting assumptions, seemingly across the board, most assumptions trended against customers relative to the forecasts developed in UM 1475. Interest rates were lower, contributions lower, and the amortization of other gains/losses grew rapidly.

Q. WERE THESES DIFFERENCES DUE TO EXTRAORDINARY CIRCUMSTANCES?

A. Unlike the dramatic changes that took place with respect to interest rates following the financial crisis in 2008, interest rates during the period in which the PBA operated were relatively stable. To be clear, interest rates were low during the period, but were not subject to large unexpected swings, such as those that occurred in the financial crisis. The pension losses that occurred during the financial crisis had passed, or at least NW Natural represented that those historical losses were not to be tracked through the PBA. NW Natural represented that it would [redacted].[27] Yet, these promised contributions were not made.

g. <u>Impact of Contributions Relative to UM 1475 Stipulation</u>

Q. WHAT REPRESENTATION DID NW NATURAL MAKE WITH RESPECT TO ANY OF ITS EXPECTED CONTRIBUTIONS TO THE PENSION PLAN IN UM 1475?

A. In UM 1475, NW Natural represented that it planned to make contributions "[redacted]."

Q. DID NW NATURAL ACTUALLY MAKE THOSE CONTRIBUTIONS?

A. No. AWEC requested that NW Natural provide its actual pension contributions in AWEC Data Request 66. In 2011, actual plan contributions were [redacted] that NW Natural represented that it would contribute in 2011. Note that in

27 UM 1475, NW Natural/200, Feltz/11:3-4

AWEC DR 66, the [redacted], which I do not consider in this comparison. In 2012, actual plan contributions were just [redacted] NW Natural represented it would contribute for 2012. Similar underfunding can be observed in other years, as detailed in Table 2, below.

CONFIDENTIAL TABLE 2

Comparison of NW Natural Pension Contributions with UM 1475 on a Calendar Year Basis
Actual Contributions from AWEC Data Request 66 (See Confidential Exhibit AWEC/704)

[redacted]

In Table 3 below I show the same actual contributions by Plan year. The actual contributions assigned to a given plan year often occur subsequent to the calendar year, so comparing to the calendar year contributions might skew the result. Notwithstanding, when viewed from the perspective of the plan year, the same pattern of underfunding can be observed. In 2012, actual plan year contributions were [redacted] NW Natural represented it would contribute for 2012.

CONFIDENTIAL TABLE 3

Comparison of NW Natural Pension Contributions with UM 1475 on a Plan Year Basis
Actual Contributions from AWEC Data Request 66 (See Confidential Exhibit AWEC/704)

[redacted]

Q. HOW DO PLAN CONTRIBUTIONS IMPACT PENSION EXPENSES?

A. There is a direct relationship between plan contributions and future periodic pension expenses. Lower plan contribution levels produce higher future periodic pension expenses. In UM 1475, NW Natural estimated the expense impact of making a $35,300,000 of incremental contribution to the Pension plan as follows:

> For example, for Plan years 2004 and 2005 the Company made actual contributions totaling $36.3 million compared to minimum required contributions of $1 million. See Confidential Exhibit NWN/204. At 8.25 percent, the extra $35.3 million in contributions reduced FAS expense by $2.9 million in the first year, and by $2.9 million plus any additional return generated from returns on this amount that affect future years.

Thus, lower contributions result in higher SFAS 87 expense in the year of the lower contribution and in all subsequent years. As noted above, SFAS 87 expense also includes an interest component on the pension benefit obligation, and accordingly, the reduced contribution also results in a higher interest cost included in SFAS 87 expense. Further, if actual market returns were favorable relative to the assumed investment yield, the contribution may reduce the amortization of Other Gains or Losses, as well. Thus, not only is the amount of the contribution important, the timing of the contribution is also vitally important in transitioning to a fully funded status.

Q. DID THESE REDUCED CONTRIBUTION LEVELS CONTRIBUTE TO THE FAILURE OF THE PBA?

A. Yes. Base on my review the reduced contribution levels appear to be one of the key reasons that the PBA did not reverse. It is true that in later years, NW Natural's contributions exceeded the forecast. NW Natural began exceeding the forecast in 2015 because the plan was expected to be fully funded around that time. The time value of money implications, however, are the important consideration. If NW Natural had made the earlier contributions, a portion of the later contributions would have been unnecessary, similar to paying off a car to avoid future payments.

Q. DID NW NATURAL HAVE IN INCENTIVE TO REDUCE THE CONTRIBUTIONS?

A. Yes. NW Natural had an incentive to reduce its plan contributions. By contributing less, not only did NW Natural avoid the cashflow implications of making such contributions, doing so would increase the SFAS 87 Expense in later years, leading to higher revenue accruals through the PBA—that it now argues is the responsibility of ratepayers. This is why the requirement in the UM 1475 Stipulation for the PBA to reverse was such an important provision.

