

**BEFORE THE
WASHINGTON UTILITIES AND TRANSPORTATION COMMISSION**

WASHINGTON UTILITIES AND
TRANSPORTATION COMMISSION

Complainant,

v.

NORTHWEST NATURAL GAS
COMPANY,

Respondent.

DOCKET UG-18____

NORTHWEST NATURAL GAS COMPANY

Direct Testimony of Jorge O. Moncayo

OPERATIONS & MAINTENANCE

Exh. JOM-1T

December 31, 2018

DIRECT TESTIMONY OF JORGE O. MONCAYO

Table of Contents

	<u>Page</u>
I. Introduction and Summary.....	2
II. Operations and Maintenance Costs.....	3
1. O&M Test Year Costs.....	3
2. O&M Management and Performance.....	8

1
2
3
4
5
6
7
8
9
10
11
12
13
14
15
16
17
18
19
20
21
22
23

I. INTRODUCTION AND SUMMARY

Q. Please state your name and position with Northwest Natural Gas Company (“NW Natural” or “the Company”).

A. My name is Jorge Moncayo. I am the Budget and Financial Planning Director at NW Natural. I am responsible for producing the annual operations and maintenance (O&M) budget, the capital expenditures (capex) budget, and the income statement budget. I also manage the department that develops short-term and long-term financial forecasts for senior management and supports the organization with financial modeling and analysis.

Q. Please summarize your educational background and business experience.

A. I have Bachelor’s degrees in Business Administration and Accounting from Universidad Catolica, Ecuador and a Masters of Business Administration and a Master of Science in Industrial Engineering from Oregon State University. Since joining NW Natural in 2003 as a market research analyst, I have held positions in Consumer Research and Analysis, Operations Support Services, Business Analysis and Finance. I have been in my current position since 2013.

Q. Please provide a summary of your testimony.

A. My testimony explains how NW Natural calculated the O&M expense included in its revenue requirement in this case. I start by providing an overview of how the Company adjusted Test Year O&M to arrive at its rate case request. I then provide background and context on how NW Natural has controlled its O&M expense over time, and how that O&M expense compares with O&M expense included in the rates of other gas utilities.

1 **II. OPERATIONS AND MAINTENANCE COSTS**

2 **Q. What is the Washington-allocated O&M expense included in the Company's**
3 **revenue requirement in this case?**

4 A. The Washington-allocated expense included in the revenue requirement in this case is
5 \$18.06 million.

6 **1. O&M Test Year Costs**

7 **Q. How did the Company calculate the Test Year O&M cost?**

8 A. NW Natural started with the O&M expenses incurred by the Company in the historical
9 Test Year—October 1, 2017 through September 30, 2018. This total Company amount
10 was then adjusted for amounts that represent O&M for which the Company is not
11 seeking cost recovery in this case—which are discussed below. After this adjustment,
12 the Test Year O&M expense is then state allocated.

13 In addition, the Company made certain restating and pro forma adjustments to
14 better reflect the expense the Company will incur during the rate effective period. As
15 will be discussed in more detail below, these Washington allocated restating and pro
16 forma adjustments are for bargaining unit (BU) and non-bargaining unit (NBU) wage
17 and salary increases, adjustments to reflect end of Test Year FTE counts, benefit and
18 incentive compensation adjustments, an additional director fee, rate case expense, and
19 two restating adjustments for clearing and claims. These adjustments are discussed in
20 more detail below.

21 **Q. Please describe the O&M expenses that were removed from the O&M Test Year.**

22 A. The historical Test Year O&M was adjusted to remove expenses which the Company
23 is not seeking cost recovery in this case. Specifically, the Company removed all

1 expenses attributable to non-utility operations, the Supplemental Executive Retirement
2 Plan (SERP), Executive Supplemental Retirement Income Plan (ESRIP), FERC 912
3 (Marketing) and FERC 913 (Promotional advertising) expenses, and all other non-
4 recoverable costs.

