BEFORE THE WASHINGTON
UTILITIES AND TRANSPORTATION COMMISSION

WASHINGTON UTILITIES AND TRANSPORTATION COMMISSION, Complainant, v. NORTHWEST NATURAL GAS, COMPANY Respondent.	DOCKET NO. UG-181053

POST-HEARING BRIEF OF PUBLIC COUNSEL

September 12, 2019

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ATTORNEY GENERAL OF WASHINGTON
Public Counsel
800 5th Ave., Suite 2000
Seattle, WA 98104-3188
(206) 464-7744

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ATTORNEY GENERAL OF WASHINGTON
Public Counsel
800 5th Ave., Suite 2000
Seattle, WA 98104-3188
(206) 464-7744

I. INTRODUCTION

1. Public Counsel respectfully requests the Washington Utilities and Transportation Commission ("WUTC" or the "Commission") to reject the Decoupling Agreement, filed by Northwest Natural Gas Company d/b/a NW Natural ("NW Natural" or the "Company"), the Staff of the WUTC ("Staff"), Alliance of Western Energy Consumers ("AWEC"), and The Energy Project ("TEP"), jointly referred to as the "Parties." The revenue-per-customer methodology proposed by the Decoupling Agreement is an inappropriate approach to decoupling for NW Natural at this time due to the significant growth expected by the Company over the next six years. Under revenue-per-customer decoupling, this growth, coupled to the increased energy efficiency of new homes and appliances, is likely to result in cost-shifting and unjust rate increases for ratepayers. NW Natural and Staff support this result by relying on the incorrect premise that decoupling should guarantee recovery of the incremental costs of serving new customers between rate cases, reduce the frequency of rate cases, and address regulatory lag. Decoupling, however, is not intended to address these issues and is poorly designed for that purpose.

2. For these reasons, Public Counsel opposes the Decoupling Agreement and requests that the Commission reject revenue-per-customer decoupling for NW Natural at this time. If the Commission decides to authorize a decoupling mechanism for NW Natural, Public Counsel recommends that it implement rate class decoupling instead.

3. This brief primarily addresses the contested decoupling issue, but Public Counsel also requests that the Commission approve the All-Party Agreement without modifications or

conditions. The All-Party Agreement is in the public interest and represents a reasonable outcome of all issues in the rate case except for the contested decoupling issue.

II. LEGAL STANDARD

4. The legal standard that the Commission must apply in its review of any settlement agreement is set forth in WAC 480-07-750(2), which provides that "[t]he commission will approve a settlement if it is lawful, supported by an appropriate record, and consistent with the public interest in light of all the information available to the commission."[1]

III. THE COMMISSION SHOULD REJECT THE DECOUPLING AGREEMENT BECAUSE REVENUE-PER-CUSTOMER DECOUPLING IS NOT APPROPRIATE FOR A UTILITY EXPERIENCING SIGNIFICANT CUSTOMER GROWTH

5. The Decoupling Agreement establishes a full decoupling mechanism for NW Natural for a five-year period. As discussed by the Commission's *Report and Policy Statement on Regulatory Mechanisms, Including Decoupling, to Encourage Utilities to Meet or Exceed Their Conservation Targets* ("Policy Statement"),[2] decoupling is intended to remove barriers to utilities acquiring and encouraging all cost-effective conservation.[3] Decoupling is intended to sever the link between a utility's sales and the revenue the utility collects from customers.[4] When properly designed, full decoupling shields the utility from reductions in revenue due to conservation efforts and other factors that affect customer usage such as weather. Any additional revenues from increases in customer usage or the addition of new customers can be returned to

[1] WAC 480-07-750(2).

[2] *In the Matter of the Wash. Utils. and Transp. Comm'n's Investigation into Energy Conservation Incentives*, Docket U-100522 (Nov. 4, 2010).

[3] Policy Statement at 8.