Q. SHOULD NW NATURAL BE ALLOWED TO RECOVER THE BALANCES IN THE PENSION BALANCING ACCOUNT THAT ARE DUE TO NW NATURAL'S FAILURE TO MAKE ADEQUATE CONTRIBUTIONS?

A. I recommend that the Commission give careful consideration to making adjustments to account for the underfunding. The balances that accrued due to the fact that NW Natural underfunded the pension plan should not be recoverable from ratepayers, since that was a variable explicitly within NW Natural's control.

Q. WHAT WAS THE IMPACT OF REDUCED CONTRIBUTIONS ON THE PBA BALANCE?

A. If one just looks to the contribution levels promised in UM 1475, the impact is somewhat complicated because it is difficult to compute what the expense levels would have been if the promised contributions in the earlier years had been made. In confidential Table 4, below, I've performed a calculation to estimate the time value implications of NW Natural's under-contribution, in addition to the cumulative contribution variance over the period.

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CONFIDENTIAL TABLE 4
Estimated Impact of NW Natural Pension Contribution Pattern

[redacted]

As can be noted through Table 4, the time value implications of NW Natural slower funding pattern are significant. [redacted] Those costs flow through the interest expense and net gain and loss component of SFAS 87 pension expenses. [redacted]

h. Impact of De-risking the Pension Plan

Q. HOW DO INTEREST RATES IMPACT SFAS 87 EXPENSE?

A. Interest rates impact SFAS 87 expenses in many ways. In fact, since pension expenses are concerned with changes to the present value pension benefit obligation, the expense is highly sensitive to interest rates. Interest rates impact the periodic expense calculation in several ways. First, an interest rate is used to establish the expected return of investment yield on plan assets for purposes of determining the pension benefit obligation. This interest rate is not the actual plan return, but a forecast of future plan returns. To the extent that actual returns are different than the forecast, the impact of the difference is trued up through other gains and losses.

In addition, a different interest rate is used to calculate the present value of the pension benefit obligation, as well as the associated interest accrued with respect to the pension benefit obligation liability. This other interest rate will be discussed further below.

Q. WHAT INVESTMENT YIELD DID NW NATURAL ASSUME IN UM 1475?

A. Based on the forecast provided in response to Staff Data Request 03 in UM 1475, NW Natural assumed an investment yield of 8.25%.

Q. WHAT INVESTMENT YIELD WAS ASSUMED IN CALCULATING ACTUAL PENSION EXPENSES?

A. Based on my review of the actuarial reports provided in response to AWEC Data Request 65, the expected return on plan assets fluctuated but was generally reduced to around 7.50%. This reduction in the expected investment yield of plan assets materially increased the pension benefit obligation, and the associated pension expense.

Q. DOES NW NATURAL CONTROL THE INVESTMENT YIELD?

A. Yes. NW Natural controls the investment portfolio of the plan and therefore is in control of the investment yield. NW Natural, for example, is able to select a higher-risk, higher-yield portfolio or a lower-risk, lower-return portfolio. Thus, the investment yield selection involves a tradeoff between risk and return. NW Natural may wish to select a lower risk portfolio for the pension plan. Such a decision, however, will result in a higher pension expense, which may not be desirable from a ratepayer perspective. In its UM 1475 forecast, NW Natural represented that it would apply a consistent investment yield. That is, UM 1475 assumed that NW Natural would not take actions to "de-risk" the pension plan, as doing so might cause the balance to not reverse.

Q. HOW DID THE LOWER INVESTMENT YIELD IMPACT THE BALANCING ACCOUNT?

A. When viewed in the context of the PBA, the higher expense allowed NW Natural to increase the deferrals accumulated to the PBA. Thus, by lowering the yield, NW Natural not only reduced its own risk, but also recorded additional deferred revenues through the PBA.

It is difficult to calculate the precise impact of reducing the expected investment yield, particularly since there are no workpapers supporting the UM 1475 forecast. Using the market value of plan assets identified in NW Natural/3002, however, I was able to develop the following estimate in Table 5:

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TABLE 5
Estimated Impact of De-risking
Per NW Natural/3002

Year	Market Value of Plan Assets		UM 1475 Yeild	Per Actuarial Report	Delta	Impact of Lower Yeild
2011	210,390,581		8.25%	8.25%	0.00%	-
2012	230,251,201		8.25%	8.00%	0.25%	575,628
2013	252,770,744		8.25%	7.50%	0.75%	1,895,781
2014	261,808,153		8.25%	7.50%	0.75%	1,963,561
2015	277,476,709		8.25%	7.50%	0.75%	2,081,075
2016	269,372,004		8.25%	7.50%	0.75%	2,020,290
2017	272,783,336		8.25%	7.50%	0.75%	2,045,875
2018	272,783,336	*	8.25%	7.50%	0.75%	2,045,875
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	272,783,336					12,628,085
					Avg. O&M Allocation	0.651625
					Avg. Oregon %	0.8995
					Oregon Share	7,401,784

* not reported in public version, assumed 2017 value.