5 **Q. Please describe the adjustment for pay increases mentioned above.**

6 A. Bargaining Unit (BU) employee payroll costs were escalated for contractually-
7 determined wage increases, which are scheduled to take effect on December 1st, 2018.
8 The Company also assumes an additional 0.5 percent for promotions and movements
9 from entry rate to experienced rate as described in the Collective Bargaining
10 Agreement. The current Collective Bargaining Agreement runs through November 30,
11 2019, and is included as an exhibit to the direct testimony of Melinda B. Rogers as Exh.
12 MBR-4. The pro forma pay increase adjustment for BU wage increases assumes that
13 similar pay increase and promotions will occur in the next Collective Bargaining
14 Agreement beginning December 1, 2019.

15 In addition, NBU employee payroll costs were escalated to reflect the known
16 increase that will take effect on March 1, 2019. This increase is to be 3.25 percent. The
17 Company also assumes an additional 0.75 percent for promotions that have historically
18 occurred throughout the year. The pay increases described above are discussed in
19 greater detail in the testimony of Ms. Rogers.

20 **Q. How many FTEs are being requested?**

21 A. The Company adjusted payroll to reflect the Washington allocated expense for the
22 number of FTEs at the end of the Test Year (1,150.6).

23 **Q. Does the O&M payroll expense include any non-regulated FTEs in the Test Year?**

1 A. No, the Test Year O&M requested during the Test Year excludes any and all payroll
2 related to non-regulated activity. This non-regulated activity includes any time spent
3 by employees on affiliate activities. In addition, a pro forma adjustment was made for
4 indirect “common costs” for departments that perform administrative and general
5 functions for the benefit of all operating companies and affiliates. The direct testimony
6 of Amanda Faulk describes the Company’s cost allocation methodologies for services
7 provided to affiliates, which are explained in detail in the Company’s Cost Allocation
8 Manual. The Cost Allocation Manual is included with Ms. Faulk’s testimony as Exh.
9 AEF-2.

10 **Q. Please describe the benefits adjustments.**

11 A. The Company has made two adjustments for both Health & Life Insurance and pension
12 expense. The Health & Life Insurance pro forma uses 2019 Health & Life Insurance
13 costs. This adjustment reflects known costs changes as well as employee service
14 elections completed in November 2018. The pension expense adjustment reflects
15 pension expense related to the 12 months of 2018 as compared to the Test Year which
16 included expenses for nine months of 2018 and the last three months of 2017.

17 **Q. Please describe the incentive compensation adjustment.**

18 A. The Company used a three-year historical average of annual incentive compensation
19 paid, and made an adjustment to the Test Year to reflect this average amount. This
20 adjustment reduced the Test Year O&M expense. The direct testimony of Melinda
21 Rogers found in Exh. MBR-1T provides more information on the incentive
22 compensation and wages and benefit expense included in the case.

23 **Q. Does the Test Year reflect changes to pension accounting?**

1 A. Yes. Effective January 1, 2018, NW Natural has adopted Accounting Standards Update
2 (ASU) 2017-07, modifying the presentation of net periodic cost and net periodic
3 postretirement benefit cost, and also limiting the portion of defined benefit (DB)
4 pension costs and other postretirement benefits (OPEB) costs that are eligible for
5 capitalization.

6 **Q. Please explain the mechanics of the changes in pension accounting.**

7 A. Since ASU 2017-07 was implemented in December 2017, only the service cost
8 component of DB and OPEB expense are recognized through payroll overheads and
9 are capitalized according to the O&M/capital mix of the employees' salaries and wages.
10 All other cost components of DB and OPEB are recognized as expenses. For DB and
11 OPEB, the new accounting standard increases the amount of expense as compared to
12 the former accounting guidelines.