[4] Response Testimony of Scott J. Rubin, Exh. SJR-1T at 4:1-2.

ratepayers.[5] Under revenue-per-customer decoupling, the utility collects revenue requirement on a per customer basis according to a baseline usage per customer established in a rate case.[6] Rate increases due to the decoupling mechanism are intended to be balanced by the public interest in encouraging energy conservation and the potential to return revenue to customers.

6. NW Natural, however, expects to grow significantly over the five years of the proposed decoupling program. Additionally, those new customers will use less natural gas than existing customers. Revenue-per-customer decoupling under such circumstances alters the balance of equity such that a policy that should balance the interests of utility shareholders and customers will now be tilted squarely in favor of the utility.

A. NW Natural is expected to grow significantly and new customers will use less gas on average than existing customers.

7. NW Natural currently provides service to 84,000 customers in Southwest Washington.[7] The Company forecasts that it will add more than 20,000 residential customers over the next six years, increasing its customer base by more than 25 percent.[8] These new customers are expected to use less natural gas than existing customers because new housing stock is much more energy efficient than the existing housing stock.[9]

8. Public Counsel witness, Scott Rubin, reviewed a variety of data sources, including the Company's own data on customer usage, which all agree that new residential customers use significantly less gas than existing customers use.[10] Data from the U.S. Department of Energy's

[5] *See* Policy Statement at 6:9 for a discussion about lost margin; *see also Id.* at 7:11 for a discussion about found margin.

[6] Revised Rebuttal Testimony of Kyle T. Walker, Exh. KTW-4Tr at 18:3-6.

[7] Direct Testimony of David H. Anderson, Exh. DHA-1T at 3:7-11.

[8] Rubin, Exh. SJR-1T at 18:1-4.

[9] *Id.* at 8:12-14.

[10] *Id.* at 9:1 to 10:5; *Id.* at 13:1 to 17:6.

Residential Energy Consumption Survey (RECS) showed that new homes in 2015 were likely to use 95 fewer therms per year, or 14 percent, than homes constructed in 2010.[11] Similarly, the Company's data showed that customers from 2010 to 2017 used an average of almost 175 fewer therms per year, approximately 25 percent less, than customers in older homes.[12] Mr. Rubin concluded that advances in space heating efficiency, water heating efficiency, water efficiency of appliances that use hot water, differences in insulation, and smart thermostats are just some of the innovations that have made new construction much more energy efficient than the average existing home.[13]

B. Revenue-per-customer decoupling for NW Natural will result in unfair cost-shifting and unreasonable rate increases.

9. Under revenue-per-customer decoupling, existing customers set the baseline usage. New customers who are added to the system after the baseline is set are likely to use less gas than expected by that baseline, and will therefore result in a shortfall. Using the RECS data discussed, above, the shortfall from new customers would be 95 therms per year, or a 14 percent reduction in usage. If revenue-per-customer decoupling is implemented, customers would be required to make up the so-called "shortfall" through increased rates since the utility would be allowed to collect revenue up to the expected, baseline amount per customer.

10. Mr. Rubin illustrated this effect in his testimony using a hypothetical utility residential class with $1 million in annual revenues from gas sales (excluding the cost of gas), 5,000 customers, three million therms of sales, and $200 in sales revenue per customer.[14] Under the

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[11] *Id.* at 10:3-5.
[12] *Id.* at 15:3-9.
[13] *Id.* at 8:12-18; *see also Id.* at 16:3 to 17:2.
[14] Rubin, Exh. SJR-1T at 10:11 to 11:8.

hypothetical example, the utility was assumed to experience three percent customer growth, adding 150 new customers, and each new customer was assumed to use 14 percent less gas than existing customers, or 516 therms per new customer.[15] The following table shows what would happen to this residential class under per-customer decoupling, assuming existing customers still use three million therms of gas.[16]

	Customers	Therms	Sales Revenues
Existing customers	5,000	3,000,000	$ 1,000,000
New customers	150	77,400	25,797
Total	5,150	3,077,400	$ 1,025,797
Average		597.6	$199.18