This analysis does not assign any carrying costs to the lower annual yield, which if applied would imply a higher impact associated with NW Natural's de-risking.

Q. SHOULD NW NATURAL BE ALLOWED TO RECOVER THE IMPACT OF CHANGES TO THE INVESTMENT YIELD?

A. Not necessarily. Since NW Natural has control over the investment decisions of the pension plan, it should not necessarily be allowed to recover any funds accrued in connection with de-risking its pension plan.

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i. Double Counting of Interest Expenses

Q. IS IT REASONABLE FOR NW NATURAL TO COLLECT INTEREST WITH RESPECT TO THE PENSION BALANCING ACCOUNT?

A. For a multitude of reasons, it is not fair, just or reasonable for any interest to be recoverable through the PBA.

Primarily, since the mechanism had to be terminated early, prior to naturally reversing as required in the UM 1475 Stipulation, NW Natural should have no claim to earn carrying charges with respect to the PBA balances, particularly carrying charges which contemplate NW Natural earing it's return on equity with respect to the account.

Further, NW Natural's calculation of pension expenses double counts interest because SFAS 87 already compensates for the time value of money through the Interest on Liability Component of the expense.

Q. PLEASE FURTHER DESCRIBE HOW INTEREST EXPENSE IS INCLUDED IN SFAS 87 EXPENSE?

A. As noted above, the primary objective of the capitalization method of pension accounting is to determine the change in the present value of the pension benefit obligation. When moving from one period to another, a portion of the change in present value of the benefit obligation can be attributed to interest. The difference between the two present value calculations, say $1/(1+r)^t$ and $1/(1+r)^{t-1}$, is simply the incremental interest that occurred between the two points in time.

Q. IS THE PENSION BENEFIT OBLIGATION CONSIDERED AS A SOURCE OF FINANCING FOR RATEMAKING?

A. No. While for financial purposes pension expense is viewed as a source of financing, for regulatory purposes, the pension liability is typically not considered when determining a utility's overall rate of return.

Q. DOES THE INTEREST COMPONENT OF SFAS 87 EXPENSE ALREADY COMPENSATE THE COMPANY FOR THE TIME VALUE OF MONEY?

A. Yes. Because there is an interest rate assumption inherent in both the amount included in rates and actual pension expenses, the PBA already accounts for the time value of money, without the need for an addition interest accrual, as NW Natural has done.

Q. CAN YOU PROVIDE AN EXAMPLE?

A. For illustrative purposes, consider a $5 million forecast of pension expenses consisting of $1 million of interest cost and $4 million of other pensions costs. If actual pension expense were higher—due to reduced contributions, lower interest rates, or some other factor—the resulting actual pension expense would be higher with greater interest costs. Consider, for example if the actual expense were $12 million, consisting of $4 million of interest and $8 million of other pension costs. In this case, the excess pension expense would be $7 million ($12 million - $5 million). Of the $7 million, however, approximately $3 million would be attributable to interest expense. Thus, by truing up to actual SFAS 87 pension expenses, the incremental interest costs associated with the pension FAS 87 have already been considered.

NW Natural proposes to calculate a carrying charge on top of the interest that is already embedded in excess interest expense, and accordingly, double counts the time value of money.

Q. WHY DID THE UM 1475 STIPULATION ALLOW NW NATURAL TO RECOVER INTEREST ON THE PENSION ACCOUNT BALANCES?

A. The UM 1475 Stipulation was a good deal for customers and NW Natural, because NW Natural was allowed to earn its rate of return and the balances in the account were to reverse naturally with no further obligation for customers. Now that we have a complete change of circumstances, it is no longer appropriate for NW Natural to collect from customers interest that has been recorded on its financial statements.

Q. HOW MATERIAL ARE THESE INTEREST EXPENSES?

A. Interest expenses constitute a major portion of the proposed amortization amount. Of the $79,861,289 NW Natural proposes to recover $20,936,625 explicitly identified as interest accrued at NW Natural's full rate of return. In addition, SFAS 87 expense already compensates NW Natural for interest costs of approximately $77,333,755. Accordingly, through NW Natural's amortization proposal it would recover approximately $98,270,380 in accrued interest, which is more than its overall amortization proposal. This may be seen in Table 6, below:

TABLE 6
Total Amount of Interest Recovered Through PBA

	SFAS 87 Interest				Additional	Total
Year	Interest	O&M%	OR%	OR Share	PBA Interest	Interest
2011	16,784,849	66.7%	90.2%	10,098,336	234,378	10,332,714
2012	16,052,036	67.1%	90.5%	9,747,679	903,997	10,651,676
2013	15,271,527	66.4%	90.2%	9,146,545	1,576,811	10,723,356
2014	16,971,714	65.6%	90.2%	10,042,367	2,249,908	12,292,275
2015	17,115,645	64.4%	90.0%	9,920,228	2,965,951	12,886,179
2016	17,115,408	64.4%	90.2%	9,942,135	3,780,615	13,722,750
2017	16,870,615	63.5%	89.8%	9,620,131	4,579,476	14,199,607
2018	15,762,594	63.2%	88.5%	8,816,334	4,645,489	13,461,823
				77,333,755	20,936,625	98,270,380