13 **Q. Please describe the additional director fee adjustment.**

14 A. As part of the Commission's order authorizing NW Natural to reorganize to form a
15 holding company structure,¹ the Company was required to have at least one director of
16 NW Natural that is independent of the Northwest Natural Holding Company board of
17 directors. In other words, NW Natural was required to have at least one director that
18 sits on the gas utility's board of directors, but does not also sit on the holding company's
19 board of directors. This independent director was appointed on October 2, 2018, after
20 the historical Test Year period. A pro forma adjustment was made to include the
21 Washington allocated portion of this additional director to the Test Year O&M.

¹ *In the Matter of Nw. Natural Gas Co.'s Application for Approval of Corporate Reorganization to Create a Holding Co.*, Docket UG-170094, Order 1 (Dec. 29, 2017) and Errata to Order 01 (Mar. 3, 2018).

1 **Q. Did the Company make any other adjustments to Test Year O&M?**

2 A. Yes, the Company made three final restating adjustments. The first restating
3 adjustment is to include outside service expense related to this rate case. The expense
4 amount reflects one third of the total expense expected in this case to reflect an average
5 rate case frequency.

6 The second restating adjustment is a claims adjustment for “ordinary” and
7 “extraordinary” claims. An ordinary claim involves a claim for damages related to
8 Human Resources issues, operating issues, and automobile claims. Extraordinary
9 claims are all other claims. The adjustment for ordinary claims reflects the actual claims
10 paid during the Test Year. In addition, we have adjusted the Test Year extraordinary
11 claims by using a 3-year average of extraordinary claims paid versus the Test Year
12 expense.

13 Lastly, a clearing restating adjustment was made to adjust for the difference
14 between actual costs and what was expensed during the Test Year. These three
15 adjustments can be found in the revenue requirement model Exh. KSM-4.

16 **Q. How did NW Natural allocate O&M expenses to Washington?**

17 A. The Test Year expenses were allocated to O&M FERC accounts. The Company then
18 applied the Washington allocation factors to each FERC account to calculate
19 Washington-allocated O&M. The Washington allocation factors were also applied to
20 each adjustment to calculate the Washington-allocated O&M amount.

21 **Q. Please summarize these O&M adjustments.**

22 A. The below table summarizes all the adjustments made.

	<u>(\$000's)</u>
O&M Test Year Results	\$17,639
<u>Adjustments (Restating)</u>	
Annual Incentive Adj.	(\$161)
Marketing & Promotional Adj.	(\$288)
Claims Adj.	\$35
Rate Case Adj.	\$138
Clearing Adj.	\$16
Total Restating Adj.	<u>(\$259)</u>
<u>Adjustments (Pro Forma)</u>	
Payroll Adj.	\$539
Payroll Overhead Adj.	\$157
Holdco Allocation Adj.	(\$37)
Director Fee Adj.	\$19
Total Pro Forma Adj.	<u>\$678</u>
Test Year O&M Expenses	<u><u>\$18,058</u></u>

1 **2. O&M Cost Management and Performance**

2 **Q. How long has it been since NW Natural applied for a general rate increase in**
3 **Washington?**

4 A. NW Natural last requested a general rate increase in March 2008, with new rates
5 effective January 1, 2009. Since that time, the Company has not sought a rate increase
6 in great part due to management of costs in its O&M budget.

7 **Q. Please describe the protocols the Company has in place to control its O&M**
8 **budget.**