11. As explained by Mr. Rubin, adding new, more efficient, customers to the system reduces the average sales per customer from 600 therms to 597.6 therms, and the average revenue per customer declines from $200 to $199.18. Under the revenue-per-customer model, the assumed $200 in sales per customer (the baseline) would dictate a total revenue of $1,030,000, but actual usage would result in a total sales revenue of $1,025,797. So, even though existing customers used exactly the same amount of gas and the hypothetical utility's revenues <u>increased</u> by $25,797, revenue-per-customer decoupling would show that the utility experienced a "shortfall" of $0.82 per customer, or approximately $4,200, requiring a 0.4 percent increase in the revenues collected from these customers. In other words, the "shortfall" would result in a rate increase.[17]

12. A 0.4 percent increase does not seem particularly troubling on its own, but when this type of growth continues for years without resetting the baseline, the impacts can be significant. Mr. Rubin's testimony showed that, if the same utility were to continue for five years at the same

[15] *Id.*
[16] *Id.* at 11.
[17] *Id.*

ATTORNEY GENERAL OF WASHINGTON
Public Counsel
800 5th Ave., Suite 2000
Seattle, WA 98104-3188
(206) 464-7744

level of growth without resetting the baseline, while new customers continued to use less gas than existing customers, the results would look as follows:[18]

	Customers	Therms	Sales Revenues
Existing customers	5,000	3,000,000	$ 1,000,000
New customers	750	387,000	128,987
Total	5,750	3,387,000	$ 1,128,987
Average		589.0	$196.35

13. After five years, the average sales per customer would decline from the initial 600 therms to 589 therms, and the average revenue per customer would decline from $200 to $196.35. Thus, even though the hypothetical utility's revenues increased by $128,987, revenue-per-customer decoupling would show that the utility experienced a shortfall of $3.65 per customer, or approximately $21,000, requiring an almost two percent increase in the revenues collected from customers. This rate increase would occur even though the utility's revenues are almost 13 percent higher than the baseline ($1,128,987 compared to $1,000,000) due to increased sales to the new customers.[19] Moreover, in this example, existing customers' gas usage is exactly equal to the baseline projection, and the hypothetical situation does not include any reductions in usage by existing customers over the five years. The alleged "shortfall" is solely a result of customer growth.

14. These examples show how implementing revenue-per-customer decoupling on a utility that is growing significantly will result in ratepayers paying increased rates to guarantee a level of revenues from new customers that those customers are not likely to generate. The Decoupling Agreement will implement revenue-per-customer decoupling on NW Natural under these exact

[18] *Id.*
[19] *Id.* at 12:1-9.

ATTORNEY GENERAL OF WASHINGTON
Public Counsel
800 5th Ave., Suite 2000
Seattle, WA 98104-3188
(206) 464-7744

circumstances. NW Natural expects to add more than 20,000 customers by 2024. These new customers are likely to use less gas than existing customers due to more energy efficient housing and appliances. Through the decoupling mechanism, NW Natural will require existing customers to guarantee a level of consumption from every new customer that they are not likely to reach. The Company will increase rates to collect revenue for a fictitious reduction in usage that is actually the result of the addition of new customers who use less energy to begin with.

15. Within five years, the Company's gas sales are projected to grow by 10 million therms annually.[20] NW Natural's distribution revenues from those gas sales would increase by more than $4.6 million annually.[21] Additionally, the Company would receive another $1.9 million in additional customer-charge revenues from the 20,000 new customers it plans to add by 2024.[22] Thus, the Company would receive additional revenues from customers of $6.5 million compared to its baseline projection in this case. Yet, revenue-per-customer decoupling would produce a fictitious "shortfall" of revenues in 2024 of $1.37 million. That is, an additional increase of $1.37 million on top of the $6.5 million in new revenues already received by the Company. These results are unjust and unreasonable. As Mr. Rubin testified, "to say that we need to give the utility an incentive to reduce consumption at the same time they're projecting that their consumption will increase by nine or ten million therms a year over the next five years seems … inconsistent."[23]

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[20] Walker, Exh. KTW-11r (Total Residential Usage of 62.35 million therms in 2024 compared to 52.47 million therms in 2018).