Q. WHAT DO YOU RECOMMEND WITH RESPECT TO THESE INTEREST AMOUNTS?

A. Since the PBA failed, and did not reverse as required by the UM 1475 Stipulation, I recommend that, in no case should interest be recoverable from ratepayers beyond the interest already included in SFAS 87 expense. The account ran away, and one of the reasons it ran away, is due to the compounding interest calculation NW Natural was performing.

Accordingly, providing NW Natural with such significant financial returns in connection with a balancing account mechanism that failed due factors within the utility's control is untenable. Further, NW Natural's proposal vastly overstates interest because it includes the interest embedded in SFAS 87 expense in addition to interest accrued on the account balance.

j. Summary

Q. BASED ON YOUR REVIEW, WHAT HAVE YOU CONCLUDED WITH RESPECT TO THE PENSION BALANCING ACCOUNT?

A. Based on the terms of the UM 1475 stipulation, NW Natural is not entitled to amortize any excess pension expenses incurred with respect to the PBA. If the Commission is to conclude that some customer sharing is required, however, NW Natural's request for nearly $79,861,289 is wholly unreasonable. Customers should bear only a portion of the PBA balances after taking into account the adjustments described in my testimony, including the impact of reduced contributions to the pension plan, NW Natural's decision to de-risk the pension plan, and the double counting of interest expenses.

III. INTERIM PERIOD TAX REFORM SAVINGS

Q. WHAT IS NW NATURAL'S PROPOSAL WITH RESPECT TO THE INTERIM PERIOD TAX REFORM SAVINGS?

A. NW Natural's proposal and calculation with respect to the Interim Period tax reform savings was detailed in Exhibit NW Natural/2901. In that exhibit, NW Natural proposed a *with* and *without* method for calculating the impact of the Interim Period deferral. Based on that calculation, NW Natural calculated $4,991,000 of tax expense savings over the ten-month Interim Period. Grossed up to NW Natural's revenue requirement, this amount equates to $6,800,000.

Q. DO YOU HAVE ANY CONCERNS WITH THIS CALCULATION?

A. In general, I support a revenue requirement methodology that determines the amount of revenue attributable to tax expenses, and determining the Interim Period impact of the Tax Cuts and Jobs Act ("TCJA") from that perspective. Under the revenue requirement approach, the goal is to determine the amount of revenues necessary to produce the same rate of return, as if the TCJA not been enacted.

NW Natural's approach simply recalculates the expense incurred in the Interim Period at the lower tax rate to determine the savings amount. This is not appropriate because the actual expense is influenced by a number of non-normal factors that were not considered when setting rates. The *with* and *without* method does not answer the question of what NW Natural's revenues would have been, if the effects of the TCJA had been incorporated into rates as of January 1, 2018.

Notwithstanding, in Docket UM 1920, AWEC recently stipulated to an Interim Period tax reform calculation that relies on the *with and without* method for PGE. While I continue to believe the *with and without* method is not the best nor most accurate method, AWEC is willing to accept NW Natural's calculation of the Interim Period tax deferral using the *with and without* method with two adjustments which are necessary to make the treatment consistent between NW Natural and PGE.

Q. HOW IS NW NATURAL'S CALCULATION DIFFERENT FROM PGE'S?

A. The Interim Period tax savings calculation does not consider any provision for protected or unprotected EDFIT amortized in the Interim Period. As can be noted in Order 18459 in Docket UM 1920, protected and unprotected EDFIT amortization was passed through the

Interim Period deferral account for PGE.[28] NW Natural's calculation, however, does not provide for these amounts.

Q. WHAT DO YOU RECOMMEND?

A. I recommend that both of these EDFIT items be considered in NW Natural's Interim Period deferral calculation. Specifically, I recommend: (1) that protected EDFIT amortization of $2,719,166[29] be considered in the Interim Period deferral calculation; and (2) that unprotected EDFIT amortization of $6,700,000 be include in the Interim Period deferral calculation.[30] After including these amortization amounts, the total Interim Period deferral AWEC supports is $16,207,166, relative to the $6,788,000 included in NW Natural's Phase II testimony.

Q. WHY DID NW NATURAL PROPOSE TO EXCLUDE THOSE AMOUNTS?

A. NW Natural views the normalization requirements of the TCJA to be more of a "speed limit," rather than a strict requirement. Under NW Natural's interpretation, it could withhold refund protected EDFIT amounts recognized in the Interim Period using the Average Rate Assumption Methodology ("ARAM"), so long as it does not refund the monies more rapidly that calculated under the ARAM.