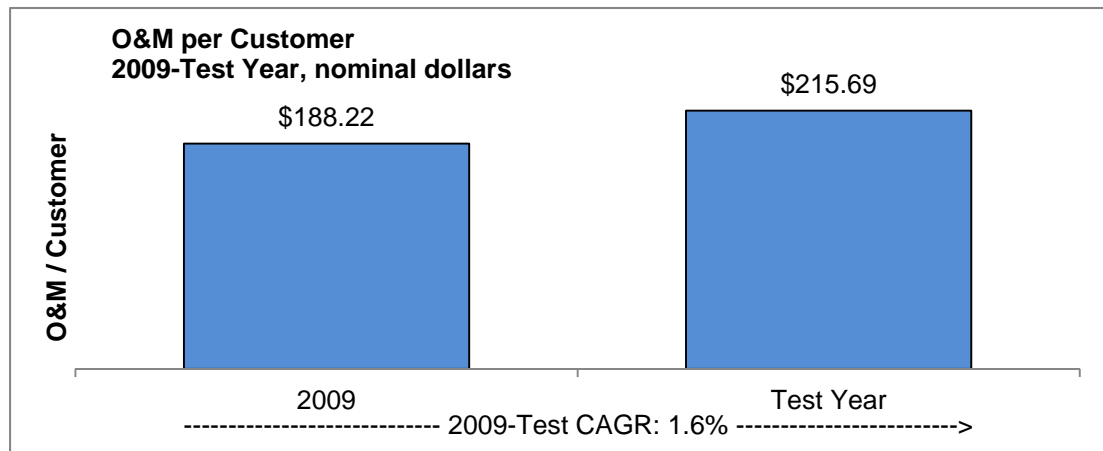
9 A. Under the direction of the CFO and CEO, my department engages in an annual
10 budgeting and financial planning process, through which we determine and manage to
11 a Company-wide budget. This budget is informed by individual departmental needs,
12 customer and operational requirements, and an ongoing focus on controlling costs.
13 Throughout the year, we review and provide actuals-to-budget reports to each

1 department, and engage with departments on their spending levels. We also require
2 that each department justify their budget and explain any significant departures from
3 budgeted amounts.

4 **Q. Please provide your view of NW Natural's O&M levels, and the amounts of O&M**
5 **reflected in the Test Year.**

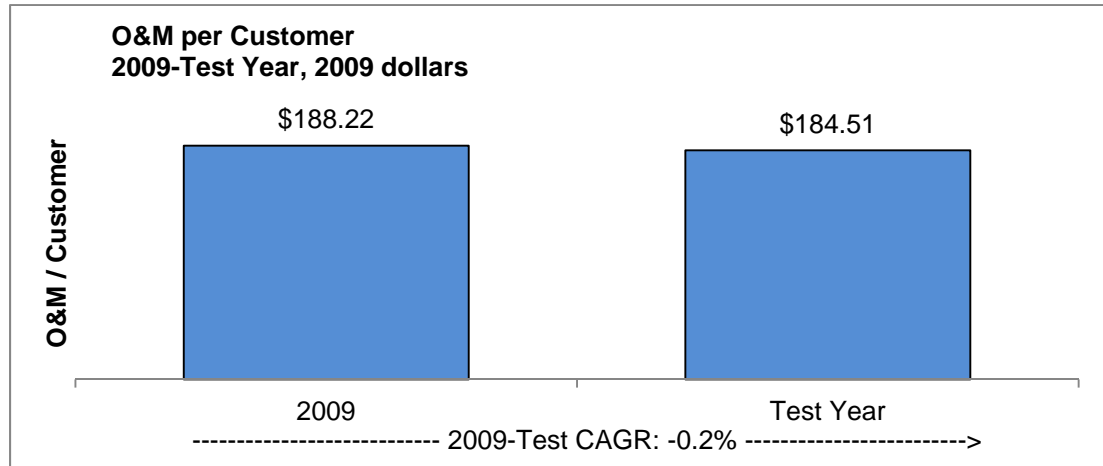
6 A. NW Natural's O&M levels have grown at a reasonable rate over the past decade,
7 reflecting good cost management practices within the Company. As is true with most
8 companies, much of the pressure on our O&M expense levels comes from inflation.
9 O&M expenses also naturally rise with the addition of new customers over time.

10 The chart below shows O&M expense per customer (system-wide, including
11 uncollectible, excluding environmental remediation expenses and charges, in nominal
12 dollars) over time.



13 As shown above, O&M expenses per customer have increased from \$188.22 in 2009
14 to \$215.69 for the Test Year, which reflects a compound annual growth rate (CAGR)
15 of 1.6 percent from 2009.