[21] 10 million therms x distribution rate of $0.46523 per therm [Walker, Exh. KTW-7 at 5] = $4,652,300 per year.

[22] Walker, Exh. KTW-11r (Total Customer Count Forecast of 98,181 in 2024 compared to 77,357 in 2018). 20,000 new customers x $8.00 per month customer charge x 12 months = $1,920,000 in additional customer-charge revenues annually.

[23] Rubin, TR. 108:15-20.

16. Public Counsel's witness, Mr. Rubin, characterized the collection of additional revenue to make up for the artificial shortfall as a "windfall" for the Company.[24] NW Natural and Staff objected to the characterization of the excess revenue collected through revenue-per-customer decoupling as a windfall because the revenue will not fully compensate the utility for the costs to serve new customers,[25] suggesting that, to them, a windfall can only occur in the case where all costs are exceeded by decoupling revenues and there is some revenue left over to benefit the company. Regardless of what the additional revenues are called or how they will be ultimately used by the Company, the fact remains that rate increases to pay for a manufactured shortfall are neither fair, just, nor reasonable, as required by RCW 80.28.010, and the Decoupling Agreement should not be found to be in the public interest.

C. NW Natural acknowledges that revenue-per-customer decoupling can increase rates when new customers use less natural gas.

17. In its rebuttal testimony, the Company agreed with Public Counsel's arguments regarding cost-shifting associated with newer customers consuming less natural gas. The Company stated, "If new customers use less, the revenue-per-customer mechanism arguably would have surcharge pressure from these new customers in a normal weather scenario."[26] The Company attempted to minimize the impact of this acknowledgement by arguing that "the surcharge pressure is exactly the same as that from an existing customer choosing to add conservation measures,"[27] but this comparison is misleading.

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[24] *Id.* at 12:14-15; *see also, Id.* at 24:5-7.
[25] Rebuttal Testimony of Jing Liu, JL-5T at 7:3-8; Walker, Exh. KTW-4Tr at 3:14 to 4:2.
[26] Walker, Exh. KTW-4Tr at 23:12-15.
[27] *Id.*at 23:16-17.

18. From a very limited perspective, the two scenarios may appear exactly the same, since the Company will increase rates under both scenarios. But in the customer-growth scenario that is expected for NW Natural, the Company would receive $6.5 million in new revenues in just one year. To further increase rates because of some fictitious "shortfall" in per-customer usage makes no sense. In contrast, in a no-growth scenario, which no party expects to occur for this Company, increased rates through the operation of a decoupling mechanism would be due to actual, not fictional, reductions in per-customer-consumption.

19. Furthermore, from the perspective of a customer, the two scenarios are distinctly different. Increasing rates to account for the reduction in consumption from adding conservation measures, weather, or other factors impacting consumption is arguably decoupling functioning in the way it is intended. Implementing revenue-per-customer decoupling when the company is growing significantly and all new customers are highly likely to use less gas than existing customers essentially rigs the system to result in rate increases that are wholly beyond the control of existing customers and is grossly unfair.

20. NW Natural does not address the question of whether this surcharge pressure is fair and, instead, argues that the amount of cost-shifting is insignificant, "because, as proposed in the Decoupling Agreement, the surcharges are spread to all customers – including both new and existing customers."[28] Public Counsel acknowledges that the rate increases would be spread to all customers, but does not agree that the cost-shifting is insignificant. The Company's calculations show that, assuming new customers use 522 therms per year rather than the baseline of 678 therms per year and the baseline is not reset, by 2024, <u>revenue-per-customer decoupling</u>

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[28] *Id.* at 23.

alone would increase all residential customer total bills by 2.3 percent.[29] Looking only at the distribution portion of the bill (that is, excluding the cost of gas from the total bill), the increase would be closer to 3.5 percent.[30] Additionally, from 2019 to 2024, the Company would collect more than $4.3 million in revenue in excess of the base level of residential revenues due to revenue-per-customer decoupling.[31]

