

Rates and Regulatory Affairs
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August 29, 2008

NWN Advice No. OPUC 08-6

VIA ELECTRONIC FILING

Public Utility Commission of Oregon
550 Capitol Street, N.E., Suite 215
P.O. Box 2148
Salem, Oregon 97308-2148

Attn: Filing Center

**Re: Schedule P: Purchased Gas Cost Adjustments
Interim 2008-09 Purchased Gas Cost Adjustment Mechanism**

Northwest Natural Gas Company, dba NW Natural (“NW Natural” or the “Company”) files herewith the following revisions to its Tariff P.U.C Or. 24, stated to become effective with service on and after November 1, 2008:

Eighth Revision of P-5,
Schedule P,
“Purchased Gas Cost Adjustments (continued)”.

The purpose of this filing is to revise Schedule P to make an interim modification to Provision 3 of the section titled “Calculation of Monthly Gas Costs for Deferral Purposes” that pertains to the treatment of accounting for differences between Actual Commodity Cost and Embedded Commodity Cost for the 2008-2009 PGA Year (the “Sharing Mechanism”). Accordingly, this filing requests that the Public Utility Commission of Oregon (the “Commission”) approve a temporary change in the sharing percentages applicable to NW Natural’s Sharing Mechanism in the current PGA from 67/33 to 90/10. This change would be adopted on an interim basis, for one year only, pending the Commission’s final decision in UM 1286. **We request that the Commission rule on this tariff filing only in the event the Commission is not able to issue its final order in UM 1286 in time for the 2008-2009 PGA year.** The reasons for and details of the proposed revision are set forth in this letter.

Background

Oregon Administrative Rule 860-022-0070 governs the procedures and standards for reviewing natural gas utility rates in the context of PGAs. The purpose of the PGA is “to permit each natural gas utility to adjust revenue annually to reflect actual increases or decreases in gas costs.”¹ The PGA mechanism currently applicable to NW Natural was established by the Commission in 1989. This current PGA includes a sharing component that allows the LDCs and customers to share in savings or costs resulting from differences in the embedded and actual costs of gas.² Under NW Natural’s tariff, differences between actual gas costs and WACOG are shared with customers on a 67/33 percent basis.³ Thus, customers receive 67% of the benefit when the difference between the two costs is positive, and bear 67% of the costs when the difference is negative.⁴

In November 2006 Commission Staff (“Staff”) recommended that the Commission open an investigation to review and modify as appropriate the PGA mechanism used by Oregon’s three LDCs. In doing so, Staff specifically recognized changes in the market that resulted in less stability and more risk for the LDCs.⁵ The Commission accepted Staff’s proposal, and opened UM 1286.⁶

On August 24, 2007, NW Natural filed Advice No. 07-6 requesting an interim revision to its PGA incentive mechanism pending the outcome of UM 1286.⁷ In that filing, NW Natural noted that higher and more volatile gas prices had left the company exposed to a disproportionate amount of risk, and suggested a change to the mechanism was necessary to realign the interests of customers and shareholders.⁸ At the Public Meeting, the Commission rejected the Company’s request, citing its expectation that the changes to the PGA adopted in UM 1286 would be in place in time for the 2008-2009 PGA year.

¹ Commission Order No. 03-198, entered 4/3/03; see also OAR 860-022-0070(1) (purpose of the rule is to ensure that an LDC’s PGA earnings are not excessive prior to passing through prudently incurred base gas cost changes in rates through a fair and efficient mechanism).

² Schedule P-5, Provision 3.

³ *Id.*

⁴ NWN Advice No. OPUC 06-13A, UG 174 Replacement Filing: Purchased Gas Cost and Technical Rate Adjustments (LSN Application Enclosed), filed 10/4/06, Sheet P-4 (“A debit or credit shall be made equal to 67% of the difference between the Actual Commodity Cost and the Embedded Commodity Cost.”).

⁵ Commission Staff Report for Public Meeting, Nov 21, 2006, at p. 1.

⁶ *Id.*

⁷ NWN Advice No. OPUC 07-6, Schedule P: Purchased Gas Cost Adjustments Interim 2007-08 Purchased Gas Cost Adjustment Mechanism, filed 8/24/07, Sheet P-5.

⁸ OPUC 07-6/NWN/100/Miller.

In its Opening Comments filed in UM 1286, NW Natural explained how changes in market conditions and reductions in hedging have resulted in increased financial risk to the Company.⁹ NW Natural also explained how, given this increased risk, the 67/33 percent sharing levels in the Company's current PGA are out of alignment with the financial risk experienced by its customers and therefore need to be adjusted. Specifically, the Company proposed that the Commission alter its sharing percentages in the Sharing Mechanism from 67/33 to 80/20.¹⁰

After several settlement conferences, the Company joined the other LDCs, Staff and Northwest Industrial Gas Users ("NWIGU") in Stipulating to a number of adjustments to the PGA.¹¹ The parties to docket UM 1286 requested a Commission decision on the matter by October 1, 2008—a date which was selected to allow any changes adopted by the Commission to the current PGA to be incorporated in the LDCs filings for the 2008-2009 PGA year. However, the parties were aware at the time that they were not guaranteed to have a decision in place by that date. NW Natural is filing this request to address the possibility that the Commission may not reach a decision in UM 1286 by October 1.