Q. DO YOU AGREE WITH THIS INTERPRETATION?

A. No. NW Natural may be splitting hairs with its interpretation of the TCJA normalization requirements. Ultimately, if the ARAM is to be used, the amortization schedule should follow the ARAM. NW Natural offers no compelling reason to return those monies more slowly than calculated using the ARAM, and for that reason, there is no valid reason to withhold the

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28 See UM 1920, Order 18 459, Appendix A at 10 (the footnote clarifies that unprotected EDFIT was included in the line titled "Net Effect of Other Tax Act Changes").

29 See Exhibit NW Natural-Staff-CUB/201. Calculated by prorating $3,263,000 protected EDFIT amortization over 10 months.

30 Id.

Interim Period ARAM amortization. Even if it were permissible to withhold those monies under the TCJA normalization requirements, that does not mean that it is appropriate in this case.

Further with respect to the unprotected EDFIT amounts, NW Natural has acknowledged that $6,700,000 is due to customers for that category of TCJA savings. NW Natural was willing to return this amount, but only if it was used to offset the PBA balance. Since the PBA balance is a separate issue, with a number of complicating factors, AWEC believes it is appropriate to pass through the Interim Period deferral calculation as PGE has done.

Q. WHAT RATE SPREAD SHOULD BE USED FOR THE INTERIM PERIOD DEFERRAL?

A. Because theses tax savings items relate primarily to rate base, and are unrelated to variable gas costs, it is most appropriate to refund the amounts on an equal percent of margin basis, consistent with the rate spread approved in Phase I of this docket. AWEC does not object to returning the amounts due solely to sales customers through a separate schedule. This rate spread is also consistent with the treatment for PGE. In UM 1920, parties agreed to spread the Interim Period deferral on "an equal percentage basis using the applicable schedule's forecasted revenues at current prices excluding net variable power costs," the electric equivalent of equal percent of margin.

Q. DOES THIS CONCLUDE YOUR PHASE II REBUTTAL TESTIMONY?

A. Yes.

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.	)
	)

EXHIBIT 701

TO THE

REBUTTAL TESTIMONY OF BRADLEY G. MULLINS

ON BEHALF OF

ALLIANCE OF WESTERN ENERGY CONSUMERS

December 12, 2018

NW Natural®

Rates & Regulatory Affairs
UG 344
2017 General Rate Revision
Data Request Response

Request No.: UG 344 AWEC (fka NWIGU) DR 65
65. For the accounting periods 2010 through 2018, please provide all actuarial reports and accounting workpapers necessary to support the FAS 87 pension expense amount. For 2018, please provide the information through the most recent month available. In the response please identify where in the supporting reports and workpapers that the annual FAS 87 expense can be found. Please also affirm that the amounts correspond to the FAS 87 expenses provided in response to AWEC data request 64, and if not, please explain why not.

Response:

See Confidential UG 344 AWEC 65 Attachments 1 through 10 for actuarial reports. See Confidential UG 344 AWEC 65 Attachment 11 for a summary of report files and the FAS 87 expense disclosure location within each report. All actuarial reports were prepared by certified actuaries engaged by NW Natural. Amounts reported in NW Natural's actuarial valuation reports correspond to FAS 87 expenses provided in response to AWEC data request 64.

NW Natural®

Rates & Regulatory Affairs
UG 344
2017 General Rate Revision
Data Request Response

Request No.: UG 344 AWEC (fka NWIGU) DR 66
66. Please provide a schedule of actual monthly pension plan contributions for each period beginning January 2011 through October 2018.

Response:

See attached Confidential UG 344 AWEC DR 66 Attachment 1.