1 Expressed in constant 2009 dollars, calculated using the All Urban Consumer
2 CPI index (CPI-U)², the Test Year O&M expense per customer is \$184.51, a CAGR of
3 -0.2 percent from 2009.

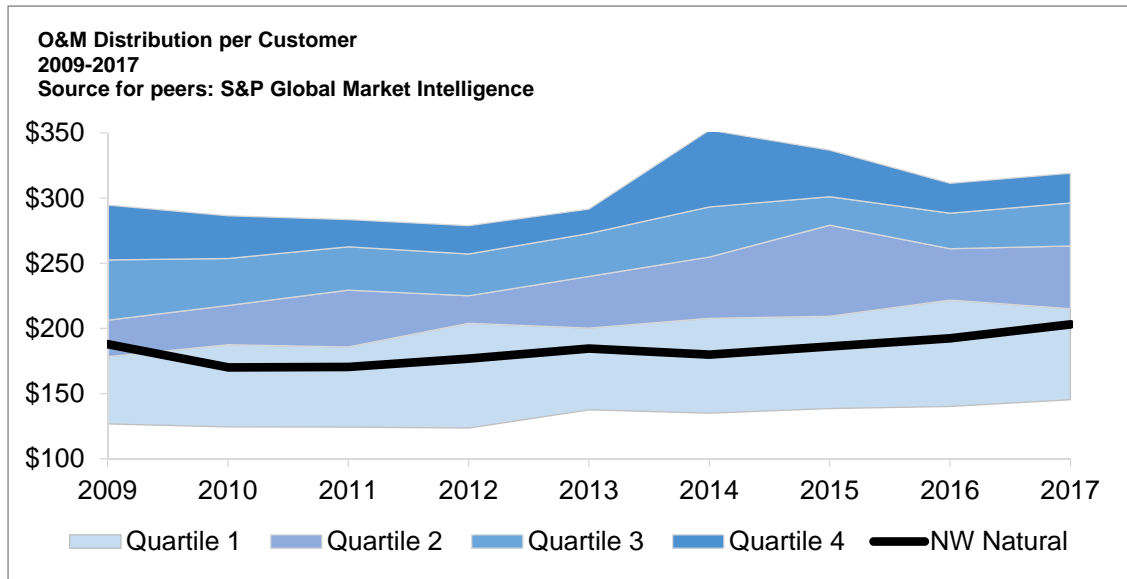


4 As depicted above, this means that NW Natural's O&M expense levels have been
5 essentially flat for the last decade, after taking into account inflation and customer
6 growth. This reflects good cost management practices at the Company and helps
7 explain why the Company has been able to successfully avoid the need for a rate case
8 for so many years. As shown by the above graphs, NW Natural has been effectively
9 managing its O&M levels to stabilize rates as much as possible for customers.

10 **Q. Have you compared the Company's O&M expense per customer to O&M**
11 **expenses per customer at peer utilities?**

² U.S. Department of Labor, Bureau of Labor Statistics, Consumer Price Index for September 2018 (available at <https://www.bls.gov/cpi/tables/supplemental-files/historical-cpi-u-201809.pdf>).

1 A. Yes. The following chart provides a comparison of the Company's O&M per customer
2 expense, relative to a panel of similar gas utilities. For comparability purposes, only
3 total distribution expenses are used for the peer group and NW Natural.



4 The chart shows that NW Natural is consistently a top performer in O&M
5 expense management. The panel uses customer counts and distribution costs for those
6 companies with FERC Form 2 information available in S&P Global Intelligence, and
7 includes the following companies: Atmos, Avista, Cascade, National Fuel, New Jersey
8 National Gas, South Jersey Gas, and Washington Gas and Light. Again, this
9 information shows that NW Natural performs very well in managing its O&M expense
10 levels to keep rates as low as reasonably possible for customers.

11 **Q. Does this conclude your testimony?**

12 A. Yes, it does.