IV. DECOUPLING IS NOT INTENDED TO FULLY COMPENSATE A COMPANY FOR THE COST TO SERVE NEW CUSTOMERS, ADDRESS REGULATORY LAG, OR RATECASE FREQUENCY

21. As discussed in the Commission's Policy Statement, decoupling is intended to remove barriers to utilities encouraging all cost-effective conservation.[32] Throughout its analysis of different mechanisms to meet conservation targets, the Commission consistently considered the balance of equity between utility shareholders and ratepayers.[33] Not once did the Commission suggest that decoupling is intended to compensate a utility fully for the cost to serve new customers, alleviate regulatory lag, or reduce rate case frequency.

22. NW Natural and Staff, however, repeatedly indicate that they expect revenue-per-customer decoupling to address these issues. Staff unequivocally stated that one of the policy reasons supporting decoupling is the idea that existing customers should fully compensate the utility for the incremental cost of serving new customers between rate cases.[34] Staff also implies that part of the $24 million in additional revenue from revenue-per-customer decoupling

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[29] *Id.* at 24:4.

[30] Mr. Walker agreed that the typical bill without the cost of gas is approximately $33.80 per month. Walker, TR. 51:17-21. The estimated increase from revenue-per-customer decoupling in 2024 is $1.17 per month. Walker, Exh. KTW-11r (Monthly Decoupling Impact on Customer Bills). $1.17 ÷ $33.80 = 3.46%.

[31] Walker, Exh. KTW-11r, sum of "Decoupling Balance" from 2019 to 2024 ($107,841 + $322,574 + $577,457 + $836,319 + $1,101,812 + $1,374,472 = $4,330,475).

[32] Policy Statement at 8.

[33] *See generally* Policy Statement.

[34] Liu, TR. 69:22 to 70:4.

calculated by Mr. Rubin would represent revenue that the Commission might authorize for the Company in iterative rate cases, and believes that allowing a utility to retain the excess revenues "is a positive step forward in addressing regulatory lag and rate case fatigue."[35]

23. To bolster their positions, Staff and NW Natural devote significant pages of testimony trying to undermine Mr. Rubin's statement that he does not agree that the Company's cost of adding new customers justifies the level of increased revenues that would occur under revenue-per-customer decoupling. Public Counsel raised questions regarding NW Natural's and Staff's cost calculations in Mr. Rubin's testimony and during the evidentiary hearing, and the Company has not sufficiently justified all of its cost estimates. In particular, the Company has not adequately demonstrated that there are incremental operations, maintenance, or customer-service expenses from adding a new customer.[36]

24. However, regardless of the exact quantification of the cost to serve new customers or how much of the costs are paid for by the excess revenues collected from decoupling, the primary point is that decoupling is not intended to fully compensate a utility for customer growth, utility operations, or capital expenditures between rate cases.

25. To the extent a utility cannot collect enough revenue to meet its needs, the solution is not to implement an unfair decoupling methodology that unreasonably increases rates for fictional "shortfalls". The company can always file a rate case to adjust its rates in a fair and comprehensive manner.

26. Similarly, decoupling is not intended to address regulatory lag or rate case fatigue. Those are complex issues that decoupling is not designed to address in a manner that balances utility

[35] Liu, Exh. JL-5Tr at 21:16-20.
[36] *See* Walker, TR. 52:17 to 66:13.

ATTORNEY GENERAL OF WASHINGTON
Public Counsel
800 5th Ave., Suite 2000
Seattle, WA 98104-3188
(206) 464-7744

and consumer interests. Further, Public Counsel notes that there is an ongoing rulemaking, Docket U-180907, regarding the adequacy of the current regulatory framework where Parties can address these issues.

27. In summary, revenue-per-customer decoupling for NW Natural will likely result in unreasonable rate increases. Allowing the Company to implement the mechanism as a shortcut for dealing with other regulatory policy problems would be grossly unfair to NW Natural's customers.