NW Natural's Proposal

In its Opening and Reply Comments in UM 1286, the Company explained that it believes that the current PGA is basically sound, but that the current sharing percentages applicable to NW Natural are no longer sustainable.¹² For that reason, the Company proposed that the Commission retain the current PGA mechanism with one change—altering the sharing of differences between Embedded Commodity Cost and Actual Commodity Costs from 67/33 to 80/20. In the year since NW Natural filed its first "interim mechanism" in Advice 07-6, gas prices and market volatility has continued to grow. More than ever, it is crucial that the level of risk between customers and shareholders is addressed and reapportioned, so that customer and shareholder interests remain in alignment.¹³

In the process of negotiating a Stipulation to UM 1286, NW Natural agreed to additional changes to the current PGA mechanism, which it believes improve upon the existing mechanism. However, these changes are more extensive and are therefore not suited for an interim change to be adopted on a 60-day schedule. For these reasons, in the event the Commission does not issue its decision in UM 1286 by October 1, 2008, NW proposes that the Commission alter, on

⁹ NWN Opening Comments, UM 1286 (Dec. 4, 2007) at 1-2, 11-14, 19-21.

¹⁰ *Id.* at 14-21.

¹¹ Stipulation by Joint Parties and Joint Direct Testimony of Ken Zimmerman, Brian Hirschhorn, Katherine Barnard, Alex Miller, and Paula Pyron, UM 1286 (May 2, 2008).

¹³ NWN Opening Comments, UM 1286 (Dec. 4, 2007); NWN Reply Comments, UM 1286 (Jan. 28, 2008).

an interim basis, NW Natural's sharing levels to 90/10. In recognition of this lower sharing percentage, NW Natural proposes that the Commission make a change to NW Natural's earnings threshold from 300 basis points of ROE to 215 basis points of ROE.

Conclusion

NW Natural is committed to cost-effective, sustainable pricing and has been actively involved in working with the UM 1286 parties to come to agreement on a long-term solution. However, given the current volatile gas markets, the Company must address the potential that a decision will not be reached in the UM 1286 docket. Should this occur, the Commission should grant the Company's request for an interim change to its PGA sharing levels and earnings threshold.

The Company requests that the tariff sheets filed herewith be permitted to become effective with service on and after November 1, 2008.

Copies of this letter and the filing made herewith are available in the Company's main office in Oregon and on its website at www.nwnatural.com.

Please address correspondence on this matter to me at Inara.Scott@nwnatural.com, with copies to the following:

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Sincerely,

NW NATURAL

/s/ Inara K. Scott

Inara K. Scott, Manager
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NORTHWEST NATURAL GAS COMPANY

P.U.C. Or. 24

Eighth Revision of Sheet P-5
Cancels Seventh Revision of Sheet P-5

SCHEDULE P PURCHASED GAS COST ADJUSTMENTS (continued)

CALCULATION OF MONTHLY GAS COSTS FOR DEFERRAL PURPOSES (continued):

2. A debit or credit entry shall be made equal to 100% of any monthly difference between Embedded Non-Commodity Costs and Monthly Seasonalized Fixed Charges. The monthly Seasonalized Fixed Charges for the period November 1, 2008 through November 30, 2009 are:

November 2008	\$8,469,845
December 2008	\$11,639,785
January 2009	\$11,456,425
February	\$9,539,265
March	\$8,306,343
April	\$6,032,131
May	\$4,111,401
June	\$2,783,618
July	\$2,327,295
August	\$2,352,433
September	\$2,634,257
October	\$5,142,612
November	<u>\$8,373,598</u>
ANNUAL TOTAL	\$74,699,163

3. For the 2008-2009 PGA Year commencing November 1, 2008 and ending October 31, 2009, a debit or credit entry shall be made equal to 90% of the difference between the Actual Commodity Cost and the Embedded Commodity Cost. A debit or credit entry will also be made equal to 100% of the difference between storage withdrawals priced at the actual book inventory rate as of October 31 prior to the PGA year and storage withdrawals priced at the inventory rate used in the PGA filing. Changes to the PGA mechanism that arise out of the Commission decision in Docket UM 1286 shall be effective with the 2009-2010 PGA Year. (C)
(C)
4. Monthly differentials shall be deemed to be positive if actual costs exceed embedded costs and to be negative if actual costs fall below embedded costs.
5. The cost differential entries shall be debited to the sub-accounts of Account 191 if positive, and credited to the sub-accounts of Account 191 if negative.
6. Interest – Beginning November 1, 2007, the Company shall compute interest on existing deferred balances on a monthly basis using the interest rate(s) approved by the Commission. (N)
(N)

(continue to Sheet P-6)

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