NW Natural Gas Company

Pension Contribution Analysis 2011 -2018

	Plan Years							
Calendar Dates	2011PY	2012PY	2013PY	2014PY	2015PY	2016PY	2017PY	2018PY
10/14/2011	1,000,000	-	-	-	-	-	-	-
1/13/2012	2,800,000	-	-	-	-	-	-	-
3/30/2012	11,000,000	-	-	-	-	-	-	-
4/13/2012	4,600,000	-	-	-	-	-	-	-
7/13/2012	4,500,000	-	-	-	-	-	-	-
9/14/2012	600,000		-	-	-	-	-	-
1/15/2013	-	1,400,000	-	-	-	-	-	-
4/15/2013	-	-	2,800,000	-	-	-	-	-
7/15/2013	-	-	2,800,000	-	-	-	-	-
9/13/2013	-	1,900,000	-	-	-	-	-	-
10/15/2013	-	-	2,800,000	-	-	-	-	-
1/2/2014	-	-	2,800,000	-	-	-	-	-
4/15/2014	-	-	-	3,200,000	-	-	-	-
7/1/2014	-	-	-	3,200,000	-	-	-	-
9/15/2014	-	-	1,300,000	-	-	-	-	-
1/15/2015	-	-	-	2,630,000	-	-	-	-
4/15/2015	-	-	-	-	3,180,000	-	-	-
7/15/2015	-	-	-	-	3,180,000	-	-	-
9/15/2015	-	-	-	2,790,000	-	-	-	-
10/15/2015	-	-	-	-	2,340,000	-	-	-
1/15/2016	-	-	-	-	2,900,000	-	-	-
4/15/2016	-	-	-	-	-	3,220,000	-	-
7/15/2016	-	-	-	-	-	3,220,000	-	-
9/15/2016	-	-	-	-	1,910,000	-	-	-
10/14/2016	-	-	-	-	-	3,220,000	-	-
1/13/2017	-	-	-	-	-	3,220,000	-	-
4/13/2017	-	-	-	-	-	-	4,030,000	-
7/14/2017	-	-	-	-	-	-	4,030,000	-
9/15/2017	-	-	-	-	-	4,120,000	-	-
10/13/2017	-	-	-	-	-	-	4,030,000	-
1/12/2018	-	-	-	-	-	-	1,720,000	-
4/13/2018	-	-	-	-	-	-	-	3,850,000
7/13/2018	-	-	-	-	-	-	-	3,850,000
9/14/2018	-	-	-	-	-	-	2,270,000	-
10/15/2018	-	-	-	-	-	-	-	3,850,000
Summary	2011	2012	2013	2014	2015	2016	2017	2018
Plan Year Totals	**24,500,000**	**3,300,000**	**12,500,000**	**11,820,000**	**13,510,000**	**17,000,000**	**16,080,000**	**13,040,000**
Calendar Year Totals	**20,245,000**	**23,500,000**	**11,700,000**	**10,500,000**	**14,120,000**	**14,470,000**	**19,430,000**	**15,540,000**

Notes:

Calendar Year 2011 total includes amounts allocated to plan years 2010 ($19,245,000) and 2011 ($1,000,000).

Plan Year 2018 total includes amounts allocated to Calendar year 2019 ($1,490,000).

NW Natural®

Rates & Regulatory Affairs
UG 344
2017 General Rate Revision
Data Request Response

Request No.: UG 344 AWEC (fka NWIGU) DR 67
67. For each accounting period beginning in 2011 through 2018, please provide the calculation of the pension balancing account balance in excel format, with all links intact. To the extent that the file contains any hard-coded numbers or numbers that link to an external spreadsheet, please identify the source of the numbers and provide a copy of the source document. For 2018 please provide the calculation through the most recent month available.

Response:

Please see Confidential UG 344 AWEC 67 Attachments 1 through 9. Confidential Attachment 1 contains Excel copies of 2017 and 2018 monthly entry amounts and year-end Excel calculations for 2011 through 2016. Note that NW Natural has not yet located the journal entry for July 2016, but will continue to look to identify the information and supplement this data response when it is located. Due to its size, Attachment 1 along with Confidential attachments 8-9 are being submitted on CD via mail. Prior to 2017, only year-end copies of the PBA calculation were retained in Excel. Attachments 2 through 9 contain PDF copies of each month's calculation, review, and approval for 2011 through October 2018.

Please note that documents in 2013 through 2018 also contain a calculation of SEC deferred interest. GAAP and SEC reporting requirements dictate that the equity portion of regulatory interest cannot be recognized in net income under GAAP until collection of its associated regulatory balance begins. The deferral is for SEC reporting purposes only and has no impact on the pension balancing account for regulatory and ratemaking purposes.

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Rates & Regulatory Affairs
UG 344
2017 General Rate Revision
Data Request Response

Request No.: UG 344 AWEC (fka NWIGU) DR 68

68. Please identify and describe all internal controls in place over the time period 2011 through 2018 with respect to the monthly and annual accounting accruals for the pension balancing account, including identification of the individuals responsible for preparing the accrual amount and those responsible for reviewing it. If a written policy was in place, please provide a copy of the policy document in its entirety.

Response:

In accordance with the Oregon PUC Order 11-051 in Docket UM1475, which approved the implementation of the pension balancing account ("PBA"), the Company has developed processes and internal controls over recording pension expense and the respective balancing amounts for years 2011-2018.

The Order approved the implementation of the PBA as of January 1, 2011 to include all Oregon allocated FAS 87 pension expense net of amounts recovered in rates.