V. IF THE COMMISSION DECIDES TO IMPLEMENT A DECOUPLING MECHANISM FOR NW NATURAL, THE DECOUPLING SHOULD OCCUR ON A RATE CLASS BASIS

28. In light of NW Natural's significant growth projections and the expected lower gas consumption from new customers, revenue-per-customer decoupling would not result in just and reasonable rates for customers. Rather than revenue-per-customer decoupling, if the Commission determines it is in the public interest to implement some form of decoupling for NW Natural, Public Counsel recommends that the decoupling occur on a total-sales basis for the Residential class as a whole. Under rate class decoupling, the class totals become the baseline without regard to the number of customers added or lost, and utility revenues from gas sales would be reconciled to maintain that baseline.[37]

29. During high-growth periods, rate class decoupling would result in lower rates to existing customers. This provides existing customers with some of the expected benefits from system growth – spreading fixed costs over a large customer base, thereby reducing the cost per customer to support that investment.[38] Public Counsel recommends a form of rate class

[37] Rubin, Exh. SJR-1T at 8:4-11.
[38] *Id.* at 26:7-9.

decoupling that does not reconcile the customer charge revenues from new customers. This would permit the Company to keep additional revenues from the customer charge.

30. Public Counsel's recommended form of rate class decoupling would appropriately share the benefits of growth between the Company and customers.[39] Rate class decoupling would provide the Company with a return of and on its incremental investment and provide customers with credit for the backbone and common costs fully included in existing customer's rates, but used by new customers.[40]

VI. THE COMMISSION SHOULD APPROVE THE ALL-PARTY JOINT SETTLEMENT AGREEMENT

31. Public Counsel also requests that the Commission approve the All-Party Agreement without modifications or conditions. The All-Party Agreement is the result of negotiations between all parties in this proceeding, and as such, represents a reasonable compromise among the parties' positions on all issues except for the decoupling issue discussed, above. Public Counsel believes that the resulting revenue requirement and other terms of the Settlement are fair, just, reasonable, and sufficient, and in the public interest.

VII. CONCLUSION

32. The revenue-per-customer methodology proposed by the Decoupling Agreement is an inappropriate approach to decoupling for NW Natural at this time due to the significant growth expected by the Company over the next six years. Under revenue-per-customer decoupling, this growth, coupled to the increased energy efficiency of new homes and appliances, is likely to result in cost-shifting and unjust rate increases for ratepayers. NW Natural and Staff support this

[39] *Id.* at 26:13-15.
[40] *Id.*

ATTORNEY GENERAL OF WASHINGTON
Public Counsel
800 5th Ave., Suite 2000
Seattle, WA 98104-3188
(206) 464-7744

result by relying on the incorrect premise that decoupling should guarantee recovery of the incremental costs of serving new customers between rate cases, reduce the frequency of rate cases, and address regulatory lag. Decoupling, however, is not intended to address these issues and it is poorly designed for that purpose.

33. The Commission must regulate in the public interest[41] and has a duty to ensure all rates are fair, just, reasonable, and sufficient.[42] NW Natural and Staff rely heavily upon revenue-per-customer decoupling to ensure sufficient rates for the Company but appear to do so at the expense of rates that are also fair, just, and reasonable for customers. In light of all the information set forth above, the Decoupling Agreement should not be found to be in the public interest. Public Counsel respectfully requests the Commission to reject revenue-per-customer decoupling for NW Natural at this time. If the Commission determines it is in the public interest to implement some form of decoupling for NW Natural, Public Counsel recommends that it implement rate class decoupling instead.

DATED this 12th day of September 2019.

ROBERT W. FERGUSON
Attorney General

/S/ Nina Suetake
NINA SUETAKE, WSBA No. 53574
Assistant Attorney General
Public Counsel Unit
Email: Nina.Suetake@ATG.WA.GOV
Phone: (206) 389-2055

[41] RCW 80.01.040(2).
[42] RCW 80.28.010(1).