Agenda Date: August 30, 2016
Item Number: D3

Docket: UG-160967
Company: Cascade Natural Gas Corporation

Staff: Betty Erdahl, Regulatory Analyst

Recommendation

Take no action, allowing the proposed revisions to Tariff WN U-3 to go into effect on September 1, 2016, by operation of law.

Discussion

On July 29, 2016, Cascade Natural Gas Corporation (Cascade or company) filed a revision to the company's line extension policy to increase the allowance therefore decreasing the cost to a customer to extend a natural gas line to their home or business. The commission has identified expanding natural gas service as a positive goal to reduce carbon emmissions compared to other carbon fuel resources. Increasing the line extension allowace reduces the customer's initial cost barrier for homeowners and businesses to convert to natural gas.

Cascade's filing is similar to Avista's filing in Docket UG-152394 to change the method of calculating the line extension allowance provided to the customer. Cascade's filing differs from Avista's plan in that Cascade does not propose: 1) to offer the use of any excess allowance to customers for the purchase of space and water-heating equipment when the cost of the line extension is less than the maximum value of the line extension allowance; and 2) a request for a limited waiver of WAC 480-90-223(1) concerning utility advertising (later withdrawn by Avista).

Change in Allowance Methodology

Cascade, like Avista, proposes adopting a new methodology for the calculation of line extension allowances. This methodology is known as the Perpetual Net Present Value method. The methodology is reviewed in a paper titled "Line Extensions for Natural Gas: Regulatory Considerations," by Ken Costello of the National Regulatory Research Institute.[1] Staff supports using this methodology because it produces the maximum line extension allowance that is economically-viable for the company.

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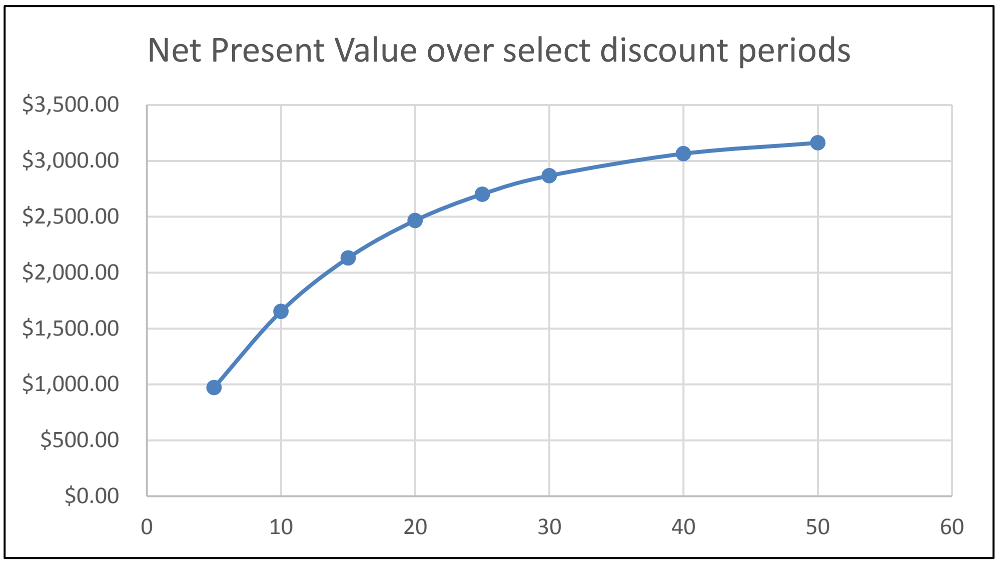
[1] *Line Extensions for Natural Gas: Regulatory Considerations,* by Ken Costello. February 2013, National Regulatory Research Institute. See page 20.

A benefit of this methodology is that it is simple to calculate and uses figures that are established by the commission during a rate case. The anticipated revenue from an average customer[2] is divided by the authorized rate of return. The resulting figure is the net present value of an average customer's presence on the system, and therefore the financial break-even point at which the company and existing customers are indifferent to a new customer's presence. The illustration below demonstrates net present values under select discount periods. At 50 years, the net present value is found to be $3,161 – not significantly different than the $3255 proposed here.



Cascades's current line extension allowance methodology is more arbitrary in that each customer gets an allowance based on that customer's plan for gas appliances to estimate gas consumption. The current policy is also less generous. Under the current policy, an average Cascade line extension allowance is $572, 3.3 times the estimated annual margin, or the distribution charge times the therms that will be billed over a year based on the appliances that the customer plans to install. Residential customers connected under the existing line extension methodology contribute approximately $1,300 more to the utility than they cost to serve on an annual basis.

The new methodology offers a maximum fixed amount of $3,255 towards residential customer's cost to connect regardless of customer appliances. For line extensions that cost less than $3,255, the customer pays nothing. This more generous line extension allowance is a fair balance of sharing the fixed costs to expand the system between new customers and existing customers.

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[2] The anticipated revenue from the customer is found by summing the annual revenues from basic charges and the decoupled revenue per customer, after "backing out" the rate of return component embedded in those figures. The company earns a rate of return on the line extension when the line extension is added to rate base.

The residential allowance is a fixed amount which is consistent with the company's recently approved decoupling mechanism that recovers a specific amount of revenue per customer served.

Conclusion

Cascade's revised natural gas line extension allowance methodology allows the company to make natural gas service a more viable option to businesses and single-family residences in its service territory.

Recommendation

Take no action, allowing the proposed revisions to Tariff WN U-3 to go into effect on September 1, 2016, by operation of law.