The annual amount recovered in rates for 2011-2018 is $3,796,055. For purposes of determining the required monthly entry to the PBA, 1/12 of the annual amount recovered in rates is used. The actual amount to be compared against the amount recovered in rates will be determined by calculating the Oregon allocated, O&M-specific, FAS 87 pension expense for the month. Therefore, the key consideration is the actual annual FAS 87 pension expense itself. The Company has a number of processes and controls surrounding the annual FAS 87 pension expense as described below. The FAS 87 pension expense itself is determined by a third party actuary and provided to the Company management in the form of an Annual Valuation Report as of 12/31 of each year. During 2011-2018 the accrual amount has been prepared by an Accounting Analyst III and reviewed by the Financial Reporting and Technical Accounting Manager. Additionally, the pension balancing account activity is subject to general internal controls that cover journal entry accuracy and appropriateness, reconciliation of the accounts, and management review of all regulatory account balances during monthly meetings

In conjunction with the Company's internal control program, the pension accounting, including the PBA, is subject to certain key internal controls as documented in the attached flowchart and summarized below. The pension expense controls, including responsible party, are as follows:

- SOX Key Control 5000.PR.RTM.01.07 – Management's Valuation of Pension Assets – The Mid-Office prepares an annual Pension Assets Valuation Memo (in accordance with ASC 820) to document management's considerations of the reasonableness of the valuation of pension plan assets and related disclosures in accordance with ASC 820.

  Control and certifying process owner: Financial Risk Senior Manager
  Certifying officer: Controller/Chief Accounting Officer

- SOX Key Control 5000.PR.RTM.01.03 - Post Retirement and ESRIP Expense – Review Pension Valuation – To ensure validity of actuarial results, the Mid-Office ensures the reasonableness of custodian pension assets including reconciling year-end 12/31 custody statements from the current custodian (Wells Fargo) to the Investment Consultant's (AON/Fidelity) performance valuation report to ensure that fair value amounts reported in the financial statements are accurate and reasonable.

  Control owner: Financial Risk Analyst III
  Certifying process owner: Financial Risk Senior Manager
  Certifying officer: Controller/Chief Accounting Officer

- SOX Key Control 5000.PR.RTM.01.04/5 – Pension Assumptions Reasonableness – To ensure the validity of actuarial results major data inputs used by the actuary are reviewed for reasonableness.

  Control and certifying process owner: Financial Reporting Manager
  Certifying officer: Controller/Chief Accounting Officer

- SOX Key Control 5000.PR.RTM.01.01 – Post Retirement and ESRIP Expense – Pension Data (from NWN) Reconciliation and Review – To ensure accuracy, completeness and validity of employee pension data sent to the actuary and used in the calculation of the 1) Company Pension expense, liability and respective balancing amount and the 2) Company Post-Retirement Benefit expense, liability, and balancing amount an annual review and reconciliation of the prior year's pension data provided to Pension Administrator (Fidelity) is completed by HR Financial Analyst 3.

  Control owner: Financial Risk Analyst III
  Certifying process owner: Financial Risk Senior Manager
  Certifying officer: Controller/Chief Accounting Officer

- SOX Key Control 5000.PR.RTM.01.02 – Post Retirement and ESRIP Expense – Reconciliation and Review of data used by Fidelity – To ensure accuracy, completeness and validity of employee pension data used in the calculation of the 1) Company Pension Liability, Expense, and balancing amount, and the 2) Company Post-Retirement Benefit Liability, expense, and balancing amount an annual review and reconciliation of pension data received from Pension Administrator (AON/Fidelity) is completed by the HR Financial Analyst 3 after obtaining the completed FAS 87 calculation.

Control owner: HR Financial Analyst III
Certifying process owner: HR Director
Certifying officer: Chief HR and Diversity Officer

- SOX Key Control 5000.PR.RTM.01.06 – Accounting for Pensions – To ensure the accuracy and completeness of the monthly pension journal entries an annual review of the Actuary Report and Accounting entries is performed.

  Control owner: Accounting Analyst III
  Certifying process owner: Financial Reporting Manager
  Certifying officer: Controller/Chief Accounting Officer

Please see UG 344 AWEC DR 68 Attachment 1 for a flow chart relating to this response.

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Request No.: UG 344 AWEC (fka NWIGU) DR 69
69. For each month, beginning January 2011 through October 2018, please provide the chain of emails, and any other associated approval documentation, approving the pension balancing account accrual and balance.

Response:

We record pension expense monthly and as a result, make a journal entry to the pension balancing account monthly. That entry is made in our general ledger (SAP) and is prepared and reviewed in SAP. In addition, we do account reconciliations for all general ledger accounts in a separate system (Blackline). All account reconciliations are also prepared and reviewed.

There are no emails or other correspondence outside of SAP or Blackline with respect to the approval of amounts recorded to the balancing account. As described in UG 344 AWEC DR 68, we have internal controls over financial reporting that apply to the recording of pension expense and include a control over the preparation and review of journal entries and account reconciliations.

The accounting workpapers supporting the journal entries and account reconciliations for pension expense entries are included in Confidential UG 344 AWEC DR 67 Attachments 2 through 9.

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Request No.: UG 344 AWEC (fka NWIGU) DR 70
70. Please provide any accounting documentation or emails transmitted over the period 2011 through the November 2018 that discuss, or consider, application of a valuation allowance to the pension balancing account regulatory asset balance.

Response:

We are not aware of any such documentation or correspondence. It is and has always been the Company's belief that this account would be fully recovered through the balancing of negative FAS 87 expense, or through collection/refund of remaining balances in the account, allowing for the full recovery of FAS 87 expense for the period in which the balancing account was in existence.

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Request No.: UG 344 AWEC (fka NWIGU) DR 73
73. Please identify each and every data request to which NW Natural responded in Docket UM 1475 and provide a copy of NW Natural's response, including all attachments and confidential information, to said data requests.

Response:

NW Natural responded to DRs 1-10 from Staff and DR 1 from CUB. Please see UG 344 AWEC Attachments 1-3 which contains NW Natural's non confidential responses and attachments to Staff DRs 1-10 in UM 1475. Please see Confidential AWEC DR 73 Attachments 4-7 for NW Natural's Confidential responses and attachments to Staff DRs 1-10 in UM 1475. Please see UG 344 AWEC Attachment 8 for NWN response to CUB DR 1 in UM 1475.

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Request No.: UG 344 AWEC (fka NWIGU) DR 74
74. Please provide copies of all workpapers associated with NW Natural's September 20, 2010 Direct Testimony filing in Docket UM 1475.

Response:

NW Natural did not submit work papers in association with its September 20, 2010 Direct Testimony filing in Docket UM 1475 and has not retained any such documentation in compliance with our records retention policy.

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Data Request Response

Request No.: UG 344 AWEC (fka NWIGU) DR 75
75. Please identify any accounting changes that the NW Natural has made with respect to calculating its FAS 87 pension expense over the period beginning 2011 through 2018.
75. Please identify any accounting changes that the NW Natural has made with respect to calculating its FAS 87 pension expense over the period beginning 2011 through 2018.

Response:

There have been no changes to the methods for calculating FAS 87 pension expense for the period from 2011 through 2018.

The Company did adopt FASB ASU 2017-07 “Improving the Presentation of Net Periodic Pension Cost and Net Periodic Post Retirement Benefit Cost” on January 1, 2018. This did not impact the calculation of FAS 87 expense, rather only changed how the company presents pension expense in its financial statements. As of January 1, 2018, the Company now disaggregates current service cost from the other components of net periodic benefit cost and presents it with other current compensation costs for related employees in the income statement and presents the other components elsewhere in the income statement and outside of income from operations.

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Request No.: UG 344 AWEC (fka NWIGU) DR 76

76. Reference Docket UM 1475, NWN/200, Feltz/10:25-11:19: Please provide workpapers supporting each of the numerical figures included the referenced section of testimony, including the confidential information.

Response:

NW Natural did not submit work papers in association with this filing and has not retained any such documentation in compliance with our records retention policy.

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Request No.: UG 344 AWEC (fka NWIGU) DR 77
77. Please provide a copy of the exhibits to the Direct Testimony of Mr. Feltz in Docket UM 1475 (i.e. NWN/201 - NWN 206 Confidential). Please provide the exhibits in Excel format with all links and formulas intact. Please include both confidential and non-confidential exhibits.

Response:

Please see UG 344 AWEC DR 77 Attachment 1 and Confidential UG 344 AWEC DR 77 Attachment 2.

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Data Request Response

Request No.: UG 344 AWEC (fka NWIGU) DR 78

78. Please describe the accounting treatment that NW Natural intends to use on its financial statements for the pension balancing account accrual beginning November 1, 2018, following the Commission's October 26, 2018 order in this docket. In the response, please state whether NW Natural intends to accrue any additional amounts (including interest) to the pension balancing following the effective date of the Commission's October 26, 2018 decision.

Response:

Beginning with pension expense recorded for the month of November 2018, the Company will recognize the full Oregon allocated expense after amounts capitalized in the Company's statement of comprehensive income. No additional FAS 87 pension expense will be recorded to the balancing account. The only entry made to the balancing account will be a monthly entry to record interest, at the Company's authorized rate of return, accruing on the account.

THIS EXHIBIT IS DESIGNATED CONFIDENTIAL BY GENERAL PROTECTIVE ORDER

NO. 18-002

THIS EXHIBIT IS DESIGNATED CONFIDENTIAL BY GENERAL PROTECTIVE ORDER

NO. 18-002

THIS EXHIBIT IS DESIGNATED CONFIDENTIAL BY GENERAL PROTECTIVE ORDER

NO. 18-002

CERTIFICATE OF SERVICE

I HEREBY CERTIFY that I have this day served the foregoing document upon all parties listed below electronically. All parties waived paper service, and service was completed by uploading both Confidential and Non-Confidential versions to Huddle.

Public Utility Commission of Oregon **(C)** Attn: Filing Center PO Box 1088 Salem, OR 97308-1088	STEPHANIE S ANDRUS **(C)(HC)** BUSINESS ACTIVITIES SECTION 1162 COURT ST NE SALEM OR 97301-4096 stephanie.andrus@state.or.us
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Dated in Portland, Oregon this 12th day of December 2018.

Respectfully submitted,

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Of Attorneys for Alliance of Western Energy Consumers